



Southern Tier West
Regional Planning & Development Board
4039 Route 219, Suite 200, Salamanca, New York 14779
Tel 716-945-5301 Fax 716-945-5550

Walter M. Martelle, Chairman
Donald R. Rychnowski, Executive Director

May 29, 1998

William E. Ingram
Director Strategic Planning
Norfolk Southern Corporation
Three Commercial Place
Norfolk, VA 23510-2191

Re: Southern Tier Extension

Dear Bill:

The following is a Memorandum of Agreement by and between Southern Tier West Regional Planning and Development Board ("STW"); the New York State Department of Transportation ("NYSDOT"); Norfolk Southern Corporation ("NS"), for itself and on behalf of Lessee (as defined herein); and Consolidated Rail Corporation ("CRC"), on behalf of PRR (as defined herein). STW executes this agreement on behalf of the New York counties of Chautauqua, Cattaraugus, Allegany, and Steuben.

WHEREAS, CRC, CSX Corporation ("CSX"), NS, and certain of their respective affiliates entered into a Transaction Agreement, dated June 10, 1997 ("Transaction Agreement"), which provides, among other things, that CSX and NS will acquire control of CRC and that CRC will form two wholly owned limited liability companies (the "LLC's"), which will acquire certain property of CRC, and

WHEREAS, the Transaction Agreement refers to a transaction involving, among other things, acquisition of control of CRC in common by CSX and NS that requires Surface Transportation Board approval under Section 11322 of the Interstate Commerce Commission Termination Act, and

WHEREAS, if the conditions of the Transaction Agreement are satisfied, including receipt of final regulatory approval, CRC will convey The Southern Tier Extension (defined herein) to one of the LLC's (hereinafter for convenience referred

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to as "PRR"), and

WHEREAS, if the conditions of the Transaction Agreement are satisfied, including receipt of final regulatory approval, PRR will lease or make available the operation of its assets (including the Southern Tier Extension) to railroad operating affiliates of NS (such affiliates being hereinafter for convenience referred to as "Lessee"), and

WHEREAS, CRC, CSX, NS and certain of their respective affiliates entered into an Agreement and Plan of Merger, as amended, which provides, among other things, that CRC may not abandon any of its lines of railroad without the consent of NS and CSX,

NOW, THEREFORE, STW, FOR ITSELF AND ON BEHALF OF THE NEW YORK COUNTIES OF ALLEGANY, CATTARAUGUS AND CHAUTAUQUA; NYSDOT; NS, FOR ITSELF AND ON BEHALF OF LESSEE; AND CRC, ON BEHALF OF PRR, AGREE AS FOLLOWS:

1. **Southern Tier Extension.** The term "Southern Tier Extension" refers to Conrail's line between a connection with the Conrail Southern Tier Line at Hornell, New York (Cass Street interlocking, MP 331.8 +/-) and a connection with the line of the Northwest Pennsylvania Rail Authority at Corry, Pennsylvania, comprising all of the rail lines and facilities between those points that are the subject of the "Southern Tier Agreement" dated October 12, 1982 between Conrail and NYSDOT, as amended. NYSDOT and STW represent and warrant to PRR and Lessee that the Southern Tier Agreement, as amended, contains any and all understandings by, between, and among Conrail, NYSDOT and STW, or any of them, concerning the Southern Tier Extension, as of the date of this agreement. PRR and Lessee represent and warrant that they will use their best efforts to re-establish a connection with the Allegheny & Eastern Railroad at Corry.
2. **Operation and Maintenance by PRR or Lessee.** During the term of this agreement, and except as otherwise provided herein, PRR or Lessee agree to operate and maintain the Southern Tier Extension in accordance with the following standards:

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- **Local freight service.** The line will be operated "as needed" unless car volume exceeds the threshold volumes indicated in the Southern Tier Agreement, whereupon service will be scheduled as indicated in the Southern Tier Agreement. The parties hereby stipulate that 1989 Southern Tier Extension carloadings between Olean and Jamestown were 1,500 cars. At any time during the term of this agreement, PRR or Lessee may request that the threshold volume described above be adjusted based upon economic necessity. STW's consent to such a request shall not be unreasonably withheld. PRR or Lessee will faithfully perform its common carrier obligation to provide transportation service upon request to any point on the line to which service has not been formally abandoned. Pricing actions will not be used to frustrate the objective of this agreement to maintain service and promote economic development, but nothing herein shall obligate PRR or Lessee to price its services below rates giving PRR or Lessee economic returns on the movements.
 - **Maintenance.** Between Olean and Jamestown, if PRR or Lessee finds that the line is not at Federal Railroad Administration Class 2 standards, then PRR or Lessee have twenty-four (24) months from the Closing Date, as that term is defined in paragraph 7 below, to achieve compliance with Class 2 standards at a minimum; thereafter, the line shall have no more than ten (10) miles that fails to meet or exceed Class 2 standards. Other segments will be maintained to a standard adequate to support as-needed service.
3. **Sale/Leaseback; Property Tax Abatement.** As more fully described in the Addendum hereto, PRR and an acquiring entity (hereinafter, "the Acquiring Entity") designated by STW will enter into a sale/leaseback transaction providing property tax abatement for PRR or Lessee:
- 100% property tax abatement during each of the first seven years.
 - After the first seven years, the schedule of payments-in-lieu-of-taxes ("PILOT payments") shown in Exhibit A will apply.

4. **Abandonment of Service.** In the event PRR petitions the Surface Transportation Board to abandon its operating rights over any segment of the Southern Tier Extension, the Acquiring Entity shall have the right to acquire all of PRR's rights with respect to such line segment (including operating rights and the right to re-acquire the segment) for the then-current Net Liquidation Value ("NLV") of the segment to be abandoned, *less* the product of (1) the Depreciation Factor and (2) the sum of:

- a.) the cumulative value of net tax abatements granted to the date of abandonment with respect to the segment to be abandoned, where "net tax abatements" shall mean the property taxes that would have been due in each year, less PILOT payments that were due in the same year, plus interest on the cumulative difference compounded annually at an interest rate of 7.5%;
- b.) the cost of any capital improvements thereto funded by the Acquiring Entity or by Allegany County, Cattaraugus County, Chautauqua County, Steuben County, and/or the City of Hornell, if and to the extent that the cost of such capital improvement is included in the NLV; and
- c.) a portion of \$2.136 million, prorated as follows:

$$\frac{\text{route miles to be abandoned}}{128 \text{ route miles in New York State}} \quad \times \quad \$2,136,000$$

Where the Depreciation Factor is:

Until December 31, 2008	100%
From January 1, 2009 To December 31, 2016	A percentage between 100% and zero representing straight line depreciation month-by-month

5. **Abandonment by CRC.** NS agrees that it will not consent to any CRC petition to the Surface Transportation Board to abandon any part of the Southern Tier Extension before NS and CSX Corporation obtain control. In

the event that CRC otherwise removes track or other facilities deemed by the agreement to be part of the Southern Tier Extension, NS will take such steps as it may legally take, if any, to prevent such removal, and will cooperate with STW and NYSDOT in opposing such removal.

6. **Transfer of operating rights.** Rights and obligations under this Agreement may be subdivided, assigned, conveyed, sub-leased, or sold, other than to a subsidiary or affiliate, only with the consent of the Acquiring Entity; *provided, however*, that such consent shall not be unreasonably withheld, and shall not be required for PRR or Lessee to grant overhead trackage rights to another carrier.
7. **Term of Agreement.** The term of this agreement shall be from the date first shown above to December 31, 2008. The Acquiring Entity's rights under paragraph four shall survive the termination of this agreement and run until December 31, 2016. This agreement shall be binding upon all parties from the beginning of the term, but shall not become effective until the Closing Date, as that term is defined in the Transaction Agreement.
8. **Discharge of NYSDOT Obligation.** NYSDOT agrees that in consideration for the undertakings of the parties hereunder, CRC's indebtedness to NYSDOT with respect to the TCS-Wellsville project, as that matter is referred to in the Southern Tier Agreement as amended, is hereby discharged.
9. **NYSDOT Support.** As a party of record before the Surface Transportation Board in the CRC control case, NYSDOT agrees that, with respect to the Southern Tier Extension, this agreement achieves NYSDOT's objectives in connection with the division of CRC.
10. **STW Support.** As a party of record before the Surface Transportation Board in the CRC control case, STW agrees that in consideration for the undertakings of the parties hereunder, it supports the proposed division of CRC, and will provide a letter to the Surface Transportation Board to that effect.

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11. **Consent of the Counties.** The agreement is conditioned upon the unconditional consent of all four counties, which shall be furnished in writing to CRC and NS by STW no later than 90 days after the date first shown above.

12. **Rights as to Capital Improvements.** With respect to the line between Hornell and Wellsville, the Acquiring Entity shall have the right to make capital improvements to this line segment necessary to repair washouts and restore the line to in-service condition while it is under lease to PRR; provided:
 - a.) Such repairs and improvements are approved in advance by PRR or Lessee, which approval shall not be unreasonably withheld;
 - b.) The Acquiring Entity shall contract with Lessee or a third party to perform such work; and
 - c.) All such work shall be at the sole expense of the Acquiring Entity; which shall have the right to approve or disapprove budgeted costs in advance.

PRR or Lessee shall have no obligation to repair washouts and reopen the line between Hornell and Wellsville, provided PRR or Lessee otherwise is able to perform the service obligations described in paragraph two above.

With respect to the line between Corry and Wellsville, the Acquiring Entity shall have the right to fund, and PRR or Lessee shall have the obligation to make, capital improvements to be performed by PRR or Lessee forces or contractors retained by PRR or Lessee, subject to the terms of subparagraphs (12a) and (12c) of this paragraph. The Acquiring Entity shall have no obligation to make or fund capital improvements to any part of the Southern Tier Extension.

13. **Relations with the Northwest Pennsylvania Rail Authority.** The parties hereto agree to oppose any request for conditions in the Conrail control case that purports to limit or obstruct utilization by PRR or Lessee of a continuous line of railroad between Erie, Pennsylvania; Corry, Pennsylvania; and

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Jamestown, New York, including the Southern Tier Extension between milepost 60.5 +/- and milepost 60.8 +/- at Corry, Pennsylvania.

14. **Insurance and Liability.** The parties agree that insurance and liability issues relating to the Southern Tier Extension shall be addressed in the operating agreement for the Southern Tier Extension.

If this letter agreement is acceptable, please indicate by having an authorized officer sign below.

for the Southern Tier West Regional Planning and Development Board

Name

Title

Date

for the New York State Department of Transportation

Name

Title

Date

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for Norfolk Southern Corporation, for itself and on behalf of Lessee

Name

Title

Date

for Consolidated Rail Corporation, on behalf of PRR

Name

Title

Date

ADDENDUM

Sale/Leaseback -- Property Tax Abatement

- A. Not more than 120 days after the Closing Date (as that term is defined in paragraph seven of the agreement), PRR will sell the Southern Tier Extension for \$1 to an acquiring entity designated by STW (hereinafter, "the Acquiring Entity"). In the event that such a sale is delayed through no fault of PRR until after the spring 1999 taxable status date(s), STW will use its best efforts to obtain property tax abatements for PRR or Lessee as if such sale had occurred before such taxable status date(s). In the event STW is unable to obtain such property tax abatement for the initial year contemplated herein, then the schedule of PILOT payments shown in Exhibit A attached hereto shall be adjusted to provide for 100% tax abatements in each of year 8 and year 9, plus the \$20,000 PILOT fee.
- B. Simultaneously, PRR and the Acquiring Entity will enter into an agreement whereby:
- 1.) PRR may at any time at its option re-acquire the Southern Tier Extension for \$1 plus the cost of any capital improvements thereto funded by the Acquiring Entity, plus the cumulative value of any net tax abatements, where "net tax abatements" shall mean the property taxes that would have been due in each year, less PILOT payments that were due in the same year, plus interest on the cumulative difference compounded annually at an interest rate of 7.5%;
 - 2.) Except as otherwise provided herein, on December 31, 2008 PRR must re-acquire the Southern Tier Extension for \$1 plus the cost of any capital improvements thereto funded by the Acquiring Entity; and
 - 3.) During the term of the agreement, PRR or Lessee will, except as otherwise provided herein, lease the sole and exclusive right to operate and maintain the Southern Tier Extension.
- C. As consideration for the lease, PRR or Lessee will each year make payments in lieu of taxes ("PILOT payments") based on the formula shown in Exhibit A and the schedule shown in Exhibit B.
- D. The Acquiring Entity shall each year calculate and provide to PRR or Lessee the cumulative value of net tax abatements granted to PRR or Lessee

hereunder, including interest. Assessed value will be based on the 1998 assessment ceilings published by the State of New York for each jurisdiction in which the Southern Tier Extension runs.

- E. Liability for property taxes in New York State is determined by the "taxable status date" which varies from one jurisdiction to the next but generally falls between January 1 and June 1. Ownership as of the taxable status date in a given year establishes liability for any school, village, town, city, or county taxes that come due in the same year and/or the following year, depending upon the tax (refer to Exhibit B).

The next taxable status dates following the CRC Closing Date should be those occurring in the spring of 1999. Thus the first taxes to be abated would be the school taxes due in September 1999 and the village, town, and county taxes due in 2000. The last taxes to be abated would be the school taxes due in September 2008 and the village, town, and county taxes due in 2009 (refer to Exhibit B).

- F. PRR or Lessee will be solely responsible for any lease payment that may be due to the Seneca Nation of Indians during the tax abatement period.

EXHIBIT A

Payment in Lieu of Taxes (PILOT)

<u>Year (1)</u>	<u>Total PILOT Due (2)</u>		
1	0%	+	\$20,000
2	0%	+	\$20,000
3	0%	+	\$20,000
4	0%	+	\$20,000
5	0%	+	\$20,000
6	0%	+	\$20,000
7	0%	+	\$20,000
8	33%	+	\$20,000
9	66%	+	\$20,000
10	100%	+	\$20,000

Notes

1. "Year" refers to the year of the ten-year abatement period, running from 1999 through and including 2008.
2. The total Payment in Lieu of Taxes (PILOT) percentage figure indicates an amount which is a percentage of taxes for which PRR or Lessee would become liable as of the current year's tax status date, if PRR owned the line, plus an annual abatement fee of \$20,000.

EXHIBIT B

<u>PILOT Due</u>	<u>Based On Tax Status As Of</u>	<u>Replaces School Taxes Due</u>	<u>Replaces Town/County Taxes Due</u>
12/31/99	spring 1999	Sep 1999	Jan 2000
12/31/00	spring 2000	Sep 2000	Jan 2001
12/31/01	spring 2001	Sep 2001	Jan 2002
12/31/02	spring 2002	Sep 2002	Jan 2003
12/31/03	spring 2003	Sep 2003	Jan 2004
12/31/04	spring 2004	Sep 2004	Jan 2005
12/31/05	spring 2005	Sep 2005	Jan 2006
12/31/06	spring 2006	Sep 2006	Jan 2007
12/31/07	spring 2007	Sep 2007	Jan 2008
12/31/08	spring 2008	Sep 2008	Jan 2009

Notes

1. Due dates for City and Village taxes vary with the municipality.
2. Agreement term ends December 31, 2008.
3. In each year, the total PILOT payments due to the Acquiring Entity shall consist of the percentage-based PILOT component and an annual abatement fee of \$20,000. These total PILOT payments are indicated in Exhibit A.