

BEFORE THE  
SURFACE TRANSPORTATION BOARD

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Central Oregon & Pacific Railroad, Inc. -  
Coos Bay Rail Line

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) Finance Docket No. 35130  
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RESPONSE OF RAILAMERICA, INC. AND CENTRAL OREGON & PACIFIC  
RAILROAD, INC. TO ORDER TO SHOW CAUSE

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Dated: May 12, 2008

RailAmerica, Inc. (“RailAmerica”) and the Central Oregon & Pacific Railroad, Inc. (“CORP”) respectfully submit this Response to the Order served by the Board in the above-captioned proceeding on April 11, 2008 (“*Show Cause Order*”).<sup>1</sup> The *Show Cause Order* instructed CORP to show cause why the Board should not consider CORP’s September 21, 2007 embargo of its line between Coquille and Richardson, OR to be an unlawful abandonment and why CORP should not be required either to promptly repair the tunnels on the line and resume rail service or to seek abandonment authority. *Show Cause Order* at 1.<sup>2</sup>

As this Response demonstrates, CORP’s embargo of the Coos Bay Line was reasonable when instituted and has remained reasonable at all times. CORP embargoed the line in response to serious and well-documented safety concerns relating to the condition of three tunnels on the Coos Bay Line. Those safety concerns were based upon multiple timber lining failures, rock falls, and the actual collapse of one of the tunnels during previous repairs, as well as a detailed report by an expert geotechnical firm, Shannon & Wilson, Inc. CORP’s judgment that the condition of the tunnels warranted an immediate embargo of the line was ratified by the Federal Railroad Administration (“FRA”). Based upon its independent inspection of the tunnels just three weeks after the embargo was issued, FRA concluded that “[t]hese tunnels are hazardous to train traffic and maintenance operations.” *See* Exhibit 8 at 4. FRA concurred with Shannon &

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<sup>1</sup> RailAmerica, a non-carrier, voluntarily participates in this response to the Board’s *Show Cause Order*.

<sup>2</sup> CORP’s so-called “Coos Bay Line” consists of approximately 111 miles of CORP-owned trackage between MP 652.11 at Danebo, OR and MP 763.13 at Cordes, OR, and another 103 miles of rail lines located between MP 763.13 at Cordes, OR and MP 786.5 at Coquille, OR that CORP leases from Union Pacific Railroad Company (“UP”). The embargo at issue in this proceeding encompassed that portion of the Coos Bay Line between Coquille and Richardson, OR. For convenience, the Coquille – Richardson segment will be referred to hereinafter as the “Coos Bay Line.” A copy of the Embargo Notice issued by CORP on September 21, 2007 is set forth in Exhibit 7 to this Response.

Wilson's findings regarding the tunnel repairs required to restore the line to a safe operating condition. *Id.*

Seasonal weather conditions in Oregon since September 2007 have prevented CORP from commencing the tunnel repairs recommended by Shannon & Wilson. As the Shannon & Wilson report states, the onset of the rainy season in Oregon is accompanied by conditions under which attempting substantial tunnel repairs would have been both "impossible and hazardous." See Exhibit 6, September 21, 2007 Supplement at 2. These conditions increased the risk of tunnel instability if timber sets were removed or disturbed. For that reason, Shannon & Wilson advised CORP that "it may not be safe for much of the repair work to be undertaken until the drier months of next spring and summer." *Id.* (emphasis added).<sup>3</sup> Indeed, the Congressman representing one of the districts in which the Coos Bay Line is located acknowledged in recent testimony before the Board that the past winter in Oregon was one of the most severe in many years, and that undertaking tunnel repairs under the conditions existing even as of late April 2008 "would have been very difficult, if not impossible."<sup>4</sup> Moreover, the immediate repairs to the tunnels on the embargoed line recommended by Shannon & Wilson would require approximately four months to complete. Thus, even if weather conditions would otherwise have permitted tunnel repairs to commence as early as May 1, 2008, the line could not be reopened any earlier than September 2008. CORP so advised shippers and interested parties

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<sup>3</sup> According to the National Weather Service, "[t]he rainy season in western Oregon runs from October through May." See National Weather Service Forecast Office for Portland, OR, "Some of the Area's Rainstorms," available at <http://www.wrh.noaa.gov/pqr/paststorms/rain.php>. The winter of 2007-08 was predicted to be particularly rainy; in August 2007 the Oregon Climate Service predicted "western Oregon conditions to be somewhat cooler and wetter than average" during the winter of 2007-08. Oregon Climate Service, "Fall & Winter Forecast, 2007-2008," available at [http://www.ocs.oregonstate.edu/winter\\_07-08/forecast.html](http://www.ocs.oregonstate.edu/winter_07-08/forecast.html) (August 2007).

<sup>4</sup> See Ex Parte No. 677, *Common Carrier Obligation of Railroads*, April 24, 2008 Hearing Transcript at 21 (Testimony of Rep. DeFazio).

in November 2007. Thus, the embargo continues to be reasonable, because CORP could not practicably have completed repairs to the tunnels and reopened the Coos Bay Line under any circumstances until September 2008 at the earliest.

Finally, the investment required to complete the tunnel repairs necessary to reopen the Coos Bay Line cannot be economically justified. The Shannon & Wilson report estimated the cost of necessary short-term repairs to be approximately \$2.9 million. However, as a result of the loss of traffic from a major shipper, and increasing expenses (especially the cost of fuel) that CORP has not been able to offset by raising rates or attracting new traffic to the line, operating losses on the Coos Bay Line have increased to more than \$1 million annually.

Nevertheless, rather than move immediately to seek authority to abandon the Coos Bay Line, CORP attempted over the winter to forge a partnership of interested stakeholders (including UP, the State of Oregon, the Port of Coos Bay, and shippers) to participate in a plan to preserve rail service over the line. CORP proffered multiple proposals designed to address both the capital needs of the Coos Bay Line and the ongoing losses generated from CORP's operations over the line. However, those proposals have failed to garner support. Accordingly, following the rejection of its most recent proposal by the State of Oregon on April 21, 2008, and subsequent statements by UP indicating that it has no intention of participating financially in any plan to save the Coos Bay Line, CORP has begun the process of seeking authority to abandon the line.

These facts establish that CORP's decision to embargo the Coos Bay Line for safety reasons was justified – indeed, it was necessary – and that CORP has acted reasonably in attempting to obtain financial assistance from interested parties to restore and preserve rail service on the line prior to seeking abandonment. Accordingly, there are no grounds upon which

the Board could reasonably find that the initial embargo of the Coos Bay Line and the embargo's continuation to the present time were unreasonable, or that CORP's actions have amounted to an unlawful abandonment.

**CORP'S EMBARGO OF THE COOS BAY LINE  
WAS REASONABLE AND REMAINS REASONABLE**

**I. Legal Standard**

Federal law requires rail carriers to provide "transportation or service on reasonable request." 49 U.S.C. § 11101(a). But this statutory common carrier obligation is not absolute and may be temporarily suspended if a rail carrier is incapable of providing service. *Show Cause Order* at 3, citing *Chicago & N.W. Transp. Co. v. Kalo Brick & Tile Co.*, 450 U.S. 311, 325 (1981); see *ICC v. Baltimore & Annapolis R. Co.*, 398 F. Supp. 454, 467 (D. Md. 1975). As the Board stated in the *Show Cause Order*, "[s]uch incapacity may arise from physical conditions affecting safety such as weather and flood damage [or] tunnel deterioration." *Id.*, citing STB Fin. Docket No. 32821, *Bar Ale, Inc. v. California Northern R. Co. and Southern Pacific Transp. Co.*, at 5 (served July 20, 2001) ("*Bar Ale*").

When physical conditions prevent safe rail operations, a carrier may declare an embargo without prior Board approval. See *Show Cause Order* at 2 n.2. An embargo is "an emergency measure placed in effect because of some disability on the part of the carrier which makes the latter unable properly to perform its duty as a common carrier." *Chicago N.W. Ry. Co. v. Union Packing Co.*, 373 F. Supp. 734, 736-37 (D. Neb. 1974), quoting *Froehling Supply Co. v. United States*, 194 F.2d 637, 641 (7th Cir. 1952). If justified, such an embargo temporarily relieves the carrier of its common carrier obligation. *Show Cause Order* at 2 n.2, citing STB Fin. Docket No. 42087, *Groome & Associates, Inc. v. Greenville County Econ. Dev.*

*Corp.*, at 11 (served July 27, 2005) (*Groome*); *see ICC v. Chicago, Rock Island, & Pacific R. Co.*, 501 F.2d 908, 911 (8th Cir. 1974).

An embargo will be deemed lawful if it is “reasonable at the time it is issued,” and if the carrier’s decision to maintain the embargo “continue[s] to be reasonable as well.” *Show Cause Order* at 3, *citing* STB Finance Docket No. 33386, *Decatur County Comm’rs v. The Central Railroad Co. of Indiana*, at 19 (served Sept. 29, 2000) (“*CIND*”), *aff’d sub nom. Decatur County Comm’rs v. STB*, 308 F.3d 710 (7th Cir. 2002); *GS Roofing Prods. Co. v. STB*, 143 F.3d 387, 392 (8th Cir. 1998).

In determining whether an embargo is reasonable when issued, it “is well established that a carrier must decide in the first instance whether an unsafe condition exists that prevents it temporarily from providing service.” *Groome* at 12, *citing* STB Fin. Docket No. 34236, *Bolen-Brunson-Bell Lumber Co. v. CSX Transp., Inc.*, at 6 (May 9, 2003) (“*BBB Lumber*”); *see Bar Ale* at 7. The Board “typically defer[s] to the operating carrier’s opinion” on such safety issues. *Id.* Such “deference to expert representatives of the operating carrier” is appropriate because the carrier could “be held responsible in the event of a catastrophic accident.” *BBB Lumber* at 6; *see Bar Ale* at 7.

In reviewing whether an embargo remains reasonable, the Board typically balances these factors: (1) the cost of repairs necessary to restore service; (2) the amount of traffic on the line; (3) the carrier’s intent; (4) the length of the service cessation; and (5) the financial condition of the carrier. *See Show Cause Order* at 3, *citing Groome*, at 12; *see also Decatur County Comm’rs v. STB*, 308 F.3d at 715; *GS Roofing Prods. Co. v. STB*, 143 F.3d at 392, *citing Louisiana Railcar, Inc. v. Missouri Pacific R. Co.*, 5 I.C.C.2d 542, 544 (1989); *Overbrook Farmers Union Coop. Ass’n—Petition for Declaratory Order*, 5 I.C.C.2d 316, 320

(1989). These factors “are not applied in a formulaic way,” but are considered in light of all of the circumstances to determine whether the embargo remains reasonable. *Show Cause Order* at 3; *Groome* at 12; *Bar Ale* at 6-7.

As the following sections of this Response amply demonstrate, CORP’s embargo of the Coos Bay Line clearly was reasonable when initiated, and remains reasonable at the present time.

## II. CORP’s Embargo of the Coos Bay Line Was Reasonable When Issued

CORP embargoed the Coos Bay Line because it became clear that continued operation of the line would be unsafe in light of the deteriorated condition of several timber-lined tunnels. CORP’s judgment that this “unsafe condition . . . prevent[ed] it temporarily from providing service” was eminently reasonable and justified initiating the embargo. *Groome* at 12. Indeed, CORP’s embargo decision was supported by the findings of an independent geotechnical consulting firm and confirmed by an independent inspection and report by FRA.

In the months leading up to the embargo of the Coos Bay Line, conditions in several timber-lined tunnels on the line made it clear that substantial repairs were needed to ensure safe transportation over the line. Verified Statement of Paul Lundberg at 5-6 (“V.S. Lundberg”). In October 2006, a joint inspection of the Coos Bay Line by FRA and the Oregon Department of Transportation (“ODOT”) revealed significant deterioration in Tunnel No. 15 (located near MP 721). *Id.* at 6. CORP responded immediately to this discovery by hiring a contractor to repair Tunnel No. 15. *Id.* The estimated cost of those repairs was \$350,000 - \$400,000. *Id.* However, while the repairs were being performed (in November 2006), Tunnel No. 15 collapsed. *Id.* This incident resulted in closure of the tunnel for three months, and increased the repair cost to \$1.7 million. *Id.* CORP also lost \$500,000 in freight revenues while Tunnel No. 15 remained closed. *Id.*

Following this incident, CORP engaged Shannon & Wilson in March 2007 to evaluate the condition of all nine tunnels on the Coos Bay Line. *See* V.S. Lundberg at 6. Shannon & Wilson inspected the tunnels during March and April 2007, and reported their findings to CORP's engineers on July 16, 2007. *See* Exhibit 6. Shannon & Wilson identified "severe liner and/or rock deterioration and instability" in Tunnel Nos. 13, 15 and 18. *See* Exhibit 6 at 3. The report stated that the "[i]mmediate tunnel stability problems are related to the progressively and intensely deteriorated and rotted condition of timber in timber-lined sections" in these tunnels, and "unlined sections with associated rockfall hazard" in Tunnel 13. *Id.* at 6. Shannon & Wilson recommended that certain short-term repairs to Tunnel Nos. 13, 15 and 18 be performed within 6-12 months. *Id.* at 2, 6. The estimated cost of such short-term repairs was approximately \$2,861,000. *Id.* at 11, Estimated Construction Cost Summary. Shannon & Wilson also recommended that CORP perform additional work in the tunnels on the Coos Bay Line within 12-48 months. The total cost of all tunnel work recommended by Shannon & Wilson was approximately \$6.7 million. *Id.*

The condition of the tunnels continued to worsen. Just prior to receipt of the Shannon & Wilson report by CORP in July 2007, Tunnel No. 15 experienced another timber set failure. V.S. Lundberg at 7. In August, CORP personnel conducted a detailed inspection of Tunnel No. 19 from the cab of a locomotive (rather than in a hi-rail vehicle) due to concern that falling rocks inside the tunnel presented a hazard to the inspection party. *Id.* Faced with increasingly hazardous conditions in the tunnels on the Coos Bay Line, CORP brought the situation to the attention of RailAmerica management on September 18-19, 2007. *Id.* RailAmerica agreed with CORP that the line should be embargoed for safety reasons, and CORP issued an embargo notice

covering the portion of the Coos Bay Line between Coquille and Richardson, OR on September 21, 2007. *See* Exhibit 7.

FRA concurred with CORP's judgment that conditions in Tunnel Nos. 13, 15 and 18 warranted an embargo of the Coos Bay Line. In October 2007, FRA conducted its own inspection of the tunnels, and issued a written report of its findings. *See* Exhibit 8. The FRA inspectors "substantially validate[d] the findings documented in the Shannon and Wilson report." Exhibit 8 at 4. Indeed, FRA found that "some conditions have deteriorated even further during the time since the report was prepared, partly due to the passage of time, and partly because of the onset of the wet season in Oregon in the early fall of 2007." *Id.* FRA concluded that "[t]hese tunnels are hazardous to train traffic and maintenance operations," and concurred with Shannon & Wilson's assessment of the repairs needed to restore the line to a safe operating condition. *Id.*

Thus, CORP's decision to embargo the Coos Bay Line was based upon serious and well-documented safety concerns that were subsequently corroborated by FRA. The Board has long recognized that such concerns justify the initial imposition of an embargo. *See Bar Ale* at 4. Indeed, the Board "typically defer[s] to the operating carrier's opinion" that an unsafe condition requires an embargo. *Id.*; *see BBB Lumber* at 6. That deference is particularly appropriate here, where CORP's safety concerns about conditions in Tunnels 13, 15, and 18 are confirmed by inspections and written reports developed independently by an expert geotechnical services firm (Shannon & Wilson) and by FRA. In particular, given FRA's expertise in matters of rail safety, FRA's finding that the Coos Bay Line tunnels were "hazardous to train traffic and maintenance operations" is conclusive evidence that CORP's initial decision to impose an embargo was reasonable. *Cf. Ex Parte No. 574, Regulations on Safety Integration Plans*, 63 Fed. Reg. 72225, 72225-26 (Dec. 31, 1998) ("FRA has expertise in the safety of all facets of railroad

operations”). Indeed, at the hearing in *Ex Parte No. 677* on April 25, 2008, Chairman Nottingham stated that “I don’t think you’ll get anybody from the Board questioning this – that the Federal Railroad Administration did a solid job of inspecting the situation in the wake and aftermath of your embargo last fall, and the FRA put together a report that certainly indicates serious safety problems with those tunnels, and I’m not here to second-guess, which could very well have been a life and death decision that RailAmerica had to make to put safety first based on what I saw confirmed in that FRA report.”<sup>5</sup>

### **III. CORP’s Embargo of the Coos Bay Line Has Continued To Be Reasonable.**

CORP’s embargo of the Coos Bay Line was not only justified when it was imposed, it has remained reasonable at all times. The Board has looked to five factors when determining whether continuance of an embargo is reasonable: the carrier’s intent, the length of the embargo, the cost of repairs necessary to resume service, the amount of traffic on the line, and the financial condition of the carrier. *See Show Cause Order* at 3; *Groome* at 12. Individually and cumulatively, these factors strongly weigh in favor of the reasonableness of the embargo in the instant case.

#### **A. CORP Intended to Restore Service to the Coos Bay Line, Not to Effect an Unlawful Abandonment.**

In determining whether an embargo is reasonable, the Board considers whether the carrier intended to use the embargo as a means to effect an unlawful *de facto* abandonment. *See BBB Lumber* at 4. As part of this inquiry, the Board considers whether the carrier deliberately allowed the line to deteriorate to a non-operable condition in order to hasten its closure. *See id.* Here, the record plainly demonstrates that, in the time leading up to the

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<sup>5</sup> *See Ex Parte No. 677, Common Carrier Obligation of Railroads*, April 25, 2008 Hearing Transcript at 161-162 (Comments of Chairman Nottingham).

embargo, CORP invested substantial sums for both ordinary maintenance of the Coos Bay Line and to address problems in a tunnel on the line. Moreover, in the months since the embargo was initiated (during which repairs could not have commenced in any event), CORP diligently attempted to persuade interested stakeholders to participate with it in several proposals designed to address the capital needs of the Coos Bay Line and to preserve service for the long term.

As the testimony of RailAmerica's Vice President Paul Lundberg shows, CORP has not allowed the Coos Bay Line to deteriorate as a prelude to embargo (and ultimately, to abandonment). *See* V.S. Lundberg at 4-5. To the contrary, CORP has invested in maintenance of track, bridges and crossings on the Coos Bay Line at a rate that far exceeds the prevailing level of maintenance spending in the rail industry. *Id.* Between 2003 and 2007, CORP spent an average of 28 percent of the annual gross freight revenues earned on traffic moving over the Coos Bay Line for normal track, bridge and crossing maintenance on that line. *Id.* In 2006 (the last full year of operations over the line), CORP spent \$934,000, fully 32 percent of the \$2.93 million in gross freight revenues generated by traffic on the Coos Bay Line, to maintain tracks, bridges and crossings on the line. *Id.* at 5. This level of maintenance expenditures – which is necessitated by the rugged terrain of the Coos Bay Line – far exceeds the average cost (approximately 13% of gross freight revenues) incurred by RailAmerica's other shortline carriers for track, bridge and crossing maintenance. *Id.* The percentage of gross freight revenues devoted by CORP to maintain the Coos Bay Line is likewise far greater than that invested by Class I railroads. The *Statistics of Class I Freight Railroads* for the year 2004 indicates that the aggregate expenditure by Class I carriers for all "Ways and Structures" expenses was \$6.4

billion, or 15.8% of their aggregate gross operating revenues of \$40.5 billion in that year.<sup>6</sup> In 2005 and 2006, the aggregate expenditure by Class I carriers for all “Ways and Structures” expenses represented 14.09% and 13.10%, respectively, of their aggregate gross operating revenues in those years.<sup>7</sup> As these data show, CORP has been anything but negligent in its approach to maintaining the Coos Bay Line.

Moreover, as discussed above, CORP responded promptly to the collapse of Tunnel No. 15 in November 2006 by incurring \$1.7 million in repair costs to restore service on the Coos Bay Line. V.S. Lundberg at 6. This extraordinary expenditure – at a time during which the Coos Bay Line was experiencing operating losses of approximately \$1 million per year (*see id.* at 5) – belies the notion that CORP intended to close the line. Indeed, it would make no economic sense for CORP to make such a large investment, or to continue to pour such a large percentage of gross freight revenues into ordinary maintenance, on a line that it secretly desired to abandon.

CORP’s conduct after the embargo was imposed likewise demonstrates its intent to try to preserve (rather than abandon) the Coos Bay Line. As Mr. Lundberg testifies, Shannon & Wilson’s estimate of the cost of the tunnel work required to restore service raised serious concerns at CORP (and RailAmerica) about the viability of the Coos Bay Line. *Id.* at 8. The decision by a major shipper on the line, Weyerhaeuser Corporation, to close its paper manufacturing facility at Cordes, OR in 2004 resulted in the loss of 3,000 annual carloads of rail

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<sup>6</sup> “Way and Structures” expense includes not only the cost of maintaining tracks, bridges, and crossings, but also a myriad of other maintenance-related expenses, including signals and interlockers, communications systems, certain lease and joint facility rentals, fringe benefits and certain casualty and insurance costs. *See Statistics of Class I Freight Railroads*, Table 5, Lines 1-151, at 8-9 (2004).

<sup>7</sup> *See Class I Railroad Annual Report (R-1)*, Sched. 210, Line 13 (Total Railway Operating Revenue) and Sched. 410, Line 151 (Total Way and Structures) as filed with the STB by each Class I railroad for 2005 and 2006 (at [http://www.stb.dot.gov/stb/industry/econ\\_reports.html](http://www.stb.dot.gov/stb/industry/econ_reports.html)).

business and caused the previously profitable Coos Bay Line to incur an operating loss of more than \$578,000 in 2004. *Id.* at 5. The major run-up in fuel prices during 2005 and 2006, coupled with CORP's inability to find new business to offset the loss of Weyerhaeuser's traffic, resulted in further operating losses on the line of approximately \$939,000 in 2005, \$1.17 million in 2006, and \$792,000 through September 2007. *Id.* Under these conditions, a minimum investment of \$2.9 million for short-term repairs to the tunnels on the Coos Bay Line could not be economically justified.<sup>8</sup>

Nevertheless, rather than seeking immediately to abandon the Coos Bay Line, CORP undertook an effort during the winter of 2007 (when weather conditions precluded the commencement of tunnel repairs in any event) to solicit the participation of interested stakeholders in a plan to preserve rail service over the Coos Bay Line. V.S. Lundberg at 9. After meetings with shippers, Oregon legislators and ODOT, CORP presented a plan for a "public/private partnership" based upon a model that had been successful in preserving service on a RailAmerica-owned shortline in Canada (the Cape Breton & Nova Scotia Railroad). *Id.* This plan, if implemented, would have laid the foundation for continued service on the Coos Bay Line by addressing both the capital needs of the line and mitigating the ongoing losses generated from operations. Specifically, CORP proposed that CORP, UP, ODOT, the Port of Coos Bay and shippers on the line each contribute \$4.66 million over a five-year period to fund approximately \$23.3 million dollars in capital work to address not only the tunnel repairs but

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<sup>8</sup> In evaluating the economic justification for such an investment, CORP was mindful of the fact that the collapse of Tunnel No 15 during the course of "minor" repairs in November 2006 had inflated the cost of fixing that tunnel from \$400,000 or less to approximately \$1.7 million. V.S. Lundberg at 6. Moreover, Shannon & Wilson had advised that a \$2.9 million investment in short-term repairs would not assure the safety of the tunnels on the line – rather the cost of addressing the deteriorated conditions in Tunnel Nos. 13, 15 and 18 would be nearly \$7 million over the next four years. *Id.*; see Exhibit 6 at 11, Estimated Construction Cost Summary.

also major rehabilitation of track and bridges required to assure safe and efficient operations on the Coos Bay Line. *Id.* CORP also proposed that ODOT enter into an agreement with CORP to provide an annual subsidy to offset operating losses on the line. *Id.* From CORP's perspective, such ongoing financial participation by the State was critical to preserving service over the Coos Bay Line, because no amount of investment tracks and tunnels could, by itself, stem the substantial (and growing) operating losses being incurred by CORP. *Id.*

The reaction to CORP's initial proposal was not encouraging. On January 24, 2008, Oregon Governor Kulongoski told CORP that the State would not participate in such a plan unless and until CORP itself repaired Tunnel Nos. 13, 15 and 18 (at CORP's sole expense) and resumed service on the Coos Bay Line. *Id.* at 10. Governor Kulongoski also indicated that any financial assistance that the State might extend would be contingent upon CORP giving the State an equity stake in the line. *Id.* Based on the State's response to its public/private partnership proposal, CORP presented an alternate plan to Governor Kulongoski on April 9, 2008. *Id.* This revised plan involved a joint venture between CORP and the State, under which the State would acquire a 50% equity interest in 65 miles of the Coos Bay Line between Vaughn and North Bend, OR, as well as the right to all of the freight and non-freight revenues generated by that line. *Id.* Going forward, CORP would operate the line on a contract basis on behalf of the joint venture. *Id.* The State would, in turn, contribute funds to rehabilitate that segment to a safe and stable operating condition and share equally in any profit from operation of the jointly owned line. *Id.* This proposal expressly addressed both Governor Kulongoski's requirement that State financial assistance be coupled with an equity interest in the line, and CORP's need for a plan that addressed not only the immediate capital requirements of the Coos Bay Line but also the ongoing losses from operations. However, Governor Kulongoski rejected CORP's joint venture

proposal on April 21, 2008, reiterating the State's demand that CORP repair the tunnels and recommence service as a precondition to any negotiations concerning the future of the Coos Bay Line. *See* Exhibit 9.

The response from other stakeholders was similarly disappointing. Shippers declined to participate in the proposed public/private partnership, taking the position that CORP's proposal amounted to "extortion" of repair costs that in their opinion CORP was legally obligated to incur for their benefit. V.S. Lundberg at 10. UP – for which CORP acts as a "switching carrier" on most traffic that moves over the Coos Bay Line (*id.* at 11) – did not reply at all to CORP's public/private partnership proposal until the Board's April 24, 2008 hearing in *Ex Parte No. 677*. At the hearing, UP's Vice President – Law, Mr. Hemmer, stated unequivocally that UP is not interested in participating financially in CORP's proposal to preserve the Coos Bay Line.<sup>9</sup> In a subsequent letter to the Board, Mr. Hemmer explained that, in UP's opinion, "the Coos Bay Line has generated insufficient traffic to support reinvestment in the line" and that "private entities are unlikely to recover any return on investment in the line." *See* Exhibit 4 at 2.

CORP was disappointed by these responses to its good faith attempt to find a solution that would preserve service over the Coos Bay Line. In particular, the State's insistence that CORP incur the full cost of repairing Tunnel Nos. 13, 15 and 18 before the State will even discuss such a solution places CORP in the untenable position of being required to invest a minimum of \$3 million in a line that is losing more than \$1 million per year, without any assurance that making such an investment will result in a viable plan to preserve service on the line. V.S. Lundberg at 11. UP's outright refusal to contribute to a long-term solution for the

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<sup>9</sup> *See Ex Parte No. 677, Common Carrier Obligation of Railroads*, April 24, 2008 Hearing Transcript at 142-44 (Testimony of Michael Hemmer).

Coos Bay Line suggests that UP is not concerned by the prospect of losing the traffic generated by shippers on the line – who are, under the terms of the Cooperative Marketing Agreement under which most Coos Bay Line traffic moves, UP's customers. *Id.* The Port of Coos Bay's response to CORP's proposal flies in the face of its statements that continued rail service is vital to the potential future of the port as a container facility. *Id.* Just as unfortunately, none of these stakeholders has suggested any plan of their own that would enable CORP to resume service on the Coos Bay Line on a financially sustainable basis.

In light of these developments – and, in particular, the rejection of CORP's most recent proposal by Governor Kulongoski on April 21, 2008 and UP's statements in connection with the hearings in *Ex Parte No. 677* on April 24-25 – CORP determined that it has no realistic alternative but to seek to abandon the Coos Bay Line. V.S. Lundberg at 12. Up until that time, CORP had been hopeful that its efforts to forge a partnership among interested stakeholders might ultimately be successful. However, CORP has now come to the conclusion that such a solution will not be forthcoming. Therefore, on May 8, 2008, CORP promptly took the first step required to invoke the Board's abandonment jurisdiction, by amending its system diagram map to reclassify the Coos Bay Line in Category 1. CORP intends to file a notice of abandonment and an application seeking authority to abandon the Coos Bay Line as soon as permitted by the Board's regulations.

As these facts show, until very recently, CORP's intent was to find a solution that would have resulted in the repair of the tunnels on the Coos Bay Line and the resumption of service over the line. CORP's intentions are evidenced by the consistent level of expenditures by CORP to maintain the line (despite increasing losses from operations) and by its prompt repair of the damage caused by the collapse of Tunnel No. 15 in November 2006. CORP's repeated

efforts over the past several months to solicit the participation of other stakeholders in a number of alternative plans that would have preserved long-term service on the Coos Bay Line provides further evidence that CORP did not impose the embargo with the intention of effecting an unlawful *de facto* abandonment. To the contrary, only when it became apparent (during the last week in April) that CORP's efforts had proven futile did CORP determine that abandonment of the line is inevitable. CORP then acted promptly to invoke the Board's abandonment jurisdiction. In short, the evidence demonstrates that CORP never intended to use the embargo process to accomplish an unlawful abandonment, and this factor weighs in favor of the reasonableness of the embargo.<sup>10</sup>

**B. The Length of the Embargo is Reasonable**

The length of the Coos Bay Line embargo is reasonable. In the first place, weather conditions in Oregon during the fall and winter months (and continuing into the spring) effectively prevented CORP from initiating repairs to the tunnels on the Coos Bay Line. Moreover, CORP's efforts to develop a public/private partnership arrangement to fund repairs to the tunnels and to address the ongoing operating losses on the Coos Bay Line did not unreasonably extend the embargo, because CORP could not have completed repairs to the tunnels and reopened the Coos Bay Line under any circumstances until September 2008 at the earliest. Thus, the embargo has continued to be reasonable at all times up to the present.

The timing of the tunnel failures on the Coos Bay Line made it impracticable for CORP to commence repairs immediately following issuance of the embargo notice. As Mr.

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<sup>10</sup> The fact that a carrier may seek to abandon a rail line after it has been embargoed does not make the embargo itself unreasonable. As the Board has noted, there are "many . . . cases in which a carrier first (lawfully) embargoes a line, and then (lawfully) obtains authority to abandon it." STB Docket No. 41230, *GS Roofing Products Co. v. Arkansas Midland R. Co. & Pinsky R. Co.*, at 14 n.51 (served March 11, 1997) (citing numerous cases), *rev'd on other grounds in GS Roofing, supra*.

Lundberg explains, the onset of the rainy (winter) season in Oregon is generally accompanied by increased seepage in rail tunnels. V.S. Lundberg at 7. The Shannon & Wilson report indicated that the wet conditions in the tunnels during this time increases the risk of tunnel instability if timber sets are removed or disturbed. *See* Exhibit 6, September 21, 2007 Supplement at 2. Moreover, attempting to apply shotcrete to wet surfaces within the tunnels is both impracticable and hazardous. V.S. Lundberg at 7-8. For that reason, Shannon & Wilson cautioned that “it may not be safe for much of the repair work to be undertaken until the drier months of next spring and summer.” Exhibit 6, September 21, 2007 Supplement at 2. CORP’s prior experience with Tunnel No. 15 – which collapsed while CORP’s contractor was making relatively minor repairs during the month of November – provided further warning that attempting to initiate major repairs to three tunnels during the wet winter season would be fraught with risk (both financially and to the safety of persons working within the tunnels).

Moreover, as Mr. Lundberg testifies, there are a limited number of contractors who possess the specialized experience required to undertake repairs to timber tunnels such as those on the Coos Bay Line. V.S. Lundberg at 8. It is not likely that CORP could have hired sufficient crews to perform the repair work in Tunnel Nos. 13, 15 and 18 simultaneously. Rather, the repairs to each of those tunnels would have to be performed sequentially. *Id.* For that reason, CORP estimated that the Level 1 and Level 2 repairs recommended by Shannon & Wilson would require approximately four months to complete. *Id.* In presenting its initial proposal to preserve service on the Coos Bay Line to stakeholders in November 2007, CORP indicated that, even if weather conditions permitted tunnel repairs to begin as early as May 1, 2008, shippers could expect the line to reopen no earlier than September 2008. *Id.* Thus, the embargo continues to be reasonable at the present time because CORP could not have completed

repairs to the tunnels and reopened the Coos Bay Line under any circumstances until September 2008.

This conclusion is not diminished by CORP's actions in seeking to solicit public and/or private financial participation in its efforts to repair the tunnels and to resume service over the Coos Bay Line on a financially sustainable basis. As explained above, the ongoing losses from operation of the Coos Bay Line made it impossible for CORP to justify incurring the multi-million dollar capital cost of repairing the tunnels on the line. For this reason, CORP pursued a variety of proposals that would involve assistance by other stakeholders in repairing and restoring service over the Coos Bay Line.

An embargo will not be deemed to be unreasonable while a rail carrier is making reasonable efforts to negotiate with interested parties to secure funding for the repair and continued operation of the line. Indeed, the Board has found that an embargo was reasonable during a *two-year* period in which the carrier attempted to obtain funding to restore service on the line. *See Groome* at 15; *see also Decatur County Comm'rs*, 308 F.3d 710 (upholding Board's determination that twenty month embargo was not unreasonable).

In *Groome*, the rail line at issue was taken out of service in 1997, when two bridges on the line were damaged. The line was still out of service when it was acquired by Greenville County Economic Development Corporation ("GCEDC") in June 1999. Over the next two years, GCEDC sought funding from shippers and government sources and attempted to negotiate with potential operators to restore service. These efforts were unsuccessful, and rail service was never restored. Upon complaint by a shipper, the Board found that GCEDC "made reasonable efforts to obtain funding and to find an operator for the first two years after it bought the line." *Id.* at 15. But after two years of negotiations proved unsuccessful, the Board found

“it was, or should have been, apparent to GCEDC that plans for funding and operating the line would not succeed.” *Id.* After that time, the Board held “GCEDC should have known that it was time to seek to end its obligation to provide service, and it was unreasonable for it not to begin the abandonment or discontinuance process” after that time. *Id.* The Board found that GCEDC acted reasonably in continuing the embargo while negotiating for funding to restore service and held that the embargo became unreasonable only after the rail carrier knew or should have known that its efforts to obtain funding would not succeed.

Here, as in *Groome*, CORP has diligently attempted to forge a partnership with stakeholders to restore service to the line. This effort lasted only seven months, far less than the *two years* that the Board found reasonable in *Groome*. When Governor Kulongoski rejected CORP’s joint venture proposal on April 21, 2008 and UP indicated clearly during the last week in April that it would not participate financially in any plan to save the Coos Bay Line, it became apparent to CORP that its efforts would not succeed, and CORP promptly took the first step (amending its system diagram map) required to initiate the abandonment process. CORP intends to file a notice of abandonment and an application seeking authority to abandon the Coos Bay Line as soon as permitted by the Board’s regulations. Moreover, in the instant case, CORP’s efforts to solicit financial assistance took place entirely during a period in which service could not have been restored in any event, due to the weather conditions in Oregon and the time (a minimum of four months) required to perform the necessary tunnel work. Thus, CORP’s actions did not in any way increase the duration of the embargo. In these circumstances, *Groome* clearly supports a finding that the duration of CORP’s embargo has been reasonable.

**C. The Significant Cost of Repairs Weighs In Favor of The Embargo's Reasonableness.**

There is no question in this case that the cost of necessary repairs to the tunnels on the Coos Bay Line supports a finding that the embargo implemented by CORP was reasonable. As stated above, Shannon & Wilson estimated that immediate repairs to Tunnel Nos. 13, 15, and 18 – repairs that the FRA agreed were necessary – would cost approximately \$2.9 million. Shannon & Wilson also identified nearly \$4 million in additional tunnel repairs that would be required over a four-year period to restore the tunnels to a safe and stable operating condition. *See* Exhibit 6 at 8. These estimated repair costs are particularly burdensome when considered in light of the large (and increasing) losses incurred by CORP in operating the Coos Bay Line over the past several years. In the circumstances of this case, the substantial cost of repairing the tunnels weighs heavily in favor of the reasonableness of the embargo.

“[A]n embargo may remain valid if service cannot be resumed at a safe level without substantial expenditures.” *Decatur County Comm’rs*, 308 F.3d at 393, *citing GS Roofing*, 143 F.3d at 394. Conversely, “[i]f service can be resumed at safe levels without substantial expenditures of time or money, a railroad should not be permitted to refuse to resume service simply because extensive improvements might be necessary for the long-term success of the line.” *GS Roofing Prods. Co. v. STB*, 143 F.3d at 394 (finding embargo unreasonable where carrier was able to resume service after spending only four hours and about \$10,000 in repairing washouts and other storm damage).

In cases, like this one, where an embargoed line requires substantial repairs, the “amount of traffic on the line, and the revenues that it would produce, are significant factors in assessing the relative costs of the repairs.” *BBB Lumber* at 7. The Board has explicitly held that “a carrier cannot legitimately be required to expend money to rehabilitate a line where it will lose

money on the operation.” STB Fin. Docket No. 34337, *Michael H. Meyer, Trustee, v. North Coast R.R. Auth., d/b/a Northwestern Pacific R.R.* (served July 27, 2005) (emphasis added).<sup>11</sup>

The Board has likewise recognized that “repair costs that significantly exceed the revenues or profits from the traffic on a line can justify even a lengthy embargo.” *Id.* at 7 n.12. In such cases, the Board has considered “whether it made business sense . . . to invest in the necessary repairs under the conditions that prevailed.” *Decatur County Comm’rs*, 308 F.3d at 719. The Board has not required carriers to make expensive repairs when the revenues from the line would not be enough to provide a return on that investment. *Id.* (“Projected revenues from such traffic would be significantly less than what would be needed to cover operating expenses and provide a return on investment (ROI), let alone to cover the needed repairs and rehabilitation”) (*quoting CIND* at 18). This “eminently reasonable” approach has been approved on judicial review. *Id.*

In the instant case, it clearly makes no “business sense” for CORP to invest a minimum of \$2.9 million to repair tunnels on a rail line that has been losing more than \$1 million annually in recent years (unless CORP obtains financial assistance from other stakeholders to make such repairs and to restore service on a financially viable basis). As Mr. Lundberg explains, unlike Class I railroads (and many shortline carriers), CORP does not control the pricing of the vast majority of the traffic that moves over the Coos Bay Line. Rather, the rates on that traffic are controlled by UP, with CORP being paid a fixed fee for handling the

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<sup>11</sup> See also *Purcell v. United States*, 315 U.S. 381, 385 (1942) (“When materials and labor are devoted to the [re]building of a line in an amount that cannot be justified in terms of the reasonably predictable revenues, there is ample ground to support a conclusion that the expenditures are wasteful whoever foots the bill.”); *Chicago & N.W. Transp. Co. v. Kalo Brick & Tile Co.*, 450 U.S. 311, 325 (1981) (carrier authorized to abandon rather than repair a line damaged by mud slides; duty to serve is not absolute, but requires only what is reasonable under the existing circumstances); see *Brooks-Scanlon Co. v. R.R. Comm’n of La.*, 251 U.S. 396, 397-99 (1921) (to compel a carrier “to carry . . . at a loss” could “deprive [it] of its property without due process”); accord, *Bullock v. R.R. Comm’n of Fla.*, 254 U.S. 513 (1921); *R.R. Comm’n of Texas v. Eastern Texas R.R.*, 264 U.S. 79 (1924).

traffic as a switching carrier. V.S. Lundberg at 3-4. As a result, CORP does not have the ability to take pricing actions that might generate additional revenues from its operations. Nor does there appear to be any realistic prospect that CORP can offset its ongoing losses by attracting new business to the line. *Id.* at 5. In these circumstances, it was eminently reasonable for CORP to attempt to obtain financial assistance from other stakeholders before beginning these substantial repairs. Indeed, it would have been utterly irrational for CORP to pour millions of dollars into a line that otherwise had no prospect of becoming profitable.

A carrier's capacity to make repairs on a line must be judged in light of the future projected revenues on that line. In *Decatur County Comm'rs*, for example, the repairs needed to restore service would have cost approximately \$370,000 for the embargoed portion of the line, with an additional \$187,000 needed to restore the non-embargoed portion of the line to FRA Class 1 standards, while the rail carrier "was in a difficult financial condition and faced dim prospects for increased traffic and revenues." *Decatur County Comm'rs*, 308 F.3d at 716. The complaining shippers argued that the Board should consider only the rail carrier's "present financial capability to make repairs," and should disregard the line's long-term feasibility and profitability. *Id.* Both the Board and the reviewing court rejected this approach. As the Seventh Circuit stated, "[l]imiting the Board only to considerations of present financial capability . . . would not be a sensible policy." 308 F.3d at 720. Rather, the court stated, "[t]his case is a perfect example of the need to allow the Board the flexibility to examine both past and projected financial circumstances to arrive at fiscally reasonable solutions." *Id.*

As the court stated, "[n]ot allowing the Board to consider the context of the railroad's present financial condition in light of past and projected future financial conditions would hamper the Board in deciding whether an embargo was reasonable." The court added that

“[i]t makes no economic sense always to compel a common carrier to make repairs” based solely upon the carrier’s present financial capability to do so. Distinguishing *GS Roofing*, in which the embargoed line needed “minor interim repairs” at a minimal cost, the Seventh Circuit stated, “[w]e believe that future projected revenues may be considered in determining a common carrier’s capability to carry out repairs.” 308 F.3d at 720. In light of the embargoed line’s questionable prospects for long-term profitability, the Seventh Circuit upheld the Board’s determination that the rail carrier’s embargo of the line for twenty months was not unreasonable under the circumstances. The court stated, “[i]f abandonment was to be the ultimate fate of the line, the twenty-month embargo was not unjustified.” 308 F.3d at 717.

In sum, the Board’s precedents establish that if an embargoed line can be repaired “inexpensively, quickly, and within the carrier’s means, then the carrier’s failure to provide service for a long period may constitute a violation of the common carrier obligation.” *Groome* at 13, *citing GS Roofing*. That is not the case here, where the cost of the necessary repairs is very large and where the negative operating income generated by the line makes it highly unlikely that the cost of those repairs can ever be recovered. Here, the needed “repairs will be expensive and potential traffic over the line is light,” and even “a lengthier embargo” is not unlawful. *Id.* Under the circumstances, an embargo for the seven months while CORP was actively attempting to secure partners to provide the necessary financial assistance to reopen the line is surely not unreasonable.

**D. The Embargo Was Reasonable in Light of the Amount of Traffic on the Line.**

The Board also considers “the amount of traffic on the line, and the revenues that it would produce.” *BBB Lumber* at 5. This factor supports the reasonableness of the embargo in this case, because current traffic levels make it impossible for CORP to earn sufficient revenues to fund the needed repairs. While the Coos Bay Line was profitable during the first several years

of RailAmerica ownership, a major shipper on the line, Weyerhaeuser Corporation, ceased operations at its paper manufacturing facility at Cordes, OR in 2004. *V.S. Lundberg* at 5. The closure of that plant, which generated approximately 3,000 carloads of rail business annually, contributed to a precipitous decline in the volume of traffic moving over the Coos Bay Line, from 7,574 carloads in 2003 to 5,408 carloads in 2004. *Id.* This, in turn, caused the Coos Bay Line to experience an operating loss of more than \$578,000 in 2004. *Id.* As fuel prices spiked, the operating losses on the Coos Bay Line grew to approximately \$939,000 in 2005 and \$1.17 million in 2006. *Id.* By the time the line was embargoed on September 21, 2007, the operating loss for that year was already \$792,000. *Id.*

More importantly, CORP's inability to adjust the rates on Coos Bay Line shipments prevents it from earning sufficient revenues at current traffic levels to fund operating expenses on the line—let alone the needed repairs to Tunnels 13, 15, and 18. The lack of sufficient revenues to pay for repairs to Tunnels 13, 15, and 18 strongly militates in favor of the reasonableness of an embargo while CORP attempted to secure financial assistance to remedy the fact that revenues from the Coos Bay Line could not pay for those repairs.

**E. The Embargo Was Reasonable In Light of the Financial Condition of CORP.**

Finally, the question of whether the carrier is financially able to make the repairs necessary to lift the embargo “may be relevant to the reasonableness of an embargo.” *BBB Lumber* at 9. If a carrier is experiencing financial difficulties, that factor is given “substantial weight in assessing the reasonableness” of a decision not to incur the costs of repairs. *Id.*; *see also Bar Ale* at 8 (noting that the Southern Pacific Railroad's financial difficulties played a significant role in excusing a decision not to spend \$250,000 to repair a bridge). However, this factor does not work conversely; the fact that a carrier has sufficient funds to make repairs does not require it to make repairs that are not “financially justified or legally necessary for a money-

losing line that it seeks to abandon” *BBB Lumber* at 9 (holding reasonable CSX Transportation’s embargo of a bridge it would take \$200,000 to repair, when the embargo lasted six months prior to CSX filing a petition for abandonment); *accord Decatur County Comm’rs*, 308 F.3d at 720 (“Limiting the Board only to considerations of present financial capability, however, would not be a sensible policy.”).

Here, CORP’s financial condition does not permit it to make the needed repairs to Tunnels 13, 15, and 18 without financial assistance from other parties (or from its corporate parent or affiliates). CORP’s net operating income for 2007 was approximately . Performing even the short-term repairs recommended by Shannon & Wilson (at a minimum cost of \$2.9 million) would have essentially rendered CORP’s entire operation marginal. Moreover, for the reasons detailed above, those repairs are not financially justified based upon the financial prospects for the Coos Bay Line. Accordingly, this factor does not weigh against the reasonableness of the embargo.<sup>12</sup> *See BBB Lumber* at 9 (CSX not required to spend approximately \$200,000 for bridge repair, even where it clearly could have afforded to do so).

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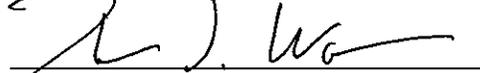
<sup>12</sup> The fact that CORP is controlled by RailAmerica, or that RailAmerica itself is owned by certain investment funds managed by Fortress Investment Group LLC, is irrelevant. The Board does not look to “the financial position of a railroad’s corporate parent or affiliates” when considering the reasonableness of an embargo. *CIND*, at 17 n.31. Moreover, it should be noted that CORP acquired the rail lines at issue as a new carrier under 49 U.S.C. § 10901 and the class exemption set forth at 49 C.F.R. § 1150.31. *See Show Cause Order* at 1 n.1, *citing* ICC Finance Docket No. 32567, *Central Oregon & Pacific R.R., Inc.—Lease, Operation, and Acquisition Exemption—Southern Pacific Transp. Co.* (served Jan. 19, 1995). The ICC and STB have required that new carriers invoking the class exemption must maintain “financial and operational independence” from their corporate parents and affiliates. *See, e.g.*, STB Finance Docket No. 34177, *Iowa, Chicago & Eastern R.R. Corp. – Acquisition and Operation Exemption – Lines of I&M Rail Link*, at 4 (served Jan. 21, 2003). Although a carrier’s parent or affiliate may provide start-up financing or loan guarantees, *id.* at 5 and n.7, the Board has stated that an acquiring carrier using the class exemption must “assume full responsibility for its operating decisions, profits, debts, and risk of loss,” and that a corporate parent “could not subsidize the new subsidiary or accept the financial risk for the ongoing enterprise,” nor could it extend its role “beyond being a mere investor.” *Id.* at 6. In this case, the Board could not require RailAmerica

## CONCLUSION

For the reasons detailed above and in the accompanying Verified Statement of Paul Lundberg and attached Exhibits, the embargo of the Coos Bay Line has not become unreasonable and CORP has not unlawfully abandoned the Coos Bay Line and it should not be required to repair Tunnels 13, 15, and 18 on the line. CORP pledges to file an application seeking abandonment authority at the earliest possible time consistent with the Board's regulations.

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Dated: May 12, 2008

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or other affiliates of CORP to fund the needed tunnel repairs or to subsidize continued operations on the Coos Bay Line without disregarding CORP's separate corporate existence, and its "financial and operational independence" from its corporate parent. Such an order would be inconsistent with the Board's own precedent, and would be wholly unjustified. In any event, the financial position of RailAmerica does not change the economic reality that the Coos Bay Line has large and continuing operating losses that cannot justify repairing and reopening the line without financial assistance.

LUNDBERG

**BEFORE THE  
SURFACE TRANSPORTATION BOARD**

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Central Oregon & Pacific Railroad, Inc. -	)	Finance Docket No. 35130
Coos Bay Rail Line	)	

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**VERIFIED STATEMENT OF PAUL LUNDBERG**

My name is Paul Lundberg. I am Vice President of RailAmerica, Inc. My business address is 5300 Broken Sound Boulevard, Boca Raton, Florida 33487. I joined RailAmerica in February 2007 following the acquisition of RailAmerica by certain investment funds managed by Fortress Investment Group LLC. In my current position, I have responsibility for managing operations and labor relations issues for the RailAmerica carriers, and for RailAmerica's relationships with connecting Class I railroads. RailAmerica is a leading railroad short line holding company with 41 Class II and III railroads located in 25 states and 3 Canadian provinces.

I began my railroad career in 1973 as a brakeman on the Chicago & North Western Transportation Company ("CNW"). During my 22 years with CNW, I held a variety of management positions in labor relations and operations, including Vice President-Labor Relations and Senior Vice President – Transportation. In the latter position, I was responsible for all transportation, commuter operations, equipment management, service design and customer service matters. After leaving CNW following its acquisition by Union Pacific Railroad Company ("UP"), I held senior management positions with SeaLand and Maersk/SeaLand (container shipping) and with Great Lakes Transportation (railroads and shipping). Prior to joining RailAmerica, I was General Manager of the Massachusetts Bay Commuter Railroad, which operates commuter rail services in the Boston area. I hold a

Bachelor of Science in Communications degree from Northwestern University, and a Master of Management degree from Northwestern's Kellogg Graduate School of Management.

The purpose of this Verified Statement is to explain the circumstances that led Central Oregon & Pacific Railroad, Inc. ("CORP") to embargo a portion of its "Coos Bay Line" between Coquille and Richardson, OR on September 21, 2007. As my testimony will show, the embargo was necessitated by unstable conditions in several tunnels on the Coos Bay Line. Weather conditions in Oregon since September have prevented CORP from performing the tunnel repairs that would be required to restore service over the line. Moreover, because the Coos Bay Line has experienced substantial (and increasing) operating losses over the past several years, the expenditure required to undertake such repairs cannot be economically justified. Nevertheless, rather than moving immediately to abandon the Coos Bay Line, CORP attempted over the past several months to persuade interested stakeholders to join CORP in a cooperative effort to rehabilitate the line and to address its ongoing operating losses. The rejection of multiple proposals made by CORP has led us to conclude that such a cooperative effort will not succeed. Accordingly, CORP has (reluctantly) initiated the steps prerequisite to seeking Board approval to abandon the Coos Bay Line.

CORP is a Class II railroad that operates approximately 441 miles of rail lines located generally between Coquille and Eugene, OR and between Eugene, OR and Black Butte, CA. Specifically, CORP owns (1) approximately 219 miles of rail lines between MP 425.3 at Belleview, OR and MP 644.3 at Springfield Junction, OR, and (2) approximately 111 miles of rail lines between MP 652.11 at Danebo, OR and MP 763.13 at Cordes, OR. CORP leases from UP another 103 miles of rail lines located (1) between MP 763.13 at Cordes, OR and MP 786.5 at Coquille, OR; and (2) between MP 425.3 at Belleview, OR and MP 346.0 at Black Butte, CA.

CORP also has trackage rights over eight miles of UP-owned track between Danebo and Springfield Junction, OR. The “Coos Bay Line” consists of the CORP-owned trackage between Danebo and Cordes, OR and the line leased from UP between Cordes and Coquille, OR. (*See* map set forth in Exhibit 1.)

CORP handled a total of 38,691 carloads in 2007, of which only 4,018 carloads moved over the Coos Bay Line. The principal commodities on the portion of the Coos Bay Line subject to the embargo include low value lumber and plywood, pulpwood and bridge components. CORP interchanges traffic with UP at Eugene and Springfield Junction, OR and Black Butte, CA; with Portland & Western Railroad, Inc. (“PNWR”) at Eugene, OR; with WCTU Railway Company at White City, OR; and with Yreka Western Railroad Company (“YWRC”) at Montague, CA.

The rail lines operated by CORP were acquired from UP’s predecessor, the Southern Pacific Transportation Company (“SP”) in 1994. (A copy of the CORP/SP Sale Agreement is set forth in Exhibit 2.) At the time of the acquisition, CORP was owned by shortline operator RailTex, Inc. (“Railtex”). Railtex was subsequently acquired by RailAmerica in January 2002.

Under the terms of a “Cooperative Marketing Agreement” entered into between CORP and SP in connection with the line sale transaction, CORP handles the vast majority of the traffic moving over the Coos Bay Line as a “switching carrier” for UP. *See* Exhibit 3, Cooperative Marketing Agreement, Section 2(a).<sup>1</sup> Under this arrangement, the traffic moves under a UP waybill, and UP has sole authority to determine the rate for the movement (including the portion over CORP’s lines). CORP receives from UP a “Handling Carrier Charge” (currently \$ -

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<sup>1</sup> CORP handles a small volume of “local” traffic to/from points on the Coos Bay Line for its own account, and interchanges a small number of shipments to/from the Coos Bay Line with PNWR. Those shipments (which totaled 932 cars in 2007) are not governed by the Cooperative Marketing Agreement.

per car) for each loaded car that it handles over the Coos Bay Line on UP's behalf. *See* Exhibit 3, Eighth Amendment. The Handling Carrier Charge is adjusted annually by an amount equal to

*See* Exhibit 3, Fourth Amendment, Section 1(a). In addition, CORP receives a fuel adjustment from UP on traffic moving for UP's account. As of the time of the embargo, the fuel adjustment was \_\_\_\_\_, or approximately \_\_\_\_\_ per car.<sup>2</sup>

Thus, unlike Class I railroads (and many shortline carriers), CORP does not control the pricing of the vast majority of the traffic that moves over its lines. Rather, the rates on such shipments are established by (and accrue to) UP, with CORP being paid a fixed fee for handling the traffic to/from UP at Eugene, OR. As a result, CORP does not have the ability to take pricing actions that would generate additional revenue for upgrading or expansion of its rail infrastructure. Indeed, the terms of the Cooperative Marketing Agreement limit annual increases in the Handling Carrier Charge paid to CORP to, at most, \_\_\_\_\_. Such annual increases have not been sufficient to cover fully the increase in normal operating expenses for the Coos Bay Line (much less to fund extraordinary capital improvements).

At the same time, the rugged terrain in which the Coos Bay Line is located makes that line extraordinarily expensive to maintain. Between 2003 and 2007, CORP spent an average of \_\_\_\_\_

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<sup>2</sup> As of April 1, 2008, UP increased this fuel adjustment to CORP to \_\_\_\_\_. In a letter filed in Ex Parte No. 677, *Common Carrier Obligation of Railroads* on April 30, 2008, UP stated that it has "voluntarily agreed to pass along such additional fuel support to CORP." *See* Exhibit 4, Letter dated April 29, 2008 from M. Hemmer to Chairman Nottingham, et al. at 1. The Cooperative Marketing Agreement does not give CORP the unilateral right to increase rates, or to impose surcharges, on traffic that it handles in conjunction with UP. Nor does that arrangement provide for negotiation of the fuel adjustment. Rather, as Exhibit 5 shows, UP essentially dictates to CORP the level of the fuel adjustment. Any increase in the Carrier Handling Charge (other than the annual adjustment based on \_\_\_\_\_) is likewise solely within the discretion of UP.

28 percent of its annual gross freight revenues earned on traffic moving over the Coos Bay Line for normal track, bridge and crossing maintenance on that line. In 2006 (the last full year of operations over the line), the cost of track, bridge and crossing maintenance on the Coos Bay Line consumed \$ 934,000, or 32 percent of the \$2.93 million in gross freight revenues generated by traffic on the line. By comparison, the average cost of maintaining the lines operated by RailAmerica's rail carriers is approximately 13 percent of gross freight revenues.

Notwithstanding the extraordinary cost of maintaining the Coos Bay Line, and CORP's inability to collect market-based rates on traffic moving over the line, the Coos Bay Line was profitable during the first several years of RailAmerica ownership. For example, the Coos Bay Line generated positive operating income of approximately \$235,000 in 2002 and \$552,000 in 2003. However, in 2004, a major shipper on the line, Weyerhaeuser Corporation, ceased operations at its paper manufacturing facility at Cordes, OR. The closure of that plant, which historically generated approximately 3,000 carloads of rail business annually, contributed to a precipitous decline in the total volume of traffic moving over the Coos Bay Line, from 7,574 carloads in 2003 to 5,408 carloads in 2004. As a result, the Coos Bay Line experienced an operating loss of more than \$578,000 in 2004. The spike in fuel prices during 2005 and 2006, coupled with CORP's inability to offset the loss of Weyerhaeuser's business with additional traffic from other sources, exacerbated the problem. The Coos Bay Line experienced operating losses of approximately \$ 939,000 in 2005 and \$1.17 million in 2006. In 2007, the operating loss through September 21 (the date upon which the embargo of the portion of the line between Coquille and Richardson, OR went into effect) was approximately \$792,000.

The viability of the Coos Bay Line was further threatened by the deterioration of several timber-lined tunnels over the past 18 months. In October 2006, a joint inspection of the Coos

Bay Line by the Federal Railroad Administration (“FRA”) and the Oregon Department of Transportation (“ODOT”) revealed significant deterioration in Tunnel No. 15 (located near MP 721). CORP responded promptly to that condition, engaging a contractor to perform repairs to the tunnel. However, while those repairs were being performed in November 2006, Tunnel No. 15 collapsed, resulting in closure of the tunnel for three months. The collapse increased the cost of repairs (initially estimated to cost \$350,000 - \$400,000) to approximately \$1.7 million, and the temporary closure of the tunnel cost CORP an additional \$500,000 in lost freight revenues.

Following that incident, in March 2007, CORP engaged Shannon & Wilson, Inc., a geotechnical and environmental services firm, to evaluate the condition of all nine tunnels on the Coos Bay Line. Shannon & Wilson inspected the tunnels during March and April 2007, and reported their findings to CORP’s engineers on July 16, 2007. (A copy of the Shannon & Wilson report is set forth in Exhibit 6.) Shannon & Wilson identified “severe liner and/or rock deterioration and instability” in Tunnel Nos. 13, 15 and 18. *See* Exhibit 6 at 3. Shannon & Wilson recommended that certain short-term repairs (“Level 1 and Level 2 repairs”) to Tunnel Nos. 13, 15 and 18 be performed within 12 months. *Id.* at 2, 6. Shannon & Wilson advised that “[i]n our opinion, the repairs recommended for tunnel sections that were classified as Repair Level 1 and 2 in our July 2007 report, are necessary to continue relatively safe train passage.” *See*, Exhibit 6, September 21, 2007 Supplement at 2. The estimated cost of such short-term repairs was approximately \$2,861,000. Shannon & Wilson also recommended that CORP perform additional work in the tunnels on the Coos Bay Line within 12-48 months (“Level 3, 4 and 5 repairs”). The total cost of all tunnel work recommended by the Shannon & Wilson report was approximately \$6.7 million. *Id.* at 11, Estimated Construction Cost Summary.

Just before the Shannon & Wilson report was issued in July 2007, another timber set inside Tunnel No. 15 failed. In August, falling rocks inside Tunnel No. 19 required CORP personnel to conduct a detailed inspection of that tunnel from the cab of a locomotive (rather than in a hi-rail vehicle) due to concern that a standard hi-rail truck would not afford them adequate protection in the event of a rock fall. The increasingly hazardous conditions in the tunnels along the Coos Bay Line led CORP management to bring the situation to RailAmerica's attention on September 18-19, 2007. RailAmerica agreed with CORP that the line should be embargoed for safety reasons. On September 21, CORP issued an embargo notice covering the portion of the Coos Bay Line between Coquille and Richardson, OR. *See* Exhibit 7.

FRA concurred with CORP's judgment that the condition of Tunnel Nos. 13, 15 and 18 warranted an embargo the Coos Bay Line. In October, 2007, a team of FRA and FHWA engineers conducted an inspection of Tunnel Nos. 13, 15 and 18, and issued a written report of their findings. (A copy of the FRA Report is set forth in Exhibit 8.) The FRA inspectors "substantially validate[d] the findings documented in the Shannon and Wilson report," and further noted that "some conditions have deteriorated even further during the time since the report was prepared, partly due to the passage of time, and partly because of the onset of the wet season in Oregon in the early fall of 2007." *See* Exhibit 8 at 4. FRA concluded that "[t]hese tunnels are hazardous to train traffic and maintenance operations," and concurred with the repair recommendations set forth in the Shannon & Wilson report. *Id.*

The timing of the tunnel failures made it impossible for CORP to commence repairs immediately following the embargo. As reflected in the FRA report, the onset of the rainy (winter) season in Oregon is generally accompanied by increased seepage in rail tunnels. This condition increases the risk of tunnel instability if timber sets are removed or disturbed, and

(according to Shannon & Wilson) makes the application of shotcrete to surfaces within the tunnels “impossible and hazardous.” *See* Exhibit 6, September 21, 2007 Supplement at 2. Thus, Shannon & Wilson advised CORP that “it may not be safe for much of the repair work to be undertaken until the drier months of next spring and summer.” *Id.* Moreover, given the limited number of contractors who possess the specialized experience required for this work, Tunnel Nos. 13, 15 and 18 would have to be repaired sequentially (rather than at the same time). CORP estimated that the Level 1 and Level 2 repairs recommended by Shannon & Wilson would require approximately four months to complete. Thus, in presenting to interested stakeholders in November 2007 a proposal (discussed below) to preserve service on the Coos Bay Line, CORP predicted that, if tunnel repairs were commenced (weather permitting) on or about May 1, 2008, the line could be reopened no earlier than September 2008.

The cost of the tunnel work identified by Shannon & Wilson (which FRA agreed is necessary) raised serious concern at CORP (and RailAmerica) about the ongoing viability of the Coos Bay Line. With operating losses on the line exceeding \$1 million annually, and with no opportunity for CORP to offset those losses by raising rates or attracting new business to the line, an immediate investment of \$2.9 million to rehabilitate tunnels on the Coos Bay Line cannot be economically justified. If repair activity caused one or more tunnels to collapse, as occurred in 2006, the cost of performing Level 1 and Level 2 repairs to the tunnels would be substantially higher. Moreover, such short-term repairs alone cannot assure the safety of the tunnels on the line; as the Shannon & Wilson report shows, the cost of addressing the deteriorated conditions in Tunnel Nos. 13, 15 and 18 would be nearly \$7 million over the next four years. CORP’s analysis showed that the total cost of restoring the Coos Bay Line to a safe and efficient condition for the long term would be more than \$23 million.

Nevertheless, we were reluctant to simply “throw in the towel” by filing for authority to abandon the line. Instead, we sought to utilize the fall/winter period (during which weather conditions precluded tunnel repairs in any event) to gauge the interest of other stakeholders in a plan to preserve rail service over the Coos Bay Line. During October and November 2007, representatives of RailAmerica and CORP (including RailAmerica CEO John Giles and me) met with shippers, Oregon legislators and ODOT to solicit their participation in a cooperative effort to address both the capital needs of the Coos Bay Line and the ongoing losses generated from CORP’s operations over the line. On October 25, 2007, I addressed the Oregon Senate Interim Committee on Transportation regarding the need for public participation in any plan to preserve service over the Coos Bay Line. On November 14, 2007, we presented a plan for a “public/private partnership” based upon a model that had been successful in preserving service on a RailAmerica-owned shortline in Canada (the Cape Breton & Nova Scotia Railroad). Specifically, CORP proposed that, over a five-year period, CORP, UP, ODOT, the Port of Coos Bay and shippers on the line each contribute \$4.66 million to fund approximately \$23.3 million dollars in capital work to address not only the tunnel repairs recommended by Shannon & Wilson, but also major rehabilitation of track and bridges required to assure safe and efficient operations on the Coos Bay Line. CORP also proposed that ODOT enter into an agreement with CORP to provide an annual subsidy to offset operating losses on the line. From CORP’s perspective, such ongoing participation by the State was critical to preserving service over the Coos Bay Line, because the investment in tunnel and track repairs, standing alone, would do nothing to mitigate the substantial (and growing) operating losses being incurred by CORP. Thereafter, at the Board’s suggestion, CORP and RailAmerica met with interested shippers in Washington, DC on January 14, 2008 to discuss CORP’s proposal.

Unfortunately, the reaction to CORP's initial proposal was not encouraging. At a meeting of interested parties (including Oregon Governor Kulongoski, Representative De Fazio, UP, ODOT and shippers) on January 24, 2008, Governor Kulongoski advised CORP that the State would not participate in a cooperative effort with respect to the Coos Bay Line unless and until CORP itself paid for the tunnel repairs required to reopen the line and recommenced service. He also indicated that the State would require an equity stake in the line in exchange for any financial assistance. In February 2008, Governor Kulongoski rejected a revised partnership proposal from CORP for the same reasons. UP did not respond to CORP's proposals. Shippers viewed the proposals as an attempt by CORP to "extort" from them the cost of repairs that they viewed as CORP's (and RailAmerica's) sole obligation.

Based on these responses to our public/private partnership proposals, CORP developed an alternate plan to preserve service on the Coos Bay Line. On April 9, 2008, CORP presented to Governor Kulongoski a proposal to establish a joint venture between CORP and the State of Oregon. Under that plan, CORP would contribute to the joint venture the rail assets comprising 65 miles of the Coos Bay Line between Vaughn and North Bend, OR, as well as all freight and non-freight revenues generated by that line. The State would contribute funds to restore that segment to a safe and stable operating condition. Going forward, CORP would operate the line on a contract basis on behalf of the joint venture. This proposal was expressly designed to address both Governor Kulongoski's requirement that State financial assistance be coupled with an equity interest in the line, and CORP's need for a plan that addressed not only the immediate capital requirements of the Coos Bay Line but also the ongoing losses from operations.

On April 21, 2008, Governor Kulongoski wrote a letter to me, in which he rejected CORP's revised joint venture proposal. (A copy of that letter is set forth in Exhibit 9.) Governor

Kulongoski reiterated the State's "bottom line" position that it would not entertain any proposal to address the Coos Bay Line's economic problems until CORP repaired the tunnels (at its sole expense) and recommenced service on the line. Stating his opinion that CORP has a "legal obligation" to repair the tunnels and restore service, Governor Kulongoski concluded that "[y]our choice seems clear: either re-open the line or seek abandonment." A few days later, at the hearing held by the Board to consider issues relating to the "common carrier obligation," UP's Vice President – Law, Mr. Hemmer, stated unequivocally that UP is not interested in participating financially in CORP's proposals to preserve the Coos Bay Line. (Mr. Hemmer's statement was the first response by UP to CORP's proposals.) In a subsequent letter to the Board dated April 29, 2008, Mr. Hemmer expressed UP's "external perspective" that "the Coos Bay Line has generated insufficient traffic to support reinvestment in the line" so that "private entities are unlikely to recover any return on investment in the line." *See* Exhibit 4 at 2.

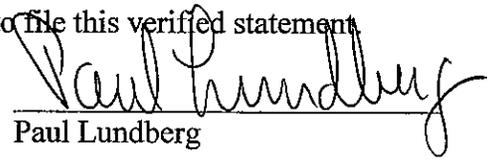
CORP is disappointed by the response to its good faith efforts to preserve service over the Coos Bay Line. The State of Oregon's insistence that CORP incur the full cost of repairing Tunnel Nos. 13, 15 and 18 before the State will even participate in discussions regarding the future of the Coos Bay Line places CORP in the untenable position of being required to invest a minimum of \$3 million in a line that is currently losing more than \$1 million annually, without any assurance that doing so will result in a viable plan to preserve service on the line. UP's outright refusal to contribute to a long-term solution for the Coos Bay Line indicates that UP is not concerned by the prospect of losing the traffic generated by shippers on the line (who are UP's customers). The Port of Coos Bay's response to CORP's proposal is likewise disappointing in light of its statement that continued rail service is important for the potential future development of the port as a container facility.

Upon assessing these reactions to our efforts to build a coalition to address the long-term viability of the Coos Bay Line – and, in particular, after seeing both the State of Oregon and UP unequivocally reject our proposals – CORP made a decision following the hearings in *Ex Parte No. 677* on April 24-25, 2008 to seek to abandon the Coos Bay Line. On May 8, 2008, CORP amended its system diagram map classifying the Coos Bay Line in Category 1. We have instructed our counsel to file the required notice of abandonment and a formal application seeking authority to abandon the Coos Bay Line at the earliest time permitted under the Board's regulations. While CORP remains willing to work with interested stakeholders to discuss solutions that would permit continued operation of the Coos Bay Line, we simply cannot justify investing many millions of dollars to rehabilitate a line that shows little (if any) prospect for returning to profitability.

VERIFICATION

I, Paul Lundberg, declare under penalty of perjury that the foregoing is true and correct.

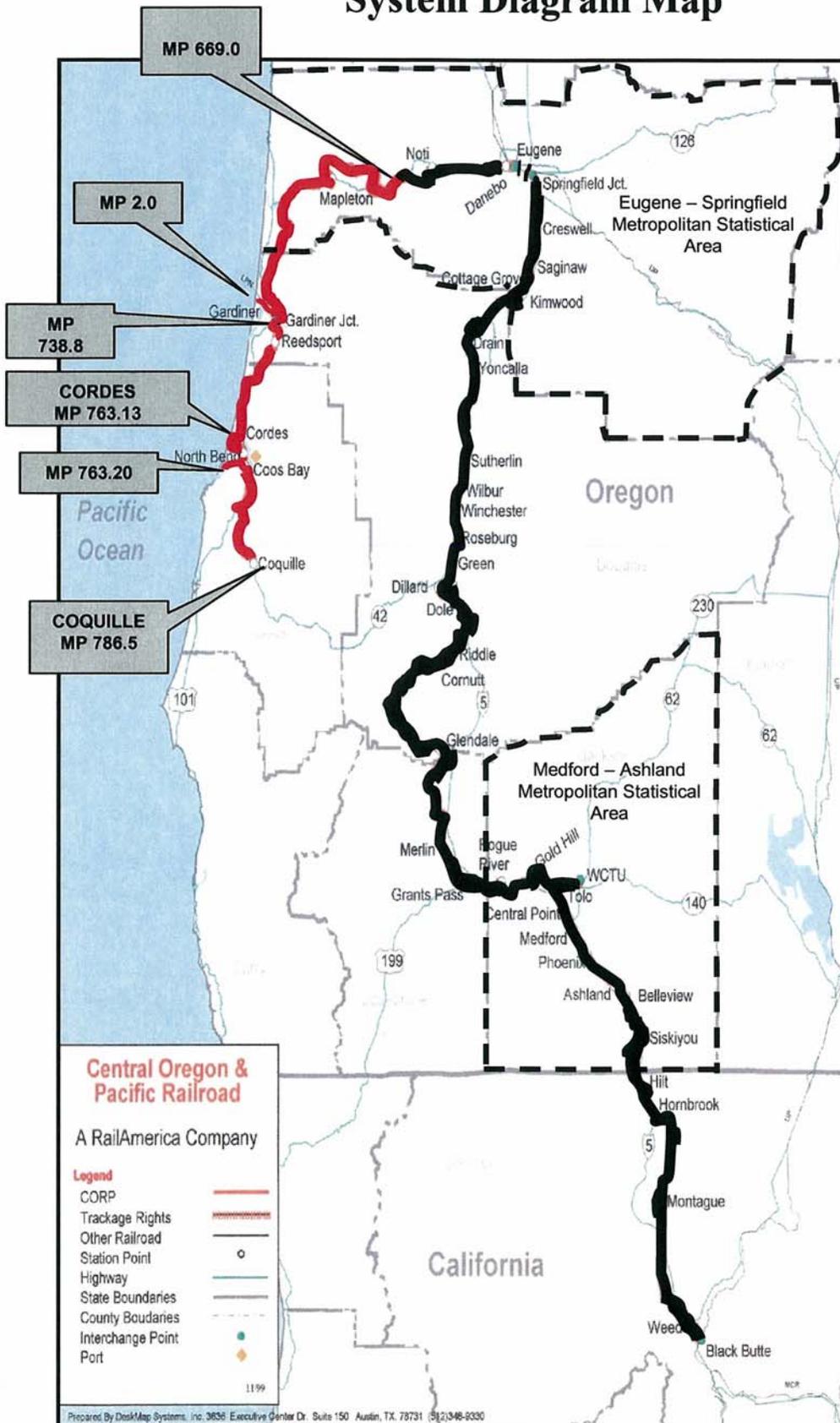
Further, I certify that I am qualified and authorized to file this verified statement.

  
Paul Lundberg

Executed on 8 May, 2008.



# Central Oregon & Pacific Railroad System Diagram Map



**CORP Category 1**  
 (Coos Bay Subdivision  
 Milepost 669.0 to  
 Coquille Milepost 786.5  
 LPN Milepost 2.0 to  
 Milepost 738.8 and  
 Port of Coos  
 Bay North Spit  
 Rail Spur  
 Milepost 763.20)  
**CORP Category 5**

**Central Oregon & Pacific Railroad**  
 A RailAmerica Company

**Legend**

- CORP
- Trackage Rights
- Other Railroad
- Station Point
- Highway
- State Boundaries
- County Boundaries
- Interchange Point
- Port

1199

Prepared By DeskMap Systems, Inc. 3636 Executive Center Dr. Suite 150 Austin, TX. 78731 (512)346-9330



**REDACTED**



**REDACTED**





J. Michael Hemmer  
Senior Vice President - Law & General Counsel

April 29, 2008

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BOARD  
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OFFICE OF CHAIRMAN  
NOTTINGHAM

By UPS Next Day Air

The Honorable Charles D Nottingham, Chairman  
The Honorable Francis P Mulvey, Vice Chairman  
The Honorable W Douglas Buttrey, Commissioner  
Surface Transportation Board  
395 E Street, SW  
Washington, DC 20423

Re STB Ex Parte No 677 - Common Carrier Obligation of Railroads

Dear Chairman Nottingham, Vice Chairman Mulvey, and Commissioner Buttrey

During your hearing in Ex Parte No 677 on April 25, 2008, a representative from RailAmerica provided inaccurate information about UP's economic relationship with the Central Oregon & Pacific Railroad. RailAmerica stated that UP's compensation to CORP consists of \$400 per car, plus 50 percent of RCAF-U adjustments up to a maximum of 3 percent annually. That information is not correct.

UP's compensation to CORP is currently about \$600 per car, not \$400 per car. As fuel prices have escalated, Union Pacific has voluntarily agreed to pass along additional fuel support to CORP. In addition, Union Pacific provides CORP a 3 percent supplement for reporting car movements through Railinc, which improves interline operations and information for customers.

Union Pacific has also given CORP approximately \$1 million since 2004 to help it repair tunnels on the Siskiyou line and maintain a key bridge on the Coos Bay line.

CORP also complained that its contract with Union Pacific limits the amount it can charge its shippers. In fact, CORP has unilaterally imposed surcharges on its shippers and is proposing additional surcharges without objection from Union Pacific.

Finally, while this does not represent compensation to CORP, during the Coos Bay line service interruption, Union Pacific has provided significant financial support to CORP customers who lack rail service, so that those customers can use transload services on Union Pacific.

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MAY 2 2008  
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in record

From our external perspective, the basic problem facing the Coos Bay line is that, since several major customers closed large shipping facilities on the line in the 1990s, the Coos Bay line has generated insufficient traffic to support reinvestment in the line. Accordingly, as I testified on April 24, 2008, private entities are unlikely to recover any return on investment in the line, unless traffic volumes increase substantially.

Respectfully,

A handwritten signature in cursive script that reads "Mike Hemmer".

J Michael Hemmer

cc: All Participants *(by US first-class mail)*



April 1, 2008

Dear Short Line Connection:

In UP's letter of December 10, 2004 we announced the initiation of a fuel surcharge program applicable to our short line handling carrier connections. This letter confirms our intent to continue this program during the Second Quarter 2008 and provides information on the surcharge rate for that period.

**Fuel Surcharge Percentage Amounts**

The handling carrier fuel surcharge for the Second Quarter 2008 will be \_\_\_\_\_ This amount will apply on each loaded car interchanged with Union Pacific on or after April 1, 2008 on which you receive a handling carrier division. Exceptions to application of the fuel surcharge are noted below.

**Fuel Surcharge Exceptions**

The fuel surcharge will NOT apply on the following situations:

1. Any unit train movements (typically coal, rock, or grain) where UP supplies the locomotive power and fuel,
2. Switch charges or haulage rates,
3. Intermodal traffic,
4. The fuel surcharge program will apply only to handling carrier divisions. Any junction settlement divisions are excluded from the program.
5. Any situation where a handling carrier has in place or imposes a direct fuel surcharge on customers of Union Pacific which move under handling carrier arrangements. It is important to understand that this exception applies to any surcharge imposed by the handling carrier on Union Pacific moves, whether on all moves or simply a portion of the UP traffic. This is an all or nothing situation. If the handling carrier applies a surcharge on any UP handling carrier traffic the UP surcharge program will not apply on any of the business interchanged with that carrier.
6. The fuel surcharge program no longer applies to those carriers who, although handling carriers, have independent authority to adjust their divisions, unless:
  - a. Those carriers notify Union Pacific that for duration of the fuel surcharge program they will waive the right to unilaterally adjust their divisions, and,
  - b. They agree to "roll back" any division increases unilaterally announced since January 1, 2005.

Union Pacific reserves the sole right to add such other exclusions or conditions as we believe to be necessary.

**Fuel Surcharge Invoices – Policy Considerations**

1. It will be your responsibility to calculate and apply the surcharge on a per carload basis starting with your invoices to Union Pacific for traffic interchanged to or from UP on and after January 1, 2008. We request that you do not issue invoices which span First Quarter 2008 and 2nd Quarter 2008 or which include traffic moved in both Quarters. On your invoices for each claimed car please show the total amount billed for that car; that is, your division increased by the surcharge. You may also include the division and the surcharge amount separately if you wish, but it is no longer a requirement to do so. The invoice should also include the statement "fuel surcharge has been applied before submission". For example, if your handling carrier division is \$300 per carload on April 1, 2008 you should submit a bill showing a billed

amount of \_\_\_\_\_ with a statement that the fuel surcharge has been applied before submission. This amount will be the amount paid to you by Union Pacific.

2. Fuel surcharge amounts have not and will not be paid retroactively. They must be shown on the original invoice for the time period being billed. Once an invoice is processed for payment by Union Pacific without the fuel surcharge it cannot be subsequently requested for the cars on that bill. Bottom line - if the fuel surcharge is omitted, then it is lost.

3. Fuel surcharge amounts will only be paid to the penny, not to amounts smaller than a penny. For example, if your handling carrier division is \_\_\_\_\_ per car, the fuel surcharge amount should be computed as \_\_\_\_\_. On your invoice, this should be adjusted to \_\_\_\_\_ by dropping all decimal amounts smaller than one penny.

We are well aware that there may be specific circumstances not fitting the patterns outlined above. Should you encounter these situations please contact your Union Pacific short line representative and they can coordinate a response to determine whether, or to what extent, the program will be applicable.

### **STB Fuel Surcharge Ruling**

In February 2007 the STB ruled that a fuel surcharge computed as a percentage of price to the customer was an unreasonable practice. As such, the Class I rail carriers have begun, in the Second Quarter 2007, and continuing at least through the Third Quarter 2007, to convert their customer fuel surcharge programs to ones which comply with the new STB guidelines. The ruling does not affect payments of fuel surcharges by Class I's to other entities, such as short lines. Thus, Union Pacific intends, at this time, to continue the current fuel surcharge program for short lines as it is presently structured. When new customer programs have been implemented, we will make adjustments, if necessary, to the short line program. Like the present program these will be designed to insure that, going forward, short lines remain compensated at levels commensurate with Union Pacific's fuel surcharge application and collection rates. It is our intent that, to the extent possible, short lines will not be disadvantaged by changes in customer programs caused by the STB ruling. We will keep you informed as additional information becomes available.

### **Summary**

This program is at UP's sole discretion and can end at anytime, but will certainly end when the applicable fuel surcharge falls below the RCAF-U recovery rate or when the UP fuel surcharge ceases to exist. The handling carrier fuel surcharge program may also be modified at any time to conform to changes in the structure of Union Pacific's customer fuel surcharge program.



July 16, 2007

Mr. Marc Bader, Chief Engineer  
Rail America Operations West  
One Harbor Center Drive, Suite 340  
Suisun City, CA 94585

**RE: TUNNEL INVENTORY – COOS BAY SUBDIVISION, OREGON**

Dear Mr. Bader:

This report documents our observations and opinions regarding the condition of nine tunnels in the Coos Bay Subdivision, and our engineer's preliminary estimate of costs for construction of short- and long-term rehabilitation work. Rail America does not seek any clearance improvement in the tunnels at this time; therefore, it was not considered in any of our recommended repairs and structural improvements in this report. Maintenance or repairs of track structure or drainage conditions within the tunnels were also not included in our assessment, but poor track and drainage conditions were noted on our log forms. General data on the condition of the existing tunnel conditions and supports, suggested methods for repairs and maintenance, and estimated rehabilitation costs are presented in Tables 1 through 10. Our engineer's estimate of tunnel rehabilitation costs is summarized separately in Table 11.

The tunnel inventory was authorized by Mr. Marc Bader, Chief Engineer of Rail America Operations West, on March 12, 2007. Shannon & Wilson, Inc. conducted the mapping and assessment of the tunnels between March 26 and 30, 2007. Rail America provided flagging services and designated a railroad employee to escort and provide access via hy-rail to the Shannon & Wilson, Inc. field crew during the tunnel visits.

We visited and logged Tunnels 16 and 21 on March 26. On March 27, our project manager, Red Robinson, joined the crew and we logged Tunnels 14 and 20 and briefly visited Tunnel 13. We mapped Tunnel 13 on March 28, and we assessed Tunnels 17 and 19 on March 29. We

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Mr. Marc Bader, Chief Engineer  
Rail America Operations West  
July 16, 2007  
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SHANNON & WILSON, INC

completed the mapping with Tunnel 18 on the March 30. Tunnel 15 had been previously logged during the rehabilitation of a severely deteriorated and partially caved portion of the tunnel in November 2006. We revisited Tunnel 15 on July 9, 2007, to observe ground conditions and timber rib conditions adjacent to a recently collapsed timber rib at around Station 3+30.

During our logging process, we noted the nature and condition of the tunnel support system and the condition and stability of the rock, where visible. The condition of the tunnel supports and rock was prioritized according to the need for repair. In our opinion, portions of the tunnels that are in need of immediate repair within six months are classified as Repair Level 1. Repair Level 2 applies to portions of the tunnels that should be repaired within the next 12 months. Repair Level 3 applies to portions of the tunnels that should be repaired in the next 12 to 30 months. Repair Level 4 applies to portions of the tunnels that should be completed in the next 30 to 48 months. Repair Level 5 applies to portions of the tunnels that are not in need of repairs within the next 48 months, based on the current conditions; however, changes in groundwater flows into the tunnel, drainage, and general time-related deterioration of the tunnel lining or rock could lead to future needs for repair. The conditions of the tunnels should be reassessed every few years and during the various repair phases.

The only documentation available for review prior to our site visit and tunnel evaluation and the preparation of this report was in-house copies of the "Central Oregon Pacific Railroads Tunnel Inspection Report – Siskiyou and Coos Bay Branch," a report prepared by Shannon & Wilson, Inc. dated March 1994. This report also included typical drawings of timber sets and gunite/shotcrete lining.

### **GENERAL CONDITION OF THE TUNNELS**

Based on available documents, the original tunnel construction took place in the 1880s. Excavation was by drill-and-blast, with local support provided by timber sets, wood lagging, and portal structures. Continuous timber sets as support, along with concrete portal structures, were

Mr. Marc Bader, Chief Engineer  
Rail America Operations West  
July 16, 2007  
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established between 1910 and the 1920s. Only the South portal of Tunnel 14 and the North portals of Tunnel 18 and Tunnel 19 are lined with shotcreted steel sets.

Anticipated lifespan for cedar timber tunnel supports is normally on the order of 50 years. Most of the timber supports in the Coos Bay tunnels have likely been in place for well over 50 years, possibly up to 95 years. However, where the timber ribs and lagging have remained dry, they are still in fairly good shape and may provide adequate support to the rock. Where groundwater is seeping from the rock and through the lining, or where the bottoms of the sets are standing in poorly drained and/or muddy drainage ditches or on low concrete footing walls where debris has accumulated and holds the groundwater, the timber supports have undergone various levels of decay. In some instances, decay is limited to only the lower 1 to 2 feet of the posts. Elsewhere, the decay is more pervasive and has penetrated the entire lining for several ribs in a row.

The significant effort required to maintain the timber lining led one of the previous owners of the Coos Bay branch, the Southern Pacific Railroad, to a program of replacing timber sets with steel sets covered with gunite in the 1970s and early 1980s. Tunnels 14, 19, and 20, with relatively stable rock conditions, were supported with only a thin layer (1 to 4 inches) of gunite after the removal of the timber lining. It appears that the timber lining in Tunnel 21 was removed more recently, possibly after a tunnel fire, and steel fiber-reinforced shotcrete was used to support the tunnel. At present, approximately 1,207 feet of timber lining remains in place in Tunnel 13, 1,073 feet in Tunnel 15, 417 feet in Tunnel 17, and 622 feet in Tunnel 18.

#### **SHORT-TERM OR IMMEDIATE (REPAIR LEVELS 1 AND 2) REHABILITATION REQUIREMENTS**

Indications of severe liner and/or rock deterioration and instability requiring immediate repair (Repair Levels 1 and 2) were observed at several locations in the timber-lined sections of Tunnels 13, 15, and 18, where the timber sets are heavily decayed, crushed, and/or offset. We also observed rockfall hazards at several locations in Tunnels 13 and 15, where timber sets were removed and replaced with steel sets, but the timber lagging was left in place and has now

Mr. Marc Bader, Chief Engineer  
Rail America Operations West  
July 16, 2007  
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deteriorated and rotted away. In addition, we identified rockfall hazards in two, short, unlined sections, also in Tunnel 13. Because of evident recent rockfalls, we strongly recommend immediate repairs in these areas as well.

Because of the potential for rockfalls and tunnel collapse during removal and replacement of the timber sets, as experienced in a short portion of Tunnel 15, we recommend that grouted rock bolts be installed through the timber liner, and then the timber ribs be removed one rib at a time and replaced with either shotcrete or steel ribs, as shown in the tables.

#### **LONG-TERM (REPAIR LEVELS 3 THROUGH 5) REHABILITATION REQUIREMENTS**

The majority of the long-term rehabilitation requirements are related to the removal and the replacement of timber sets, wood foot blocks, and timber lagging, and re-lining with steel fiber-reinforced shotcrete and rock bolts (Tunnels 13, 15, 17, and 18). The timber support in these sections of tunnel is at various stages of deterioration; consequently, isolated timber ribs could loosen and fail at any time. This also includes sections in Tunnel 13 where timber lagging was left in place after timber sets were replaced with steel sets. Rehabilitation work is also required in unlined sections and in areas with exposed bedrock and spalling shotcrete, some of them associated with apparent rockfall activity. These conditions were observed to various extents in Tunnels 13, 14, 15, 19, 20, and 21.

Recommended repairs include the application of steel fiber-reinforced shotcrete. Additional support with rock bolts is required at some locations. Typically, we recommend protecting and supporting unlined sections immediately. We designated these areas for long-term rehabilitation requirements based on our visual observation of the bedrock conditions and the fact that they have apparently been stable over some period of time. However, there is always a risk of sudden rockfalls in unlined sections or areas with only thin shotcrete/gunite cover, and if a rockfall condition develops immediate support may be needed.

Mr. Marc Bader, Chief Engineer  
Rail America Operations West  
July 16, 2007  
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An isolated rockfall occurred in Tunnel 19 roughly between Stations 35+60 and 36+00 in May 2007. A site visit was conducted on June 4, 2007, to assess the conditions. This section of the tunnel had experienced spalling in the past of thin shotcrete in the crown, and bedrock is exposed currently. At this location, the installation of additional ground support (shotcrete and, potentially, some rockbolts) may be considered at an earlier time than indicated on the summary table, and could be included during more urgent repair works in the adjacent Tunnel 18 (see above).

In Tunnel 20, which is generally lined with thin, 1- to 4-inch-thick, gunite, a 20-foot-long and a 44-foot-long section are lined with shotcreted steel sets at 3- to 4-foot spacing. Exposed bedrock above the steel sets indicates past over-break and rockfall activity in these areas, which requires remedial support. Currently, the shotcreted steel sets function as a canopy and protect the track from falling rocks to some extent, but they do not support the actively raveling rock above.

We did not include several tunnel sections lined with good-quality, sound timber in our rehabilitation program (657 feet in Tunnel 13, 745 feet in Tunnel 15, 373 feet in Tunnel 17, and 62 feet in Tunnel 18). The current conditions of timber sets, timber lagging, and wood foot blocks in these areas are generally fair to good, and we estimate a remaining average lifespan of approximately 5 to 10 years, or more. At Tunnel 15, the timber-lined sections also include areas where shotcrete was applied between the existing timber sets in order to maintain bedrock stability during repair work that was conducted in adjacent areas. However, the timber will deteriorate over time and may cause problems in these sections in the future. At locations where wood foot blocks are used to support timber sets, poor maintenance of drainage ditches can lead to rotting of the timber sets and shorten their lifespan significantly. Replacing the timber lining with rockbolts and steel fiber-reinforced shotcrete is recommended in the future in these sections in order to maintain the long-term stability of the tunnel.

We also observed several sections in Tunnel 13 where timber sets were replaced with steel sets followed by an application of shotcrete, which was applied over timber lagging that was left in

Mr. Marc Bader, Chief Engineer  
Rail America Operations West  
July 16, 2007  
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SHANNON & WILSON, INC.

place. Based on our observations, we expect void spaces of various dimensions (potentially up to 5 feet deep) behind the existing lining in these sections. Backfilling the voids with cement-based material in the future will increase the structural long-term stability of the lining and reduce the potential fire hazard of the remaining timber lagging behind the shotcrete.

Had we included in our proposed rehabilitation work the removal and re-lining of all timber-lined sections and the backfilling of void spaces behind the existing shotcrete-over-steel-sets lining, and added the shotcrete quantity needed to increase the thickness of gunite-lined sections, the total construction costs would have increased on the order of roughly \$12,000,000.

#### SUMMARY

Immediate tunnel stability problems are related to the progressively and intensely deteriorated and rotted condition of timber in timber-lined sections in Tunnels 13, 15, and 18 and unlined sections with associated rockfall hazard in Tunnel 13. We recommend relining and supporting these areas with steel fiber-reinforced shotcrete, rockbolts, and steel ribs, as indicated in the tables. We estimate the total construction costs for the Repair Levels 1 and 2 to be in the order of \$2,865,000.

Long-term rehabilitation work—within the next 1 to 5 years—is required in almost all of the tunnels (except Tunnel 16) and, in general, includes the relining and supporting of tunnel sections with steel fiber-reinforced shotcrete, rockbolts, and/or steel ribs, as shown in the tables. We estimate the total construction costs for the later repairs (Levels 3 to 5) to be around \$3,815,000.

We would be pleased to submit a detailed proposal for the engineering design work and the preparation of construction plans and specifications for your next phase of repair work on the Coos Bay Tunnels.

Mr. Marc Bader, Chief Engineer  
Rail America Operations West  
July 16, 2007  
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SHANNON & WILSON, INC.

We appreciate the opportunity to work with you and look forward to answering any questions you have about the information in this report.

Sincerely,

**SHANNON & WILSON, INC.**

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Klaus G. Winkler  
Senior Engineering Geologist

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Robert A. Robinson, L.E.G., L.G.  
Senior Vice President  
Director of Underground Services

Roberto J. Guardia, P.E.  
Vice President

KGW:RJG:RAR/kgw

Enclosures: Table 1 – List of Tunnels – Coos Bay Subdivision  
Table 2 – Tunnel 13 (4 pages)  
Table 3 – Tunnel 14  
Table 4 – Tunnel 15 (3 pages)  
Table 5 – Tunnel 16  
Table 6 – Tunnel 17 (2 pages)  
Table 7 – Tunnel 18 (2 pages)  
Table 8 – Tunnel 19 (2 pages)  
Table 9 – Tunnel 20  
Table 10 – Tunnel 21  
Table 11 – Estimated Construction Cost Summary  
Important Information About Your Engineering Report



Date: July 16, 2007  
To: Mr. Marc Bader, Chief Engineer  
Rail America Operations West

## **IMPORTANT INFORMATION ABOUT YOUR GEOTECHNICAL/ENVIRONMENTAL REPORT**

### **CONSULTING SERVICES ARE PERFORMED FOR SPECIFIC PURPOSES AND FOR SPECIFIC CLIENTS.**

Consultants prepare reports to meet the specific needs of specific individuals. A report prepared for a civil engineer may not be adequate for a construction contractor or even another civil engineer. Unless indicated otherwise, your consultant prepared your report expressly for you and expressly for the purposes you indicated. No one other than you should apply this report for its intended purpose without first conferring with the consultant. No party should apply this report for any purpose other than that originally contemplated without first conferring with the consultant.

### **THE CONSULTANT'S REPORT IS BASED ON PROJECT-SPECIFIC FACTORS.**

A geotechnical/environmental report is based on a subsurface exploration plan designed to consider a unique set of project-specific factors. Depending on the project, these may include: the general nature of the structure and property involved; its size and configuration; its historical use and practice; the location of the structure on the site and its orientation; other improvements such as access roads, parking lots, and underground utilities; and the additional risk created by scope-of-service limitations imposed by the client. To help avoid costly problems, ask the consultant to evaluate how any factors that change subsequent to the date of the report may affect the recommendations. Unless your consultant indicates otherwise, your report should not be used: (1) when the nature of the proposed project is changed (for example, if an office building will be erected instead of a parking garage, or if a refrigerated warehouse will be built instead of an unrefrigerated one, or chemicals are discovered on or near the site); (2) when the size, elevation, or configuration of the proposed project is altered; (3) when the location or orientation of the proposed project is modified; (4) when there is a change of ownership; or (5) for application to an adjacent site. Consultants cannot accept responsibility for problems that may occur if they are not consulted after factors which were considered in the development of the report have changed.

### **SUBSURFACE CONDITIONS CAN CHANGE.**

Subsurface conditions may be affected as a result of natural processes or human activity. Because a geotechnical/environmental report is based on conditions that existed at the time of subsurface exploration, construction decisions should not be based on a report whose adequacy may have been affected by time. Ask the consultant to advise if additional tests are desirable before construction starts: for example, groundwater conditions commonly vary seasonally.

Construction operations at or adjacent to the site and natural events such as floods, earthquakes, or groundwater fluctuations may also affect subsurface conditions and, thus, the continuing adequacy of a geotechnical/environmental report. The consultant should be kept apprised of any such events, and should be consulted to determine if additional tests are necessary.

### **MOST RECOMMENDATIONS ARE PROFESSIONAL JUDGMENTS.**

Site exploration and testing identifies actual surface and subsurface conditions only at those points where samples are taken. The data were extrapolated by your consultant, who then applied judgment to render an opinion about overall subsurface conditions. The actual interface between materials may be far more gradual or abrupt than your report indicates. Actual conditions in areas not sampled may differ from those predicted in your report. While nothing can be done to prevent such situations, you and your consultant can work together to help reduce their impacts. Retaining your consultant to observe subsurface construction operations can be particularly beneficial in this respect.

#### **A REPORT'S CONCLUSIONS ARE PRELIMINARY.**

The conclusions contained in your consultant's report are preliminary because they must be based on the assumption that conditions revealed through selective exploratory sampling are indicative of actual conditions throughout a site. Actual subsurface conditions can be discerned only during earthwork; therefore, you should retain your consultant to observe actual conditions and to provide conclusions. Only the consultant who prepared the report is fully familiar with the background information needed to determine whether or not the report's recommendations based on those conclusions are valid and whether or not the contractor is abiding by applicable recommendations. The consultant who developed your report cannot assume responsibility or liability for the adequacy of the report's recommendations if another party is retained to observe construction.

#### **THE CONSULTANT'S REPORT IS SUBJECT TO MISINTERPRETATION.**

Costly problems can occur when other design professionals develop their plans based on misinterpretation of a geotechnical/environmental report. To help avoid these problems, the consultant should be retained to work with other project design professionals to explain relevant geotechnical, geological, hydrogeological, and environmental findings, and to review the adequacy of their plans and specifications relative to these issues.

#### **BORING LOGS AND/OR MONITORING WELL DATA SHOULD NOT BE SEPARATED FROM THE REPORT.**

Final boring logs developed by the consultant are based upon interpretation of field logs (assembled by site personnel), field test results, and laboratory and/or office evaluation of field samples and data. Only final boring logs and data are customarily included in geotechnical/environmental reports. These final logs should not, under any circumstances, be redrawn for inclusion in architectural or other design drawings, because drafters may commit errors or omissions in the transfer process.

To reduce the likelihood of boring log or monitoring well misinterpretation, contractors should be given ready access to the complete geotechnical engineering/environmental report prepared or authorized for their use. If access is provided only to the report prepared for you, you should advise contractors of the report's limitations, assuming that a contractor was not one of the specific persons for whom the report was prepared, and that developing construction cost estimates was not one of the specific purposes for which it was prepared. While a contractor may gain important knowledge from a report prepared for another party, the contractor should discuss the report with your consultant and perform the additional or alternative work believed necessary to obtain the data specifically appropriate for construction cost estimating purposes. Some clients hold the mistaken impression that simply disclaiming responsibility for the accuracy of subsurface information always insulates them from attendant liability. Providing the best available information to contractors helps prevent costly construction problems and the adversarial attitudes that aggravate them to a disproportionate scale.

#### **READ RESPONSIBILITY CLAUSES CLOSELY.**

Because geotechnical/environmental engineering is based extensively on judgment and opinion, it is far less exact than other design disciplines. This situation has resulted in wholly unwarranted claims being lodged against consultants. To help prevent this problem, consultants have developed a number of clauses for use in their contracts, reports and other documents. These responsibility clauses are not exculpatory clauses designed to transfer the consultant's liabilities to other parties; rather, they are definitive clauses that identify where the consultant's responsibilities begin and end. Their use helps all parties involved recognize their individual responsibilities and take appropriate action. Some of these definitive clauses are likely to appear in your report, and you are encouraged to read them closely. Your consultant will be pleased to give full and frank answers to your questions.

The preceding paragraphs are based on information provided by the  
ASFE/Association of Engineering Firms Practicing in the Geosciences, Silver Spring, Maryland

**LIST OF TUNNELS - Coos Bay Subdivision**

Tunnel No.	MP @ N. Portal	Length	Tunnel Liner	Condition	Comments	Curve
13	669.47	2496 ft	Timber sets, shotcreted steel sets, steel sets with timber lagging, 100 ft unlined, 55 ft. concrete portal barrels	Poor - Good	Rotting timber sets and lagging	tangent/ 8°
14	681.09	471 ft	Shotcreted steel sets, shotcreted bedrock, 50 ft. N. portal concrete barrel	Good	Thin shotcrete, cracking and spalling	8°
15	720.73	2,143 ft	Shotcrete over steel and timber sets, timber sets and lagging, N. & S. portal are 50 ft. long concrete barrels	Poor - Good	Rotting timber sets and lagging, several cave-ins, recent repair work	tangent
16	721.52	633 ft	Shotcrete over timber and steel sets, N. & S. portal are 50 ft. long concrete barrels	Good		7°
17	727.7	1,200 ft	Shotcrete over bedrock, timber sets, shotcreted steel sets, N. & S. portal concrete barrels	Poor - Good	Timber sets with rotting foot blocks, offsets, cracks in shotcrete	tangent/ 2°
18	734.48	1,580 ft	Shotcrete over steel and timber sets, timber sets and lagging, N. & S portal are 50 ft. long concrete barrels	Poor - Good	Timber sets with rotting foot blocks, offsets, cracks in shotcrete	tangent
19	745.62	4,202 ft	Shotcrete over bedrock, shotcrete over steel sets, S. portal 50 ft concrete barrel	Fair - Good	Landslides over both portals, shotcrete thin and cracking, bedrock exposed	tangent/ 6°
20	750.1	874 ft	Shotcrete over bedrock, shotcrete over steel sets, S. portal 50 ft concrete barrel	Fair	Large areas of spalling shotcrete with exposed bedrock	2°
21	751.2	478 ft	Shotcrete over bedrock, S. portal are 50 ft. long concrete barrels	Good		4°

**Total Length 11,581 ft**



September 21, 2007

Mr. Marc Bader, Chief Engineer  
Rail America Operations West  
One Harbor Center Drive, Suite 340  
Suisun City, CA 94585

**RE: TUNNEL CONDITION ASSESSMENT FOR COOS BAY SUBDIVISION,  
OREGON**

Dear Mr. Bader:

As discussed in recent phone conversations, this letter is to provide you with our concerns regarding the current conditions and potential for rock falls, and timber rib failures in the nine tunnels on the Coos Bay Subdivision of the Central Oregon and Pacific Railroad.

As stated and described in detail in our tunnel inventory report dated July 2007, we identified and classified numerous sections in the tunnels, that are in various states of deterioration and, in our opinion, require immediate rehabilitation work (within six months) in order to reduce the currently high risk of rock falls and timber collapses to more acceptable levels. Some of the areas – particularly in Tunnel 15 and Tunnel 18, were identified and discussed with you as early as November 2006, when emergency repairs were initiated in Tunnel 15. We also identified numerous other areas in the tunnels that need repairs, but based on our field investigations did not appear to be in as great a risk of failure, and therefore were not classified as being in need of immediate repair, although we did consider that they should be repaired within the next year or so.

Mr. Marc Bader, Chief Engineer  
Rail America Operations West  
September 21, 2007  
Page 2

SHANNON & WILSON, INC.

Since November 2006, several rock falls and failed timber sets were observed in tunnels in the Coos Bay Subdivision:

- Several partially collapsed timber sets were observed in Tunnel 15 during emergency repairs from November 2006 to January 2007.
- Six timber posts in the west sidewall of Tunnel 18 shifted into the tunnel. The posts rested on deteriorated wooden foot blocks.
- Several rock falls occurred in Tunnel 19 between May and July 2007. Rock falls occurred in areas of spalled shotcrete and exposed bedrock.
- Failure of a timber set occurred in Tunnel 15 in June 2006. The timber set was highly deteriorated.

In our opinion, the repairs recommended for tunnel sections that were classified as Repair Level 1 and 2 in our July 2007 report, are necessary to continue relatively safe train passage. Recent rock fall events in Tunnel 19 require immediate attention as well. The risk of future rock falls and failing timber sets is high under the current condition of the tunnels. However, the increased seepage rate in some areas of the tunnels that normally accompanies the rainy season will contribute to an increased risk of instability and also makes the application of remedial shotcrete in these seepage areas impossible and hazardous. Consequently, it may not be safe for much of the repair work to be undertaken until the drier months of next spring and summer.

We appreciate the opportunity to work with you and look forward to answering any questions you have about the information in this report.

Sincerely,

SHANNON & WILSON, INC.



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Robert A. Robinson  
Senior Vice President  
Director of Underground Services

21-1-20713-001



**Print Embargo**

CORP-CENTRAL OREGON &amp; PACIFIC RAILROAD INC

Embargo Number: CORP000107

Amendment Number: 3

Status: Effective

Companion Embargo Number: None

Effective Date: 09-21-2007

Expiration Date: 09-21-2008

Allow Permit: Yes

Tier 2 Effective Date: 09-21-2007

Permit Officer : Don Taylor - Ph: 1.541.9572510 - Email: don.taylor@railamerica.com

Requester : Sandy Franger - Ph: 1.561.2261722 - Email: Sandy.Franger@RailAmerica.com

Bypass Local Waybills: No

Operating Station Notice: No

Effective Immediately: Yes

Include Empty Car: No

Maximum Car Allowed:

Commodities: Target All Commodities

Geography:

FSAC(s):From Stations, To Stations

CORP - 03130 - RICHARDSON, OR

CORP - 03135 - SWISSHOME, OR

CORP - 03140 - SIUSLAW, OR

CORP - 03145 - TIDE, OR

CORP - 03150 - MAPLETON, OR

CORP - 03155 - BECK, OR

CORP - 03160 - WENDSON, OR

CORP - 03165 - CUSHMAN, OR

CORP - 03170 - CANARY, OR

CORP - 03175 - KROLL, OR

CORP - 03185 - GARDINER JCT, OR

CORP - 03195 - REEDSPORT, OR

CORP - 03205 - LAKESIDE, OR

CORP - 03210 - HAUSER, OR

CORP - 03220 - CORDES, OR

CORP - 03230 - NORTH BEND, OR

CORP - 03300 - COOS BAY, OR

CORP - 03305 - MCCORMAC, OR

CORP - 03315 - HAYDEN, OR

CORP - 03325 - CHROME, OR

CORP - 03349 - COQUILLE, OR

Umler Equip. Type : Target All Umler Equipment Types

Car Weight: No Weight Restrictions

Clearance Code: No Clearance Code

Waybill Parties: Target All Waybill Parties

Cause: Other - specify

Cause Detail: Unsafe conditions in Tunnels 13, 15 and 18

Note: Effective Monday Sept 24, 2007 CORP by Permit only, will handle traffic moving outbound. Movement limited to cars currently on line.

Permit officer Tom Lanni 561-226-1798 (tom.lanni@railamerica.com) or Don Taylor 541 957 2510 Btwn 6am and 4pm Monday thru Friday

Amendment History:

Amendment 3 (Current): Remove Vaughn from Embargo and disallow Permits. Amend 2 per sandy franger email 9/22/07 allow permits and add notes

Amendment 2:

Amendment 1:

Jeffrey J. Usher

Asst. Vice President-Business Services

Association of American Railroads



*2007 Railroad Inspection  
Report*

**Evaluation of Tunnel Conditions Central Oregon and Pacific Railroad, Coos Bay Subdivision**

On Wednesday, October 9, 2007, a reconnaissance was conducted by a team of Federal Railroad Administration (FRA) and Federal Highway Administration engineers to observe conditions in Tunnels 13, 15, and 18 on the Coos Bay Subdivision of the Central Oregon and Pacific Railroad (CORP). Tunnels 13, 15, and 18 had been removed from service by CORP, and the Coos Bay Subdivision, south of Tunnel 13, is currently embargoed for all traffic.

The reconnaissance was conducted by walking through each tunnel from portal to portal, with illumination provided by flood lights mounted in the bed of a highway-rail truck and powered by a portable generator. Conditions observed in the tunnels were compared to the condition descriptors and general condition ratings contained in the report prepared by Shannon and Wilson between March 30 and July 9, 2007, and furnished to FRA by CORP.

The team evaluation substantially validates the findings documented in the Shannon and Wilson report. It should be noted that some conditions have deteriorated even further during the time since the report was prepared, partly due to the passage of time, and partly because of the onset of the wet season in Oregon in the early fall of 2007.

These tunnels were generally built in the 1880's, and rebuilt to their present configuration around 1914, using drill and blast methods common in that era. Tunnel lining construction includes unlined "bald" rock, timber sets with timber lagging, steel sets with timber lagging, shotcrete over timber or steel sets, and finally, cast-in-place concrete at both portals of Tunnels 13 and 15, and the south portal of Tunnel 18. Timber sets are constructed of 10" wide by 14" deep solid sawn cedar timbers. These sets are spaced on 48" nominal centers in Tunnels 13 and 18, and on 18" nominal centers in Tunnel 15. Voids between the timber liner and the surrounding rock were filled with cordwood packing.

The predominant problems observed were decay of the untreated cedar timbers, lagging, and footing blocks, especially in the wetter areas of the tunnels. This deterioration has resulted in differential settlement of the timber sets leading to shifting and occasional loss of the horizontal struts between adjacent sets. In addition, the lower 3-4 feet of many of the timber set posts sounds hollow or decayed when struck with a hammer, especially in locations where the footing blocks are clearly decayed or crushing. In a few of the wetter areas, severe decay of the caps and rafter timbers has destroyed the structural integrity of the lining sets. Decay, and subsequent loss of the cordwood packing, has produced a void above or behind the lagging, thereby providing weathering or blocking rock room to free-fall, striking the lagging. In areas where the timber sets and lagging have been covered with a nonstructural shotcrete veneer, evaluation of the existing condition is not possible, although it is suspected that trapped moisture is probably exacerbating the decay of surrounding timber components. In the unlined sections, there is evidence that minor, periodic rock-falls have occurred.

## General Tunnel Observations

The tunnel bores all appear to have been blasted using the methods of the day, which was to angle drill from the front face and blast. It is doubtful that any type of technique was used to control blast pressures and limit overbreak. Even with modern controlled blasting techniques, drilling and shooting tunnel bores results in some undesirable over-break. The overbreak on the three tunnels has resulted in an oversized bore with irregular pockets and voids. Overbreak from blasting has fractured some of the in-place rock. Thus, the fractured rock has to be supported, or it will continually ravel and fall out. Several areas in these tunnels had cordwood or stone packing as an effort to support the tunnel ceilings and walls. The overbroken voids are particularly difficult to support using these methods.

All of the tunnels utilized some arch segmental timber sets and lagging for support. The timber set internal dimensions are approximately 20 feet to the spring line and approximately 10 feet to the crown. Many of the timber set posts are 10 x 14-inch settings on wood blocks. The blocks appear to be cut from the post material and then laid on their side. The original timber set configuration had no structural capability for carrying lateral earth pressure loads from the tunnel walls. The lagging appears to be rough-cut 2 x 10-inch lumber, but it was not measured during the reconnaissance so these dimensions may not be accurate. All tunnels have intermittent water seepage areas. Detailed observations and conclusions for each of the three tunnels are as follows:

### **Tunnel 13; Milepost (MP) 669.47 to MP 669.94; length 2,489 feet; near Mapleton, Oregon.**

The portal had a concrete lining that was dated 1914 and extended approximately 65 feet back. In several locations, there are signs of overblasting and large voids in between the timber lagging. Cordwood packing is visible in between the timber lagging and the tunnel rock wall and ceiling face. There are intermittent water seepage areas in this tunnel. Differential weathering was noted in the tunnel walls. There are areas that have rock debris lying on top of the timber sets. In several locations, rock debris can fall through, or past, rotten timber. The timber set support blocks have rotted in several locations, allowing the timber sets to settle and pull away from the ceiling. In turn, the unsupported ceiling sections have released sandstone rock fragments ranging from gravel- to boulder-size (2 to 14 inches in diameter). Sagging timber sets have also kicked out from the tunnel walls, allowing sandstone rock fragments from gravel- to boulder-size to fall out of the excavated walls and place a thrust load on the timber set and lagging.

The tunnel had station markings on the walls from Station 0+00 to 3+00. Shotcrete had been placed, apparently as a past repair. The shotcrete condition looked good. At Station 6+00, a vertical set post is cracked from the footing up (at least 3 feet). This appeared to be an overstress condition. There is a void behind the timber set. From Station 14+00 to 16+00, approximately, the timber sets in the ceiling are bowed downward, apparently from overstress. The timber set ceiling support is discontinuous, and there is evidence

that rock blocks have dropped out of the ceiling. At Station 23+40, timber sets have rotted and fallen down. There is rock debris perched on top of the timber sets, and it is a rock-fall hazard. The Shannon and Wilson report rate this area as a Repair Level 2, but subsequent deterioration would most likely cause it to be downgraded to Repair Level 1. This tunnel has several locations that need immediate lining support repairs. There is a high risk of tunnel support failure and rock-fall hazard to train and maintenance traffic.

**Tunnel 15; length 2,148 feet; near Florence, Oregon.**

The north portal had a concrete lining that was dated 1914 and extended approximately 40 feet back. In general, the sandstone rock was softer than that of Tunnel 13. The tunnel has more seepage water, also. The rock in this area may have been slightly weakened by water saturation. This tunnel has extensive wood rot and questionable tunnel-wall and ceiling support. Several repairs have been performed, including installation of a concrete footing for timber set support. There are signs of overblasting star bursts in the tunnel walls and voids between the timber lagging and the rock face. There is potential for fractured rock to fall from these voids. At Station 14+40, the timber sets are very rotten and have sagged. There is approximately  $\frac{3}{4}$  of a yard of rock debris perched on the rotten wood. This material will fall down from the ceiling in the very near future. There is a high concern that rotten timber sets and lagging could fall into tunnel. There is a high risk of tunnel support failure and some risk of rock-fall hazard to train and maintenance traffic.

**Tunnel 18; MP 734.48 to MP 734.77; length 1,532 feet; near Florence, Oregon, off of Five Mile Creek Road.**

The north portal had a concrete lining that was dated 1914 and extended approximately 5 feet back. Some past shotcreting and steel sets have been installed in this tunnel. In some areas, the timber sets are closely spaced, indicating that during the original design and construction weak sandstone rock was recognized. The rock in this tunnel is the weakest of the three. The joints appear to be tighter, but the rock exhibits more of a soil character and may tend to slough. There are locations where the lagging has fallen out and the rock face is exposed. At Station 10+80, there is a section of the timber sets where they have apparently rotted at their bases and then slid off their footings. The timber sets have then kicked out approximately 2 feet from their original position.

The weak sandstone needs good ceiling and sidewall support, as the tunnel bore faces have weathered over the years and may be exerting more vertical and lateral pressures than where originally anticipated. At the same time, the strength of the timber sets has diminished over the years. The fact that a section of the timber sets has kicked out supports these concerns. More timber sets could kick out, which is a definite hazard to train and maintenance traffic.

**Summary and Conclusions**

The arch segmental timber sets and lagging in these tunnels have reached the end of their useful life and can no longer provide adequate support. As a result, several locations within each of the three tunnels have unsafe conditions that require repair. It is anticipated that more unsafe conditions will develop in the near future as the tunnel support continues to rot. The existing unsafe conditions include ceiling and wall rock-

fall, rock debris fall, timber set and lagging instability, and vertical timber set kick out. These tunnels are hazardous to train traffic and maintenance operations. Any future inspection or maintenance should be done with great care, with an understanding of the potential hazards. The original timber set design has severe limitations in its ability to resist lateral earth and rock loads. In addition, the timber sets are susceptible to fire.

The team evaluation substantially validates the findings documented in the Shannon and Wilson report. It should be noted that some conditions have deteriorated even further during the time since the report was prepared, partly due to the passage of time, and partly because of the onset of the wet season in Oregon in the early fall of 2007. In summary, FRA concurs with the recommendations made in the Shannon and Wilson report, that all three tunnels need immediate repairs to permit the safe resumption of railroad operations. The reconnaissance was not intended to review all of the repair recommendations that were made in the Shannon and Wilson report. All tunnel dimensions provided in this memorandum are approximate and should not be used for design or cost estimating.

Signed: Gordon A. Davids, P.E.

Chief Engineer—Structures  
Office of Safety Assurance and Compliance  
Federal Railroad Administration





THEODORE R. KULONGOSKI  
Governor

April 21, 2008

Paul Lundberg, Vice-President  
RailAmerica Operations Support Group, Inc.  
5300 Broken Sound Blvd  
Boca Raton, FL 33487

Dear Mr. Lundberg:

I received your proposal for a "joint venture" between RailAmerica and the State of Oregon on the CORP line between Vaughn and Cordes. Over two months ago, I asked RailAmerica, as a sign of good faith, to fix the tunnels and re-open the line. Your latest proposal does not respond to that request.

To put it succinctly, my bottom line has not changed. As I stated when we met in person on January 24<sup>th</sup> and repeated in my letter on February 12<sup>th</sup>, the State of Oregon would be open to a discussion with all of the stakeholders on a long-term solution for the line after you have re-opened it. Your refusal to address this bottom line leads me to conclude that you have no intention of fixing and reopening the line without a significant infusion of public dollars. Since you have made no effort since the September 2007 closure to re-open the line, I believe that your actions constitute an unlawful embargo and you are violating your common carrier obligation, thereby causing a hardship for Oregon's businesses and threatening the economic health of Oregon's coastal communities.

I continue to maintain that fixing the tunnels and restoring the flow of goods along the line is not only the right thing to do, but your legal obligation. Your choice seems clear: either re-open the line or seek abandonment. We need to come to a conclusion on this matter. I will continue to press federal authorities and Oregon's congressional delegation to close this chapter.

Sincerely,

THEODORE R. KULONGOSKI  
Governor

## CERTIFICATE OF SERVICE

I hereby certify that, pursuant to the Board's Decision served April 11, 2008, I have caused the Response of the Central Oregon & Pacific Railroad, Inc. to Order to Show Cause to be served by overnight delivery service this 12th day of May, 2008 on the following:

Governor Theodore R. Kulongoski  
State of Oregon  
160 State Capitol  
900 Court Street  
Salem, Oregon 97301-4047

Oregon International Port of Coos Bay  
Administration Office  
125 Central Avenue, Suite 300  
Coos Bay, OR 97420

J. Michael Hemmer  
Senior Vice President, Law and General Counsel  
Union Pacific Railroad Company  
1400 Douglas Street  
Omaha, NE 68179

Andy Jeffers  
Traffic Manager - Rail  
Roseburg Forest Products  
P.O. Box 1088  
Roseburg, OR 97470

Jerry Keck  
Toledo Area Manager  
Georgia-Pacific Corp.  
1400 SE Butler Bridge Rd.  
Toledo, OR 97391-1900

Paul Brewster  
Plant Manager  
American Bridge Co.  
135 American Bridge Way  
Reedsport, OR 97467

Jason W. Smith  
Mill Manager  
Southport Forest Products  
P.O. Box 298  
Coos Bay, OR 97420

Allen Dasher  
Retail Manager  
Amerigas  
425 Virginia St.  
North Bend, OR 97459

David Gray  
Plant Supervisor  
Ferrellgas  
1625 N. 7th St.  
Coos Bay, OR 97420

Tom McMann  
Transportation  
Coos Bay Lumber Co., LLC  
P.O. Box 750  
Coos Bay, OR 97420

Carl Foster  
Partner  
Danish Dairy  
94912 Hwy. 42 S.  
Coquille, OR 97423

Rocky Buckles  
Operations  
Thomas & Sons Transportation Systems  
840 South Front St.  
Coos Bay, OR 97420

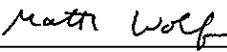
John W. Brands  
President  
Central Dock  
P.O. 148  
Coos Bay, OR 97420

Doug Woolsey  
Transportation Manager  
Coos Bay Docks  
P.O. Box 277  
Coos Bay, OR 97420

And via overnight delivery service and email on the following:

Oregon Department of Justice  
Attn: Katherine Georges  
1162 Court St. NE  
Salem, OR 97301  
katherine.georges@doj.state.or.us  
Sandra L. Brown  
Troutman Sanders LLP  
401 Ninth St., NW  
Washington, DC 20004-2134  
sandra.brown@troutmansanders.com

Oregon Department of Justice  
Attn: Stephanie Andrus  
1162 Court St. NE  
Salem, OR 97301  
stephanie.andrus@doj.state.or.us  
Ronald S. Yockim  
Attorney at Law  
430 S.E. Main St.  
Roseburg, OR 97470  
ryockim@cmspan.net

  
\_\_\_\_\_  
Matthew Wolfe