

1st MONDAY 3rd MONDAY SPECIAL

Prepared for employees by the
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Managers and Supervisors:

On June 20, Trustee Ogilvie spoke to a group of industrial and civic leaders in Milwaukee. His speech summed up where we are in the process of reorganizing the Milwaukee and what still lies ahead. The following is a slightly abbreviated text of his remarks. I commend it to your attention and to the attention of anyone interested in the future of "Milwaukee II."

"I'd like to be able to tell you without any reservations that we shall be able to reorganize the Milwaukee. Personally, I have a strong feeling that this will be the outcome. In reality, however, the jury is still out, and so today I shall stop a bit short of that point and, instead, bring you up-to-date on a number of the recent events which lie behind our current optimism.

"We have come a long and difficult way in our efforts to restructure the Milwaukee into the kind of railroad it should be. We've had a lot of help from many quarters.... We're grateful for that help. I hope that we've been able to reciprocate with a better railroad.

"If I may assume that you are generally familiar with why the Milwaukee is in trouble and what it's been trying to do about that trouble for the past 2½ years, I'd like to concentrate on the events which have occurred over the winter and spring of 1980. Let's begin with the embargo of services on those portions of the Milwaukee which, as Trustees, Stanley Hillman and I had determined shouldn't be part of a reorganized Milwaukee Road -- indeed, couldn't be part of it without jeopardizing the financial vitality of the entire operation.

"You will recall that late last year both the Reorganization Court and the Court of Appeals affirmed the need for the embargo if anything was to survive of the Milwaukee in its own name. For a week in early November, 1979, the Milwaukee Road was projected into the future as an operating property of approximately the size we saw as being its destiny. That embargo was lifted by the passage of the Milwaukee Railroad Restructuring Act, a law which had both its good and its bad features for us, mostly bad.

"In due course, time and the Interstate Commerce Commission erased most of the bad features, but certainly not the additional debt we had incurred. The federal loans which we'd been required to accept in order to continue our operations on the entire system expired at the end of February. Judge McMillen ordered me to put the embargo back in place. I did so in two stages. The embargo became fully effective April 1.

"We began to see the beneficial results almost immediately. Suddenly, for the first time in the memory of many of our veterans, the Milwaukee Road had a suitable fleet of reliable locomotives and sufficient freight cars of virtually every type to meet the needs of its customers. As we had predicted, concentrating on approximately 3,500 miles of railroad the resources which had been spread out across 9,500 miles was of immense benefit to us and to our shippers.

"I should report to you also that during the process of installing the embargo, and since, the majority of the lines which have been embargoed were ordered by the Court to be abandoned, with the ICC's concurrence. We are well on the way to becoming the 3,500-mile railroad we should be.

"We are not, however, altogether over the summit of our long climb. There are other aspects of our reorganization process which continue to be critical.

"The Milwaukee's stockholders and some of its creditors desire us dead and liquidated. They would cut off our access to the funds we need to get through to reorganization. They have appealed from the orders which Judge McMillen has entered giving me the authority to borrow the money we need. So far, the United States Court of Appeals has backed up the District Court.

"Organized labor is appealing many of the abandonments which the Reorganization Court has ordered. Labor is also asserting that full conventional labor protection is due and payable now to affected employees. You will remember that we have long been concerned that such payments, if required, probably would consume virtually all of the available assets of the estate.

"And, of course, we have this little problem with our plan of reorganization at the ICC. Last March, the ICC rejected my plan. It also rejected a stockholders' plan which calls for liquidation, the only alternative to reorganization which I have.

"The Commission's decision on our plan reflected a rather significant change in its philosophy of rail regulation, a change which we are seeing in other activities of the Commission as well. We read the decision to say that a reorganized Milwaukee Road, or for that matter any new railroad, should be able to earn a rate of return at least equal to the cost of money for a railroad, or about 11 per cent.

"What is interesting about that decision, of course, is that for generations the ICC under other leadership was perfectly content to regulate railroads so that they earn, on the average, only about a fourth of that rate. While we find ourselves applauding the Commission's enlightenment over rates of return, we also find ourselves wishing that the Commission hadn't chosen our reorganization game plan as a time to change the rules.

"As the result of the Commission's action, and more particularly as a result of the Carter Administration's efforts to limit government credit, the Federal Railroad Administration has now taken the position that it can't be as helpful as it, and we, had contemplated.

"Frankly, the FRA's change of position gives us a problem. We are within sight of the end of our borrowing from the taxpayers. If the ICC will approve a modification of our reorganization plan, we believe that we'll be able to pay the taxpayers back, with interest. But if the federal government abandons us now, our entire reorganization scenario will be jeopardized and ultimately the cost to the taxpayers may be far greater than is their temporary investment in our survival.

"In effect, I was left by the ICC with a choice from among three courses of action: a new reorganization plan; liquidation -- that is, the piecemeal sale and abandonment of the entire Milwaukee; or the sale of 'Milwaukee II' as a going concern to another railroad. I reported to the Court on May 14 as to my choice.

"I informed Judge McMillen that we have reanalyzed the potential of 'Milwaukee II' and have projected its results into the future. We have concluded that our best course is to file a new plan of reorganization with the ICC early next year based on the results of operation as we expect them to be between now and then. We believe that 'Milwaukee II' will produce positive income from rail operations in 1982 and that it will produce bottom-line profits beginning in 1983. We believe that we can meet and indeed exceed that rate-of-return criterion set by the ICC. We can do so without the earnings of Milwaukee Land Company -- and we've got the Land Company up for sale as a way to extinguish the railroad's mortgage debt and expedite the reorganization process.

"At the same time, we cannot overlook the possibility that the sale of 'Milwaukee II' to another railroad might produce even greater benefits for our customers, our employees, and the estate. So we're talking with several railroads about that.

"I trust that the mention of this alternative doesn't unduly alarm you. It is, of course, my intention to reorganize the Milwaukee as an entity if I can do so. Yet, as we look ahead at what will be happening to the nation's railroads in the corporate sense, based on current merger activities, I think we can see that our collective destiny is as a strong industry built around perhaps no more than six major railroad companies nationwide. I suggest that we would all agree that it would be better for the Milwaukee to be included in one of those major companies than to be excluded from all of them.

"Let me leave you with this message: 'Milwaukee II' can succeed if it is given the chance. We are most appreciative of the help you've given us in coming this far. I hope that we are reciprocating in a manner that will earn your continuing support. If you can help us convince our federal regulators and federal bankers that the issue, in the final analysis, is not so much our need for a strong railroad as it is yours, then perhaps together we'll achieve the reorganization which we all so deeply desire."



W. L. Smith
President