

## **ISSUES TO CONSIDER: POSSIBLE SALE OF PANHANDLE RAIL LINE**

May 13,2002

***Background and Recent History:*** In April, 1992, the State of Ohio acquired the so-called “Panhandle” rail line. The legal owner of the Panhandle is a self proclaimed “shell” corporation called Caprail I. Caprail I owns the property but leases it to the State. The Caprail I - State lease specifies that virtually all the rights and responsibilities of ownership fall upon the State.

The Panhandle was purchased through an innovative financing mechanism using Certificates of Participation, or “COPs”. COPs are similar to municipal bonds and enabled the financing to be tax exempt. The term of the COPs is 20 years. \$8.6 million in COPs were sold to finance the \$7.45 million acquisition, \$375,000 of track work, a reserve fund, and the costs of issuance. In addition, the State provided \$450,000 in grants toward the purchase. About \$5 million in COPs repayments are outstanding. Terms of the COPs issuance allow the remaining COPs certificates to be bought out with no penalty as of April, 2002.

The Panhandle properties include 161 miles of track from Columbus to Mingo Junction. Included in this trackage are branchlines between Heath and Hebron, Cadiz Junction and Georgetown, and at Trinway. Ownership of the line between Columbus and Newark (32.6 miles) is shared with CSX Transportation on an equal basis.

Since 1992, the Columbus & Ohio River Rail Road (C&ORR) has been the Contract Operator of the Panhandle line. As such, the C&ORR is responsible for all operations on and maintenance of the rail properties, for all taxes, and for the repayment of the COPs debt. The C&ORR has been paying **\$58,000** per month in COPs repayments every month since April, 1992. Maintenance expenses in recent years have been well over \$2 million per year.

The C&ORR enjoys the proceeds from serving rail users on the line. The C&ORR has built up the traffic on the line to over 21,000 carloads per year. The line generated about 10,000 carloads of traffic in the last year of Conrail operations. Major commodities now handled include coal, steel, grain, plastics, cement, and asphalt. Audited financial statements consistently show the C&ORR is a profitable railroad company.

***Panhandle and the Ohio Central System:*** The C&ORR is part of the Ohio Central Railroad system. The C&ORR is directly interconnected with the Ohio Central Railroad and the Ohio Southern Railroad. The Ohio Central Railroad uses Panhandle track between Coshocton and Dresden. Through Ohio Central trains use the Panhandle line, while the Ohio Central owned line is used by the Ohio Central/Ohio Southern/C&OR trains to serve the Conesville power plant, and to store cars. The Ohio Central locomotive shops are located on Ohio Central owned property at Morgan Run (near Coshocton) where the Ohio Central line and Panhandle cross. The C&ORR owns track in Columbus (the former Conrail Neilston Secondary and former Norfolk Southern industrial tracks) which is contiguous with the State owned Panhandle. A small portion of the Neilston line (about 1,000ft.) separates the Panhandle from NS/CSX tracks to Buckeye Yard.

## I KEY FACTORS TO CONSIDER CONCERNING THE SALE OF THE PANHANDLE

**A) Existing Rail Users and Ohio Commerce:** A critically important factor in considering any sale of the Panhandle is the impact on the commerce of Ohio. Primary consideration in this regard should go to Ohio companies which are served from the Panhandle line and Ohio companies which depend on the Panhandle for through traffic movements. Consideration to how the sale of the Panhandle could affect rail users not located on the Panhandle should also be a part of any analysis. Direct input from Panhandle rail users and transportation experts should be considered.

**B) Interests of the State of Ohio for Maximum Utility from Line:** Another critically important consideration is the interest of the State to foster commerce and improve the quality of life for Ohioans through improved freight and passenger services on the line. In terms of freight, the continued "Reasonable Access" of other freight railroads to the Panhandle in certain circumstances could be important to the future economic development in communities along the Panhandle as well as for other Ohioans. Similarly, the Panhandle line could prove invaluable for use of intercity passenger trains operating between Columbus and Pittsburgh, or commuter trains running to and from Columbus from points east. ORDC, state elected officials, and other state agencies could evaluate statewide interests.

**C) Interests of Local Public Entities:** The interests of local public bodies will most likely be diverse and could include issues from property management (rail bridges and railroad owned highway bridges over highway, culvert and drainage issues, safety and crossing issues, etc.). Direct input from public officials should be considered.

**D) Interests of ORDC:** Another important consideration is the impact of any sale on ORDC, other state agencies. Selling the line could help ORDC augment its budget and reduce legal liabilities, although it might also reduce ORDC's ability to promote the State's freight and passenger agenda.

## II OPTIONS FOR OWNERSHIP OF THE PANHANDLE

Options for ownership of the Panhandle include:

1. **Maintaining the Status Quo:** Under this scenario, Caprail I would continue to be the owner, the State the lessee, and the C&ORR, or another railroad the Contract Operator. COPSPayments would be completed in April of 2012 and Caprail I would transfer full ownership to the State.
2. **Sell Panhandle to Highest and Best Bidder:** Under this scenario, the State would conduct a competitive bid process to sell the Panhandle. Bid price, service, and other considerations could be the basis of selecting the winning bidder.
3. **Sell Panhandle to C&ORR:** Under this scenario, the State would negotiate terms and conditions with the C&ORR for the purchase.

## ISSUES TO CONSIDER FOR OPTION 1: STATUS QUO

**A) *Question of Need for State Ownership:*** Most railroads in the United States are privately owned. Of Ohio's approximately 5,800 miles of track, only about **415** miles are publically owned, including the **160** miles of Panhandle track. Generally, the publicly owned tracks are home to marginally profitable rail operations which do not produce enough revenue to provide all the capital needed to adequately maintain track and structures. The Panhandle is an exception. The C&ORR has demonstrated that the Panhandle generates enough money to pay down a significant acquisition debt, and still provide millions of dollars each year for track and structure and other infrastructure improvements. In **1992**, there were serious questions about the long term viability of the Panhandle. In **2002**, viability is no longer an issue raising the question: "Should the State continue to own economically self-sufficient rail lines such as the Panhandle?"

**B) *Existing Rail Users and Ohio Commerce, Benefits:*** Clearly, the State intervened in the Panhandle situation in **1992** because the line was critical to the commerce of Ohio, especially to those rail-dependent companies which depended on it. State ownership does facilitate some benefits rail users generally view as favorable, for example, ORDC tends to look favorably on investments in State property for railroad owned highway bridges and culverts and other such things than it would for similar projects on privately owned lines.

***Dis-benefits:*** Yet, because the State's understanding of the rail business may not always be perfect, it is possible that some State actions could result in damage to the rail freight business of its Contract Operator and the businesses it serves. For example, it is arguable that the State's facilitation of the Newark bike path in close proximity to the Panhandle line could be damaging to the Panhandle rail users. While the bike path certainly serves an important public purpose, an accident on the bike path involving a C&ORR train could result in damage claims against the C&ORR which crippled its ability to adequately serve its customers.

A question to be considered is:

"Is the State the best steward of the needs of the rail community?"

**C) *State of Ohio Benefits:*** State ownership of the Panhandle arguably has significant benefits. For example, the State's Operating Agreement with the C&ORR allows ORDC to stipulate that rail freight carriers other than the C&ORR be allowed overhead trackage rights for a specified price (**29** cents per mile with an escalator tied to rail cost indices) for specified reasons (to facilitate overhead traffic or to serve a new rail user). The Operating Agreement also specifies that ORDC can mandate that certain passenger trains use the Panhandle. Further, State ownership of the line enables ORDC to pursue State goals and objectives which a private rail carrier would never allow. For example, State ownership of the Panhandle enabled bike path interests to build a bike path along the Panhandle right-of-way in the Newark area. Also, State ownership provides a recourse for local public bodies and citizens to seek redress against the railroad. ORDC has been called upon on several occasions to mediate Panhandle rail property

and other rail related disputes because of the State's ownership position.

A questions concerning public ownership which should be addressed is:

“Can the present benefits of public ownership be maintained through provisions of a purchase and sale agreement?”

**Dis-benefis:** The dis-benefits of state ownership from the statewide perspective would be similar of the same as the dis-benefits listed in part “C” above.

**D) Local Public Entities Benefis:** Local entities sometimes experience difficulties working with railroads, especially over issues which could require the railroads to spend money with no economic return for them, for example, painting bridges or cutting weeds or other cosmetic improvements. The State's ownership position sometimes provides local entities with an effective mediator, i.e. ORDC, for contentious issues.

**Dis-benefis:** On occasion, local officials seek actions from railroads which would adversely affect the railroad's ability to serve local rail users dependent upon rail service.

**E) ORDC Benefis:** One benefit of State continued ownership of the Panhandle is that the current arrangement could be considered a good economic deal. The C&ORR is currently paying off the COPs debt for the acquisition. After the COPs are paid off in 2012, Caprail I would be dissolved and the State would be the sole owner. ORDC could sell or lease the line at that time with all proceeds going to the State. In essence, ORDC's current position is that of a landlord of a house whose tenant is paying all of the mortgage.

Note that proceeds from the Panhandle would not automatically accrue to ORDC. If the Panhandle were to be sold tomorrow, any proceeds above and beyond those needed to repay COPs would go to the General Revenue Fund. Special arrangements with the Office of Budget and Management and/or the General Assembly would be needed to enable ORDC to reap profits from a sale.

**Dis-benefis:** There are arguably considerable dis-benefits to the current arrangement. One is that ORDC is more likely to invest in projects on the Panhandle than other projects. For example, ORDC's Operating Agreement with the C&ORR specifically states that the C&ORR can apply for 90% grant funding for the repair or replacement of any highway bridge over the railroad for which the railroad line owner has responsibility. In addition, political pressure from communities sometimes pulls ORDC into various issues (culverts, drainage, spalling on bridges, etc.) because of our ownership position.

Another dis-benefit is liability. ORDC has become involved in lawsuits directly related to its ownership position. The State's “deep pockets” could well be a magnet for other legal actions against ORDC related to the C&ORR's operation of the Panhandle.

#### IV ISSUES TO CONSIDER FOR OPTION 2: SELL TO THE HIGHEST BIDDER

**A) Bid Methodologies:** There is room to debate how to go about selling the Panhandle to the “Highest & Best Bidder”. Qualitative issues to consider would be the qualifications of the bidders, their ability to effectively serve the rail shippers and Ohio’s commerce, their willingness to allow the State to continue to have specific access rights for freight and passenger purposes, and related issues. Quantitative issues to consider would be the real value of the line and the level of acquisition investment which could be made without compromising the long term viability of the line. No matter what the form, the same basic issues of benefits and dis-benefits would need to be examined.

**B) Existing Rail Users/Ohio Commerce Benefits:** On the benefit side, it may be that opening up the Panhandle to competitive purchase bids could generate rail transportation options which would never be considered in a non-competitive environment. Bidders would need to examine every advantage they might be able to bring to the table to put together the best bid. Bidders would likely look at different service logistics, different routing options, a variety of innovative intermodal options, or related issues which could improve transportation services. These investigations could bring many unforeseen benefits to shippers and commerce. Another benefit might be that the sale of the Panhandle might once and for all eliminate any questions about a non-railroad owner unwittingly damaging Panhandle rail service in pursuit of some other public goal. **This** issue could be investigated with Panhandle rail users.

**Dis-benefits:** On the dis-benefit side, rail users generally value stability and predictability in the transportation market and could view the possible change of railroad operator negatively. Long term rail contracts could be of particular concern. This issue could be investigated **with** Panhandle shippers. Another area worth examination is the possibility that a bid process would entice bidders to be overly optimistic with their bids and pay too much for the Panhandle. Putting too many resources in acquiring the line could result in lack of funds for track maintenance, rail service, and operational support.

**C) State of Ohio Benefits:** On the benefit side, the State would share in any gains made by rail users or improvements in commerce. This issue could be investigated with Panhandle rail users and transportation logistics experts. Further, an assessment of whether or not the bid process would produce the most money for state coffers could be undertaken.

**Dis-benefits:** Possible dis-benefits include the loss of control of access for future freight and passenger services. However, the State could make the retention of certain access options conditions of the sale to avoid this potential downside. The **bid** prices might be lower to account for State’s retention of select rights.

**D) Local Public Entities Benefits:** To the extent rail users and the State of Ohio benefit from a competitive sale, it can be argued that local would benefit also. Investigating local views on this issue should be considered.

**Dis-benefits:** To the extent local public bodies desire to have ORDC as a mediator, or to have ORDC be able to mandate freight and passenger trackage rights, locals may view a competitive bid sale as a dis-benefit. Local opinions on this matter could be solicited.

**E) ORDC Benefits:** On the benefit side, ORDC could ~~try~~ weigh the expected present value of the possible windfall from a competitive bid sale now, against the expected value which could be expected to be reaped from a sale or lease of the Panhandle after the COPs debt is retired. Related issues include whether proceeds from a sale would go to ORDC, or the State's General Revenue Fund.

Another benefit would be that ORDC would be relieved of the burdens of ownership, namely the expectation that select projects must be funded by ORDC because of the State's ownership position in the line, and the possible liability of being "deep pockets" in law suits resulting from some aspect of rail operations.

**Dis-benefits;** One major possible dis-benefit to the sale of the line could be that a competitive bidding process could result in lawsuits. The Ohio Central might have grounds to use litigation to stop a competitive bid process. (See section below on Ohio Central Railroad System Issues.) Or losing bidders could resort to litigation if they perceived the bid process were unfair.

**F) Ohio Central Railroad System Issues:** Before a competitive bid process for the sale of the Panhandle is pursued, questions about the impacts on the C&ORR and the Ohio Central System should be examined.

Operational issues for any new operator could be a key area of concern. For example, the Conesville Power plant is located on the Ohio Central Railroad, not the Panhandle. If a railroad other than an Ohio Central Railroad owned the Panhandle, it would not be able to get coal from Harrison Mining to Conesville on a single line haul (i.e. one railroad carrying the freight from **origin** to destination). In addition, a new operator would have to work out a myriad of new trackage rights agreements with the Ohio Central, Ohio Southern, and C&OR to effectuate effective, reliable service for all railroads involved.

**A** major consideration concerning only the Ohio Central System would be the impact of the loss of the Panhandle on the entire company, and the rail users it now serves. ORDC might want to investigate how the loss of economies of scale would impact the ability of the Ohio Central System to effectively serve its customers.

Another major consideration concerning the Ohio Central System would be how to deal with the "sweat equity" the C&ORR has in the line. The C&ORR has for the last **10** years paid all COPs debt retirement costs, invested millions in track maintenance, built up traffic and served shipper needs, and greatly increased the going concern value of the Panhandle. ORDC should examine how to factor this into any competitive bid process.

## V ISSUES TO CONSIDER FOR OPTION 3, SELL LINE TO C&ORR

**A) *Competitive Bid Issue:*** Any time a State asset is sold without a competitive bid, the policy issue of whether or not the citizens of Ohio are well served by a sole source contract is raised. ORDC should address this issue before pursuing a sole source sale of the Panhandle.

**B) *Valuation Issues:*** The question of how to value the Panhandle needs to be addressed. RL Banks made a presentation to ORDC Commissioners on valuation techniques last year (going concern, net liquidation value, fair market value, and others). Possibly complicating the issue of which methodology to select, are issues such as: 1) the value of any rights the State wants to retain; and 2) any possible change in valuation due to the C&ORR's "sweat equity" and investments in the line.

**C) *Terms and Conditions Issues:*** In addition to ORDC's possible retention of certain freight and passenger service access rights similar to those now in the ORDC - C&ORR Operating Agreement, various public entities have from time to time expressed interest in obtaining certain rights over the Panhandle for commuter service and even public trails. Decisions would need to be made about which rights would best serve the public.

**D) *Existing Rail User/Ohio Commerce Benefits:*** On the benefits side, further investigations into Panhandle shipper satisfaction may be in order. Also, it may be wise to examine what private investment the C&ORR might be able to make if it owned the line which is not feasible under State ownership. A possible benefit from privatization could be the elimination of politically driven decisions concerning the property.

***Dis-benefits:*** On the dis-benefit side, an economic analysis of the impacts of the sale on the ability of the C&ORR and other Ohio Central System railroads to maintain track, serve shippers, and operate the railroad with any new Panhandle acquisition debt might be undertaken to determine if the C&ORR would be paying too much for the rail line.

**E) *State of Ohio Benefits:*** The State would share any benefits which could accrue to shippers or result from improved commerce due to any increases in C&OR investment in the Panhandle resulting from privatization.

***Dis-benefits:*** The State would experience dis-benefits if it were less able to pursue freight and passenger access goals as the result of a sale of the Panhandle.

**F) *Local Public Entities' Benefits and Dis-benefits:*** The benefits and dis-benefits from a sole source sale would be the same of similar to those of a competitive bid sale.

**G) *ORDC Benefits and Dis-benefits:*** The benefits and dis-benefits to ORDC from a sole source sale would be very similar to those of a competitive bid sale. Similar issues as to whether a monetary gain could be made would need to be examined as would possible problems with litigation.

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**SUMMARY OF ISSUES/  
BENEFITS AND DIS-BENEFITS TO CONSIDER:  
POSSIBLE SALE OF PANHANDLE RAIL LINE**

May 13,2001

**I KEY FACTORS TO CONSIDER**

- A) Interests of Existing Rail Users and of Ohio Commerce
- B) Interests of State of Ohio
- C) Interests of Local Public Entities
- D) Interests of ORDC

**II OPTIONS FOR OWNERSHIP OF THE PANHANDLE**

- A) Maintaining the Status Quo
- B) Selling Panhandle to Highest and Best Bidder
- C) Sell Panhandle to C&OR

**III ISSUES TO CONSIDER FOR MAINTAINING THE STATUS QUO**

- A) Should State Continue to Own Viable Rail Line?
- B) Existing Rail User/Ohio Commerce Possible Benefits
  - \* Continued State Investment
  - Possible Dis-benefits
    - \* Poor Decision Making by State on Key Property Issues
- C) State of Ohio Possible Benefits
  - \* Promotion of Reasonable Freight and Passenger Access
  - Dis-Benefits
    - \* Poor Decision Making by State
- D) Local Public Entity Possible Benefits
  - \* Continued ORDC Role as Mediator
  - Possible Dis-benefits
    - \* Poor Decision Making by Locals
- E) ORDC Possible Benefits
  - \* Present Arrangement Good Economic Deal
  - Possible Dis-benefits
    - \* ORDC "Deep Pockets" Liability as Panhandle Owner

**IV ISSUES TO CONSIDER FOR SELLING TO HIGHEST BIDDER**

- A) Bid Methodologies Complicated
- B) Existing Rail Users/Ohio Commerce Possible Benefits
  - \* Possible Improved Services and Logistics

- Possible Dis-benefits
  - \* Lack of Stability for Rail Users
  - \* Bidders Pushed by Competition to Pay Too Much for Railroad
- C) State of Ohio Possible Benefits
  - \* Best Dollar Return
- Possible Dis-benefits
  - \* Loss of Control for Freight and Passenger Access
- D) Local Public Entities' Possible Benefits
  - \* Local Rail Users Possible Benefit from Improved Service and Logistics
- Possible Dis-benefits
  - \* Loss of ORDC as Mediator
  - \* Loss of Freight and Passenger Access for Local Goals
- E) ORDC Possible Benefits
  - \* Influx of Funds IF ORDC Allowed to Retain \$\$ From Sale
  - \* Eliminates ORDC "Deep Pockets" Liability
- Possible Dis-benefits
  - \* Litigation Arising Out of Competitive Bid Process
- F) Ohio Central Railroad System Issues
  - \* Operational Issues
  - \* Loss of Economies of Scale of Ohio Central System
  - \* Value of C&ORR "Sweat Equity" in debt retirement, maintenance and service

#### **IV ISSUES TO CONSIDER FOR SELLING LINE TO C&ORR**

- A) Competitive Bid Issues
- B) Valuation Issues
- C) Terms and Conditions Issues
- D) Existing Rail Users Ohio Commerce Possible Benefits
  - \* Private Investment C&ORR Could Make as Result of Ownership
  - \* Elimination of Politically Driven Decisions
- Possible Dis-benefits
  - \* C&ORR May Pay Too Much for Line
- E) State of Ohio Possible Benefits
  - \* Private Investment C&ORR Could Make as a Result of Ownership
- Possible Dis-benefits
  - \* Less Able to Pursue Freight and Passenger Goals
- F) Local Public Entities' Possible Benefits
  - \* Same as for Competitive Bid
- Possible Dis-benefits
  - \* Same as for Competitive Bid
- G) ORDC Possible Benefits
  - \* Same as for Competitive Bid
- Possible Dis-benefits
  - \* Same as for Competitive Bid