
**BEFORE THE
SURFACE TRANSPORTATION BOARD**

FINANCE DOCKET NO. 30186 (SUB-NO. 3)

**TONGUE RIVER RAILROAD COMPANY -- CONSTRUCTION AND
OPERATION -- WESTERN ALIGNMENT**

**SUPPLEMENTAL VERIFIED STATEMENT OF
MIKE T. GUSTAFSON**

My name is Mike T. Gustafson. I am the same person who submitted a verified statement in this proceeding in April 1998 in support of Tongue River Railroad Company's ("TRRC") Application for Construction and Operation ("Application"). I currently hold the position of President in Tongue River Railroad Company, Inc. ("TRRC, Inc."), an entity described further below which has succeeded to the transportation assets of TRRC.

The purpose of this Supplemental Verified Statement is to update various information set forth in my original Verified Statement. I will address, in the following order, updates to TRRC's business and financial structure; updates to various construction cost, tonnage, traffic and financial forecasts presented in the Application; the status of the transfer of the Otter Creek Tracts to the State of Montana; the status of TRRC's arrangements with BNSF; and, why the plans of the Dakota, Minnesota & Eastern Railroad ("DM&E") to expand into Wyoming will not affect the TRRC. I will also summarize the current public support for the TRRC.

I. Update to TRRC Business and Financial Structure

Current TRRC Ownership Structure. The ownership structure of TRRC described in my 1998 Verified Statement and at pages 8 to 9 of the Application has changed. In September 1998, TRRC, Inc., a Delaware general corporation, was formed to assume responsibility for construction and operation of the rail line at issue. On September 18, 1998, TRRC, Inc. filed a notice of exemption with the Board to acquire all of the transportation assets of the original Applicant (a partnership known as Tongue River Railroad Company), including the ICC and Board permits authorizing construction of the 89-mile line between Miles City, MT and Ashland, MT and the 41-mile line between Ashland and Decker, MT. Finance Docket No. 33644, Tongue River Railroad Company, Inc. -- Acquisition and Operation Exemption -- Tongue River Railroad Company (served October 8, 1998). That notice became effective on November 17, 1998. On November 13, 1998 the Board denied petitions to reject or revoke the exemption, and the transfer of assets to TRRC, Inc. was consummated on January 1, 1999. I understand that a motion to substitute TRRC, Inc. for TRRC as the applicant in this proceeding is concurrently being filed with the Board.

A copy of the certificate of incorporation of TRRC, Inc. is attached hereto as Exhibit 1. The current address of TRRC, Inc. (in lieu of the address reflected at page 6 of the Application) is 2280 Grant Road, Suite B, Billings, Montana 59102. The officers of TRRC, Inc. are as follows: President – Mike T. Gustafson; Vice-President – Douglas A. Day; Secretary – Douglas A. Day; and Treasurer – Douglas A. Day. The directors of TRRC, Inc. are Mike T. Gustafson and Douglas A. Day.

All of the stock of TRRC, Inc. is owned by TRR Limited Partnership, a Montana limited partnership. The general partner in TRR Limited Partnership is Transportation Properties LLP, a

Montana Limited Liability Partnership and the limited partner is Tongue River Holdings, Inc., a Montana corporation. The general partners of Transportation Properties LLP are WesRail, Inc., a Montana corporation, and Railco, LLC, a Montana limited liability company. Railco, LLC was established in place of The Pittsburg & Midway Coal Mining Co. which resigned from involvement in the TRRC project in April 1999. None of the officers, directors or major shareholders of TRRC, Inc. controls any other regulated carrier.

A new Exhibit A to the Application, a corporate resolution authorizing the construction of the line at issue, is being submitted herewith.

II. Update to Various Tonnage, Traffic and Financial Forecasts

Coal Production/Traffic Data. Information on the volumes of coal projected to be transported by the Applicant was set forth in the Application at pages 13-15 and at pages 21-22, as well as in my 1998 verified statement and in the 1998 Verified Statement of Ronald McMahan of Resource Data International, Inc ("RDI"). The data strongly supported the need for a new railroad to meet the demands of the market, including demands resulting from the need for low sulfur content "compliance" coal to meet requirements of the Clean Air Act Amendments of 1990. The TRRC, the evidence showed, is essential to allow for the development and production of vast coal reserves in southeastern Montana.

For purposes of updating the data presented in the Application and in Mr. McMahan's statement, TRRC recently asked Platts Research Consulting/RDI ("PRC/RDI"), the successor to RDI, to analyze the demand for southeastern Montana coal and to provide a future tonnage forecast for the TRRC. PRC/RDI has done so through the Verified Statement of Mr. Mark T. Morey, Managing Director of the PRC/RDI coal consulting group, which is being submitted as part of TRRC's Supplemental Evidence. Mr. Morey indicates in his statement that he expects,

due largely to changed economic circumstances since 1998, that demand will grow at a slower rate than predicted by Mr. McMahan. Mr. Morey nonetheless concurs with Mr McMahan's prior testimony that there will be sufficient demand for Northern Powder River Basin ("NPRB") coal to warrant the development of new mines in southeastern Montana, and sufficient demand to support the proposed TRRC rail line. In fact, Mr. Morey predicts that essentially the same coal capacity deficit in excess of 20 million tons predicted by Mr. McMahan will develop over the course of the next decade. To alleviate this deficit, it is essential that new reserves be developed such as Otter Creek. I believe that the construction of the TRRC line is essential for the development of the substantial coal resources in the Otter Creek area, as discussed further below.

Mr. Morey also provides a Total Tonnage Forecast table, reflecting a coal tonnage forecast for the TRRC for the railroad's first eleven operating years. The total volumes reflected on that table are largely similar to those reflected in the table that appeared at page 14 of the Application, which Mr. Morey's Total Tonnage Forecast table supersedes.

In short, applying conservative assumptions about growth and demand, Mr. Morey predicts ample coal tonnage for transportation by the TRRC line. The Western Alignment will facilitate the efficient transportation of this coal by shortening the number of miles on the line and thus reducing operating and maintenance costs.

Construction Cost Estimates/Completion Date Estimate. The estimated cost of constructing the Western Alignment is described at pages 12-13 of the Application and in the 1998 Verified Statement of Daniel R. Hadley, President of Mission Engineering, Inc., which was submitted with the Application. A detailed breakdown of these costs was set forth at Attachment 1 to that Verified Statement. At my request, Mr. Hadley has recently updated the estimated construction cost of the Western Alignment from 1998 escalated dollars to 2002 escalated

dollars. Based on this update, which is attached as Attachment 1 to Mr. Hadley's Supplemental Verified Statement, the estimated construction cost of the Western Alignment is approximately \$108,963,467, including all costs associated with excavation, major structure installation, construction reclamation, track installation, signals and communication system, and railroad infrastructure.

An estimate of the completion schedule/dates for the construction of the Western Alignment is set forth at page 20 of the Application. The projection of a 21 month construction period over the course of three years (given a seven month construction season) remains unchanged. TRRC will be prepared to commence construction once it receives all regulatory approvals, including secondary approvals that may be required from other agencies, and final engineering and design work, as well as environmental reviews, have been completed.

Financial Data. A pro forma statement of income and cash flow statement for TRRC were presented at Exhibit G of the Application, and this data is discussed at page 24 of the Application and at pages 8-10 of the 1998 Verified Statement of Mr. Robert Leilich of Corporate Strategies, Inc. In addition, Mr. Leilich presented at pages 5-7 and in Attachment I to his 1998 Verified Statement an analysis of the operating and economic benefits of the proposed Western Alignment versus the Four Mile Creek Alternative.

In his attached Supplemental Verified Statement, Mr. Leilich has updated the above data and restated, in current dollars, and in light of the modified traffic projections and construction costs described above, both the Exhibit G pro formas and the statement of Western Alignment benefits. Mr. Leilich's updated data demonstrates that the TRRC, Inc. proposal is viable and that the Western Alignment benefits remain substantial. In fact, Mr. Leilich's updated analysis shows that the operating and economic advantage of the Western Alignment over the Four Mile

Creek alternative is now about \$4.4 million, versus the \$2.8 million reflected in his 1998 testimony.

In addition, information concerning the plans for financing construction of the line was presented at pages 23-24 of the Application and discussed in the Verified Statement of Mr. Francis Cox of Chase Securities, Inc. The financing assumptions remain unchanged. To the extent that the capital construction cost estimate has increased, the approximate amount of capital and long term debt will increase accordingly.

Operating Plan. The Operating Plan set forth at Exhibit D of the Application remains largely unchanged, as discussed in Mr. Leilich's Supplemental Verified Statement. Mr. Leilich describes only some very modest changes, resulting from the modified coal tonnage forecasts, the predicted number of trains, the number of TRRC employees and (based on the new comparison of Western Alignment versus Four Mile Creek costs) the expected operating economies.

III. Transfer of Otter Creek Tracts to State of Montana

The Otter Creek Tracts consist of three tracts of land (Otter Creek 1, 2, and 3) comprising approximately 19,880 acres located southeast of Ashland, MT, in the area that would be served by TRRC's proposed rail line. There are significant coal reserves located beneath the Otter Creek Tracts, but at the present time those reserves are undeveloped. As explained in the Application, a principal purpose of the TRRC line is to provide rail transportation to the mines to be developed in the Ashland area, including new mines in the Otter Creek Tracts. Indeed, as a practical matter, the resources in these Tracts cannot be developed until the TRRC line has been constructed.

At the time the Application was filed, the mineral rights underlying Otter Creek Tracts 1, 2 and 3 were owned by the federal government. Since then, those mineral rights have been transferred to the State of Montana. The transfer of the federal mineral rights in the three Otter Creek Tracts to the State of Montana evolved from President Clinton's August 1996 announcement of an agreement between the federal government and Crown Butte, Inc. The Agreement required Crown Butte to abandon further development efforts of a gold mine near Yellowstone National Park in exchange for unspecified federal assets. Following discussions between federal and state officials on a transfer of assets, in October 1997, Section 503(a) of the Department of Interior and Related Agencies Appropriations Act of 1998 was enacted (Pub. Law. No.105-83), providing \$65 million for the purchase of the Crown Butte holdings and authorizing the transfer of \$10 million in federal mineral properties to the State of Montana as compensation for the economic opportunity lost to the people of Montana. Section 503(b) of this same measure directed that the Secretary of the Interior and the Governor of Montana enter into negotiations to determine which mineral rights owned by the United States should be transferred to the State of Montana. Further, the legislation provided that if the Secretary and the Governor could not come to agreement by January 2, 2001, then the federal mineral rights in Montana – referred to as Otter Creek Tract numbers 1, 2, and 3 – would transfer to the State of Montana by operation of law. Following a state assessment demonstrating the economic benefit to Montana of the transfer of those Tracts, on February 24, 1999, then Montana Governor Racicot gave formal notice to the Secretary of Interior of the State's selection of the federal mineral rights in the Otter Creek Tracts.

In August 2001, the Northern Cheyenne Tribe ("NCT"), which had raised objections to the proposed transfer of the Tracts on financial and environmental grounds, among others,

circulated a proposed settlement of NCT's objections to state and federal officials. When settlement was not reached, the NCT, in January 2002, sought to enjoin the transfer through a suit filed in U.S. District Court for the District of Columbia. However, on February 19, 2002, the Montana State Land Board voted to accept the terms of NCT's settlement proposal, resulting in NCT's withdrawal of its suit. Thereafter, the US Department of Interior, Bureau of Land Management, finalized its Environmental Assessment on the transfer of the three Otter Creek Tracts. The transfer to the State of Montana of the federal mineral rights in the three Otter Creek Tracts was finalized on April 10, 2002.

As noted in Governor Judy Martz's letter dated April 2, 2003, the Otter Creek Tracts represent an important asset to the State of Montana and provide the opportunity to provide future funding for K through 12 education. The Governor notes that the state intends to continue its efforts to bring the Otter Creek Tract assets into timely production in order to provide economic opportunity for the people of Montana. Further, the Governor notes the importance of the Tongue River Railroad as an essential transportation feature necessary for the State to recognize the economic potential offered by the State's ownership of the Otter Creek coal assets.

I want to emphasize the critical importance of TRRC to the accomplishment of the purpose sought to be achieved by the federal government's transfer of the Otter Creek mineral rights to the State of Montana. The Otter Creek coal reserves can benefit the state only if they are commercially developed. But commercial development will not -- and indeed cannot -- occur until there is a means of getting the coal to market. As a practical matter, rail continues to be the only feasible way of transporting that coal to potential customers, but at the present time no rail line reaches the Otter Creek tracts. Thus until the Tongue River Railroad is built, the

Otter Creek coal reserves will remain undeveloped and the state will be unable to realize the benefits to the people of Montana that the transfer was designed to achieve.

IV. Relationship Between BNSF and TRRC

TRRC's proposed line will connect with BNSF's line at Decker, Montana in the south and at Miles City, Montana in the north. TRRC will not connect with any other railroad and virtually all TRRC traffic will be interchanged with BNSF. The ongoing discussions between BNSF and TRRC with respect to a commercial operating agreement for operations over the TRRC line were described at pages 7 to 8 of the Application. An agreement has not yet been finalized. However, now that this application is again moving forward, BNSF and TRRC have resumed discussions and anticipate that an agreement will be in place prior to the time that operations over the line are ready to begin. In addition, BNSF has entered into a loan agreement with TRRC under which it is providing funds to TRRC for expenses incurred in the federal and state regulatory processes.

TRRC has continued to coordinate with BNSF with respect to issues of interest to both railroads. TRRC is consulting with BNSF engineering personnel with respect to various technical issues concerning construction of the line, and continues regular discussions with BNSF marketing personnel concerning developments affecting the upper midwest utility market.

V. The DM&E Extension Will Not Impact TRRC

The DM&E gained final Surface Transportation Board ("STB") authority in January 2002 to construct and operate a new 280 mile rail line from a point on its existing line near Wasta, South Dakota into Wyoming, where it would serve coal mines located in the Southern Powder River Basin ("PRB") south of Gillette, Wyoming. *See Dakota, Minnesota & Eastern Railroad-Construction into the Powder River Basin*, STB Finance Docket No. 33407 (STB

served Jan. 30, 2002). In connection with the new construction, DM&E plans to rebuild and comprehensively upgrade 598 miles of its existing rail lines in Minnesota and South Dakota.

Currently, the Union Pacific and BNSF serve the southern PRB in Wyoming. In addition, the BNSF rail line extends north into Montana. The DM&E is intended to provide a more direct east-west service into the southern Wyoming PRB, increasing regional rail capacity and strengthening rail competition for delivery of low-sulfur Wyoming southern PRB coal. In its decision, the STB found that the DM&E would be competitive in a number of markets for Wyoming southern PRB coal transportation and that there would be transportation benefits resulting from the proposed rail line due to providing increased competition for southern PRB coal traffic and improved service to DM&E's existing shippers. In its application, the DM&E reasoned that, because of its mileage advantage in certain markets, it will have a competitive edge and will take traffic away from BNSF and UP based on prevailing market rates. The STB found that the DM&E would be in a competitive position to gain an approximate equal market share with the UP and BNSF of the Wyoming southern PRB coal shipments currently being hauled by the UP and BNSF.

The principal commodity to be transported by TRRC will be coal moving from the northern PRB, and specifically existing mines near Decker, Montana and proposed coal mines in the vicinity of Ashland, Montana. Use of the TRRC line will reduce the present transportation distance for coal mined in the northern Powder River Basin (primarily in Montana and more modestly in Wyoming) to electric utilities in the upper Midwest, Great Lakes and the Pacific Northwest regions. The TRRC will provide, for the first time, rail service to largely undeveloped reserves of low-sulfur, sub-bituminous coal situated in the vicinity of Ashland, Montana and the Otter Creek area to the south and east of Ashland, MT.

The DM&E would not have access to coal production from the operating mines located near Decker, Montana or to the coal reserves situated in the vicinity of Ashland, Montana. Conversely, the TRRC would not have access to coal production from mines located to the south of Gillette, Wyoming, where DM&E would provide service. Thus, TRRC and DM&E will not be able to compete for coal from any particular mine. While there may be some source competition between mines served by TRRC and mines served by DM&E, there is already a significant amount of source competition for coal among the PRB mines and between mines in the PRB and mines in other areas. I do not anticipate that the DM&E extension will result in any significant change in the nature or level of that source competition. Depending on whether an agreement is finalized between the BNSF and TRRC, the BNSF could route coal traffic originating from mines in the vicinity of Gillette, Wyoming by way of the TRRC. It appears unlikely based on available information that the DM&E would be able to access the mines nearest to Gillette, WY.

Based on the above, I do not believe the DM&E's proposed extension will have any effect on the TRRC, nor should the construction of the TRRC line have any effect on DM&E.

VI. Public Support for the TRRC

I stated in my 1998 Verified Statement that TRRC's Application was supported by Montana's Governor, its two US Senators and its Congressman. This remains the case, even though the Governorship and Congressional seat for Montana have now changed hands. Letters of support from Governor Martz and Congressman Dennis R. Rehberg are attached, and letters from Senators Conrad Burns and Max Baucus were filed with the 1998 Application.

In sum, for all of the reasons set forth in the 1998 Application and updated here, the Board should conclude that construction of the Western Alignment will benefit TRRC, its prospective shippers and the public. This concludes my verified statement.

CERTIFICATE OF INCORPORATION
OF
TONGUE RIVER RAILROAD COMPANY, INC.

To form a corporation pursuant to the Delaware General Corporation Law, the undersigned hereby certifies as follows:

ARTICLE 1.

The name of this corporation is Tongue River Railroad Company, Inc.

ARTICLE 2.

The purpose of this corporation is to engage in any lawful act or activity for which corporations may be organized under the Delaware General Corporation Law, including, without limitation, to project, design, plan, conduct engineering studies of, arrange financing for and obtain all applicable federal, state and local permits and authorizations for the construction and operation of, to secure rights-of-way for, and to construct, equip and operate railroads.

ARTICLE 3.

The corporation shall have perpetual duration.

ARTICLE 4.

The registered office of this corporation in Delaware is 1209 Orange Street, Wilmington, New Castle County, Delaware 19801, and the name of its registered agent is The Corporation Trust Company.

ARTICLE 5.

The total number of shares of stock which this corporation is authorized to issue is 50,000 shares of nonassessable common stock with a par value of \$1.00 per share.

ARTICLE 6.

In furtherance, and not in limitation of the powers conferred by statute, the board of directors is expressly authorized to make, amend, alter, change, add to or repeal bylaws of this corporation, without any action on the part of the stockholders. The bylaws made by the directors may be amended, altered, changed, added to or repealed by the stockholders. Any specific provision in the bylaws regarding amendment thereof shall be controlling.

ARTICLE 7.

A director of the corporation shall not be personally liable to the corporation or its stockholders for monetary damages for breach of fiduciary duty as a director; provided, however, that this article shall not eliminate or limit the liability of a director (a) for any breach of the director's duty of loyalty to the corporation or its stockholders; (b) for acts or omissions not in good faith or which involve intentional misconduct or a knowing violation of law; (c) for the unlawful payment of dividends or unlawful stock repurchases under Section 174 of the Delaware General Corporation Law; or (d) for any transaction from which the director derived an improper personal benefit. This article shall not eliminate or limit the liability of a director for any act or omission occurring prior to the effective date of this article.

If the Delaware General Corporation Law is hereafter amended to authorize any further limitation of the liability of a director, then the liability of a director of the corporation shall be eliminated or limited to the fullest extent permitted by the Delaware General Corporation Law, as amended.

Any repeal or modification of the foregoing provisions of this article by the stockholders of the corporation shall not adversely affect any right or protection of a director of the corporation existing at the time of such repeal or modification.

ARTICLE 8.

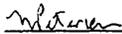
The initial board of directors shall be comprised of:

<u>Name</u>	<u>Address</u>
Mike T. Gustafson	550 N. 31st Street, Suite 250, Billings, MT 59101
Donald C. Mielke	905 Hills Creek Dr., McKinney, TX 75070-5231
James G. Di Zerega	6400 S. Fiddler's Green Circle, Englewood, CO 80111
Davin L. Anderson	6400 S. Fiddler's Green Circle, Englewood, CO 80111

ARTICLE 9.

The name and mailing address of the incorporator is: L. W. Petersen, 1200 First Interstate Center, 401 North 31st Street, Billings, Montana 59101.

Dated: September 4, 1998



L. W. Petersen, Incorporator

STATE OF MONTANA)
)
COUNTY OF YELLOWSTONE)

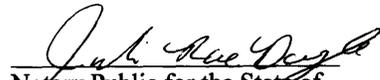
ss:

Mike T. Gustafson, being first duly sworn, deposes and says he has read the foregoing statement, knows the contents thereof, and that the same are true and correct to the best of his knowledge and belief.



Mike T. Gustafson

SUBSCRIBED AND SWORN TO before me this 25th day of April, 2003.



Notary Public for the State of
Montana.
Residing at *shepherd, Montana*
My commission expires: *January 29, 2007*

SEAL