

VERIFIED STATEMENT OF THOMAS F. POWER, JR.

I am the Assistant to the Trustee of the Milwaukee. Previously I was employed as an Assistant Vice-President in the Milwaukee Road's Planning Department. I have extensive and varied prior experience in the railroad industry with the Milwaukee and the New York Central and hold an MBA in financial management from Loyola University.

Over the last year my principal responsibilities on behalf of the Trustee have included extensive work as a liason with the consulting firm of Booz, Allen and Hamilton, analysis of the physical restructuring of the Milwaukee and development of budgets and income forecasts for the Milwaukee and various smaller configurations of the Milwaukee. In this capacity I was responsible for preparing substantial portions of the Reorganization Plan including much of the information in Sections I through IV and the associated exhibits. I am familiar with all of these Sections and believe them to be true and correct. I also supplied some information to others for use in developing Sections V through VIII.

I would like to make a correction in the Plan. Exhibit 26 should be revised to show a distance from Janesville, Wisconsin to Walworth, Wisconsin of 23.0 miles and a total of 4,938.4 miles. Milwaukee II includes service to the Kikkoman plant just outside Walworth.

In this statement I will describe how the financial forecasts set forth in the Reorganization Plan support the Trustee's conclusion that abandonment of lines not within Milwaukee II is of the utmost importance. These forecasts include a 1980 projection for the entire Milwaukee and a five year forecast for Milwaukee II. The former is based upon actual results in 1978 and forecasted 1979 results and projects a net railway operating loss in 1980 of \$170.5 million with no 4R Act rehabilitation or \$240.4 million with such rehabilitation. The Milwaukee II forecasts were developed from the Booz, Allen and Hamilton Report with adjustments as set forth at pages 26 and 32-34 of the Plan and on Exhibits 22 and 23. The results show a projected net railway operating loss in 1980 for Milwaukee II of \$104.5 million with 4R Act rehabilitation or \$34.6 million without such rehabilitation. Accordingly, requiring continued operation of lines not within Milwaukee II in 1980 would impose an additional net railway operating loss of about \$136 million.

In order to further illustrate the heavy losses imposed by lines outside of Milwaukee II, we have analyzed the 1977 base data by major system segment. The analysis is attached hereto as Appendix A. Column 1 shows actual 1977 net operating losses for the Milwaukee system of \$55.9 million. Column 2 is the pro forma 1977 Milwaukee II net operating loss of \$6.5 million developed as described in the Plan for 1980 but without any of the market opportunity considerations or cost efficiencies which are relevant in the longer time frame. Column 3 shows the losses attributable to lines west of Miles City on the basis of the breakdown contained in the report prepared by Reebie Associates for the United States Department of Transportation. We have evaluated the Report and find its methodology consistent with that used by Booz, Allen

and accurate. The data base was supplied to Reebie by the Milwaukee. This computation indicates that lines west of Miles City were responsible for \$21.1 million in losses. Column 4 shows that losses attributable to all other lines not in Milwaukee II were \$28.3 million.

Appendix B is a similar computation for 1979 showing the projected net operating loss without 4R rehabilitation expenses for the entire system of \$110.7 million, Milwaukee II net operating loss of \$20.8 million, Miles City West losses of \$46.5 million and losses for the remainder of the system of \$43.4 million. The substantial increase in Milwaukee II losses from the 1977 analysis shows the harmful effects which operating other portions of the Milwaukee has upon the operation of Milwaukee II. Without embargo and abandonment of rail services outside of Milwaukee II, traffic levels within Milwaukee II will continue to erode as a price for subsidizing the balance of the system.

The Reebie Associates breakdown of costs was based upon full allocation of costs. The Booz, Allen method of analyzing the performance of alternate configurations involves a complete and separate economic reconstruction of the alternatives and thereby avoids the problems of dealing with questions of assignment of costs. These methods are superior to attempts to allocate fixed and marginal or avoidable and unavoidable costs because they take into account the substantial opportunity costs which are currently imposed due to spreading the Milwaukee's inadequate equipment fleet across too large a system and to utilizing the equipment on slow ordered lines. The Booz, Allen approach was presented to the Court and subjected to cross examination, and a witness from Booz, Allen will appear in this proceeding. In addition, Booz, Allen's work was closely analyzed by the Federal Railroad Administration which concluded:

"the studies were carried out in a professional manner and will prove useful to the Trustee in fulfilling his responsibility for balancing public need against the protection of the corporation's assets. The approach used by the consultants and the criteria employed are, in the FRA staff's judgment, valid, consistent and reasonable, and the results will properly serve as a preliminary guide to the Trustee in developing an operating and management plan for a self-sustaining reconfigured Milwaukee Road, assuming that a decision to reorganize is taken.

As a result I do not believe that Appendix K presents a true picture of the burden of continued operation of these lines. Appendix K to the Application was prepared in full compliance with Subpart D of the Commission's abandonment regulations, but the methodology prescribed in Subpart D is of little value as applied to a mainline such as the Pacific Coast Extension.

The Commission's Subpart D methodology was designed to measure costs and revenues in the context of routine branch line abandonment proceedings. Inherent in the methodology is an understatement of avoidable costs resulting from, among other things, the variable cost approach embraced in Rail Form A, the use of historical locomotive and equipment costs and, in certain instances, the use of systemwide costs allocated to the lines to be abandoned. Moreover it overstates attributable revenues by assuming all revenue will be lost for every carload handled west of Miles City.

A basic flaw of Appendix K is that it is based on Rail Form A, which we all know Congress has already deemed insufficient for costing rail movements. That was specified in the 4-R Act where Congress mandated that the costing system -- Rail Form A -- be overhauled to bring it into the 20th Century.

Appendix K does not account for the immediate need for substantial rehabilitation. It does not account for a steadily declining revenue base resulting in part from service problems and the Milwaukee's uncertain future. It totally ignores the on-going replacement costs of power and equipment. And most of all, it does not account for the severe impact on Milwaukee's eastern lines were we compelled to continue the Pacific Coast Extension.

In recent months, we have made substantial progress in negotiations with other railroads for the purchase of railroad lines west of Miles City. I expect that agreements will be reached with the Burlington Northern and the Union Pacific Railroad Company in the next several months. In addition, we have had extensive meetings concerning rail lines in Iowa under the auspices of the FRA as mandated by Section 401 of the 4R Act. As a result of these meetings I have a high degree of confidence that the sales described on pages 34-36 and Exhibits 24 and 25 of the Plan will take place. If such agreements are reached during the 8 month period of directed service contemplated by 49 U.S.C. §11125, voluntary arrangements could be developed to assure continued service thereafter, pending final approval of sales by the Interstate Commerce Commission.

Upon completion of the sales, we estimate that Milwaukee II would service 67.5 percent of present Milwaukee originating and terminating movements, acquiring carriers would serve 29.5 percent of such movements and 3.0 percent would have no service. Doubling the 3.0 percent reaches a total of 6.0 percent of present movements which might be affected. Of shipments that traverse the territory west of Miles City, about 10% might be affected. The fact that a sale of about 680 miles of rail line

out of the 2497 which we wish to abandon will provide continued rail service to all but 5.0 percent of originations and terminations graphically illustrates the meager amount of traffic which moves on large portions of our system west of Miles City.

In conclusion, it is my belief that Milwaukee II can be successfully reorganized as an operating railroad. However, operating the lines outside Milwaukee II forces tremendous losses upon the Milwaukee and continues to jeopardize the future of Milwaukee II by depriving us of the equipment which is needed to provide proper service in this potentially viable area. I believe abandonment authority must be granted promptly not only because of the limitations imposed by available cash as Mr. Nugent will be addressing in more detail, but to assure that the viable portions of the Milwaukee can continue to provide rail service.

VERIFICATION

STATE OF ILLINOIS)  
                                  )SS  
COUNTY OF COOK)

THOMAS F. POWER being duly sworn deposes and says that the foregoing statement is true and correct to the best of my knowledge and belief.

Thomas F. Power  
(Signature)

Subscribed and sworn to before me a notary public in and for the State and County above named, this 30<sup>th</sup> day of August, 1979.

Jean M. Krascki  
Notary Public

My commission expires: June 24, 1980

APPENDIX A

PRO FORMA INCOME STATEMENT 1977  
 Stated in Millions of Dollars

	<u>System 1977</u>	<u>Milwaukee II</u>	<u>Miles City West</u>	<u>All Other</u>
Total Revenues	444.5	224.9	125.3	94.3
Total Operating Expenses	386.8	184.4	112.8	89.6
Total Taxes	42.0	18.0	12.6	11.4
Total Rents	71.6	29.0	21.0	21.6
Total Expenses, Taxes & Rents	500.4	231.4	146.4	122.6
NROI	(55.9)	(6.5)	(21.1)	(28.3)
% of Loss to System	100.0	11.6	37.8	50.6



APPENDIX B

PRO FORMA INCOME STATEMENT 1979  
 Stated in Millions of Dollars

	<u>System 1979</u>	<u>Milwaukee II</u>	<u>Miles City West</u>	<u>All Other</u>
Total Revenues	438.5	231.8	115.0	91.7
Total Operating Expenses	445.2	210.7	130.2	104.3
Total Taxes	42.1	18.4	12.7	11.0
Total Rents	61.9	23.5	18.6	19.8
Total Expenses, Taxes & Rents	549.2	252.6	161.5	135.1
NROI	(110.7)	(20.8)	(46.5)	(43.4)
% of Loss to System	100.0	18.8	42.0	39.2

\* Excludes \$30.0 million of 4R Rehabilitation Expense.