

The Milwaukee Road's Demise, Notes From Michael Sol

- On April 23, 1979 Hillman formally asked for permission to terminate operations on all but 2,400 miles of its 9,800 mile system, citing losses of \$82 million in 1978, and losses of \$45 million in the first quarter of 1979. Hillman also asked to reduce employees from 10,000 to 5,000.

- Two days before the scheduled May 4, 1979 hearing on the Trustee's motion to abandon all but 2,400 miles of track, the Federal Railroad Administration offered \$20 million to keep the lines operating until August, pending Congressional action. On Thursday of that week, a day before the hearing, the Senate Energy Committee passed a resolution urging rejection of any shutdown of any Milwaukee lines.

- Melcher's Milwaukee bill passed the Senate May 3, 1979 and on May 4, McMillen "reluctantly" overruled his special master's recommendation of embargo, and ordered the Milwaukee to keep running, that funds appeared to be available and that further action should await Congressional intervention which was "the only foreseeable alternative" to shutting down.

- In mid-May, 1979, Hillman received his consulting report which showed that the only likely configurations for a successful reorganization of the Milwaukee included Lines West.

- In June, the Trustee requested an embargo of all of the Milwaukee lines west of Miles City, but was turned down by Judge McMillen because he did not find the Railroad was so strapped for cash as to require such a shutdown.

- Hillman resigned July 24, 1979.

- On August 10, 1979, the new Trustee, Richard Ogilvie, filed a plan for reorganization of the Milwaukee Road, proposing to slash the railroad from 9,800 miles of line to a core system of 3,400, concentrated in the Midwest, and called "Milwaukee II". Ogilvie called for an "embargo" of the Company lines west of Miles City, Montana to take place October 1, 1979.

- On September 7, Congress began hearings on the Milwaukee crisis, and the ICC began holding hearings in September and October on the Milwaukee's abandonment proposals.

- A railroad employee from Tacoma had burgled the local office and had found documents from Chicago -- management instructions -- ordering the local Milwaukee Road sales forces to discourage selling transportation service for many commodities.... Ploss recognized them for what they were, a near-complete list of everything the Milwaukee Road historically had carried to the east. For years the railroad's management had been turning down available business for the transcontinental line. [Ploss]

- Port of Seattle authorities were concerned that neither the Union Pacific nor the

Burlington Northern had been particularly interested in handling the rapidly expanding container traffic through the ports, and that while the Milwaukee had been physically able to, it had introduced lower rates than the BN and the UP, and as a result had captured nearly 50% of all container traffic out of Seattle prior to 1978, leaving the UP with 36% and the BN with only 16%. Overall, the Milwaukee had a near monopoly of more than 76% of Port of Seattle business, which was booming.

-- The Port of Tacoma thought that the Milwaukee's services were more important to the country as a whole than Chrysler Corporation's, and asked, if the government could advance a billion dollars to Chrysler, why it could not make similar commitments to the Milwaukee.

-- The Milwaukee Road's Vice President of operations admitted that it was not for lack of demand that the Company's lines west of the Twin Cities were necessarily unprofitable, but that "demand has far exceeded the Milwaukee's ability to provide an adequate freight car supply."

-- Terry Cook, a clerk, told the ICC that although the Milwaukee was enjoying a good profit and large volume on lumber traffic originating in British Columbia, the Milwaukee's Chicago offices inexplicably announced that it was going to raise rates, above those of the Burlington Northern. Naturally, the shippers there switched to the BN. Another rate clerk testified that just prior to the Milwaukee's filing of the bankruptcy petition, all rate quotations to shippers were transferred to Chicago, resulting in delays of up to two days for a rate, which was unacceptable in such a competitive environment.

-- On October 2, 1979, the 7th Circuit Court of Appeals stated that McMillen did have the power to authorize the Trustee to embargo portions of the system because of lack of funds to operate it, even though it was not for lack of demand, which far exceeded capacity. For the first time in a railroad Bankruptcy proceeding, the public interest -- defined by an unprecedented existing demand for services -- was not a consideration.

-- The Trustee, rushing to Judge McMillen, obtained an order authorizing embargo of that portion of the Milwaukee Road west of Miles City, Montana as of November 1, 1979. The Judge found that the Company was "cashless" and that any loans the Company might receive from the government would be at the expense of the creditors, both secured and unsecured, which the Judge found unpalatable because of his "repeatedly expressed concern for the interests of the shareholders" and the creditors.

-- On October 30, the ICC petitioned Judge McMillen to delay his embargo order, pending Congressional action, and informing the Judge that the ICC would not order other railroads to provide service over the Milwaukee lines, unless Congress ultimately failed to act. McMillen rejected the ICC's application. "I feel unhappy about the effect the embargo will cause for shippers and other parties ... however, the railroad has done everything it can, and the trustee has to protect the railroad's creditors and its stockholders." On November 1, the transcontinental operations of the Milwaukee Road ceased. On that date, the Carter administration sought \$1 billion in loan guarantees for

Chrysler Corporation.

-- Congress rushed to provide legislation, prodded by Washington State's Senator Warren Magnuson, and Montana's Senators Baucus and Melcher. Congress was making a "desperate effort to save the Milwaukee Road," stated Magnuson.

-- On November 4, 1979, President Carter signed into law the Milwaukee Railroad Restructuring Act, which provided that an association composed of representatives of labor, employee coalitions, and shippers could submit to the Interstate Commerce Commission a proposal to convert the Milwaukee Road into an employee or an employee-shipper owned company. The legislation also provided for lifting the embargo at least until January 1. McMillen lifted it the next day. Ominously, it also implemented several of the revisions that DOT had been pressing for in its restructuring of the relationship of the bankruptcy courts and the jurisdiction of the ICC. The Milwaukee Road would be an example of how DOT thought that railroad reorganizations should be handled.

-- On December 16, the ICC held hearings, and on December 31, found that the plan was not feasible because of a lack of financing, over-optimistic traffic assessments, under-estimation of the costs and time factors involved in rehabilitating the Milwaukee Road's western lines, and underestimation of the costs involved in acquiring the necessary equipment to operate the system. In addition, the ICC found that the NewMil plan would leave the old Milwaukee with most of the debt of the Company, and take \$533 million worth of assets out of the old Company's estate, which would be an impermissible taking from the shareholders and creditors. "The Commission has determined that NewMil's plan lacks adequate financing, is not fair and equitable to the Milwaukee estate, and does not propose a railroad that can be operated on a self-sustaining basis," the ICC said. The decision was 7-0. Darius Gaskins, then-ICC chairman, later remarked that it seemed to be one of the most difficult decisions that the ICC made during his tenure there. He later became president of the Burlington Northern Railroad.

The disappointed employees attempted to regroup to determine if a new plan could be submitted. The ICC had stated that "it should be emphasized that the commission supports the concept of rail competition across the northern tier of states. Specifically, this plan (the New Milwaukee) seems sensible from the standpoint that should it be feasible, it would maintain the presence of the successor to the Milwaukee as a competitor across the northern tier of states."

On the transcontinental line, meanwhile, the Trustee began terminating operations. The Company pulled all of the SD-40 heavy mainline diesel locomotives back to the Midwest, and transcontinental trains were badly underpowered. Repeated engine failures and shortages "gave the company a chance to divert West Coast business to the Union Pacific, which they were quick to do and made little effort to recover ...". Further demoralizing to employees was the sight of some of the big Milwaukee SD-40's on parallel Burlington Northern tracks. In spite of Milwaukee power shortages, and pleas by the Trustee and his Operations Vice President that lack of equipment prevented the

Milwaukee from carrying the unprecedented demand for services in its operating territory, the same Trustee was willing to lease the Milwaukee's best units to its arch rival to alleviate its own power shortages!

-- The Trustee made immediate application to the ICC to abandon all lines west of Miles City, Montana. On January 30, 1980, the ICC rejected the Trustee's Motion. The ICC recommended that the Bankruptcy Court not make any decisions regarding abandonment of any portion of the transcontinental line until after a plan of reorganization was approved, upon the premise that such a plan might well include lines west of Miles City, Montana.

-- The ICC also acknowledged the Trustee's error regarding the profitability of the Milwaukee Road's transcontinental operations. Instead of the terrible cash drain that Trustee Hillman had alleged, the ICC carefully reviewed the Milwaukee's own books and found that lines west of Miles City had contributed \$12.7 million in profits in 1976, \$11 million in 1977, and \$2.9 million in 1978, while the railroad as a whole had been losing \$100 million in those years. In other words, only the aggressive actions of the Trustee in driving away transcontinental business had made the line unprofitable at all. SORE officials were relieved that the ICC acknowledged that the Trustee had been using misleading figures. No economic rationale existed for scrapping the Milwaukee's transcontinental lines.

The discovery was too late. The inexorable grinding away of the reorganization machinery had made the Milwaukee Road's plight irreversible. On February 25, 1980, the Bankruptcy Judge granted the Trustee's new motion to embargo -- cease operations -- on the Milwaukee Road's transcontinental line west of Miles City, Montana. The Company began its departure from the Pacific Northwest. On February 27, operations were concluded in Washington State, including Mineral Turns and WAM operations between Morton and Chehalis, and all traffic from or to destinations on the Milwaukee were transferred to the nearest Burlington Northern or Union Pacific exchange.

-- There were some suggestions that Congress might again intervene, and the State of Montana was desperately negotiating to purchase that portion of the line between Miles City, Montana and Marengo, Washington, but the Trustee had arbitrarily set midnight March 1, 1980 as the deadline for Montana to raise \$55 million to purchase the line. The State was unable to commit by that date.

Montana Governor Judge complained that Montana's Congressional delegation had hampered efforts by its inability to support one clear alternative proposal. Instead, Senator Melcher was supporting the NewMil proposal, Congressman Williams wanted to call a special legislative session and Senator Baucus as well; Max, as usual, straddled the fence.

The Carter administration knew it was going to lose Montana in the upcoming election, and didn't see any gain in allocating federal dollars to Montana. Carter Administration officials told Governor Judge that there wasn't any political gain in Carter's election

efforts against Ronald Reagan in helping Montana save the Milwaukee, and federal funds would go to places where it would help Carter's re-election efforts.

By March 1, all non-Milwaukee cars were to be off of the line, and all equipment and records were to be evacuated by March 16. Company crews manned work trains picking up derailment casualties which had been left along the tracks during the previous decade, and loaded these on flatcars, or cut into scrap for the gondola cars. Seventy years of records were loaded into boxes and tossed into boxcars; much into dumpsters.

Decrepit trains with ancient engines slowly moved the Milwaukee's equipment east to St. Paul, and for the first two weeks of March, 1980, these funeral trains hauled an exotic variety of boxcars, ancient steam tenders, rotary plows, antique ex-passenger cars, maintenance equipment, speeder cars, records, and the various paraphernalia that the Milwaukee Road had accumulated in its western attic for most of the twentieth century.

On March 15, 1980, at 8:47 p.m., Extra 5802 East cleared Tacoma Junction for its long sad night trip over the Cascades, and then the Saddle Mountains, the Bitterroot Range, the Rockies, and across the Prairie to the Midwest that had spawned the Railroad 140 years earlier. It was the last train and behind it was a dead railroad: the end of the Pacific Extension.

Newspapers would "carry no news accounts, run no photos, allot not even a pica of lineage to the "electric trains" so much a part of the St. Paul's history in the Far West." Recalling the nerve and daring of the Board of Directors in 1905, daring to invade the Northwest to compete head-on with the Great Northern, Northern Pacific and Union Pacific for transcontinental traffic, one paper remarked, somewhat accurately, the Milwaukee Road "came as a gambler ... and it lost."

Further information concerning the Milwaukee Road's bankruptcy:

-- On August 8, 1979, Milwaukee Road filed its Application to Abandon, Lines West of Miles City. In that application, Milwaukee Road conceded that the lines proposed for abandonment had been generated positive net income for the years 1976, 1977 and 1978, during years that the railroad as a whole suffered substantial losses. Hillman signed off on this prior to his resignation although it was filed after that date.

Hillman's health went into a decline -- a perforated ulcer -- after receiving the Consulting Report. He clamped an embargo on the findings of the Consulting study. The Study showed that the transcontinental alternative -- the "Louisville Transcon" which was essentially the NewMil proposal -- would have substantially higher profitability, lower capital needs, and retain more employees than the proposed Core alternatives.

I asked Judge McMillen about this alternative, and he was quite troubled. He had never heard of it as anything other than the NewMil plan which had been roundly

derided by the Trustee. He was astounded to learn that it was the preferred alternative for the Trustee's own Consulting Report and which he, McMillen, had been led to believe was the basis for the Trustee's Plan of Reorganization. What had been represented to him, the Judge, as the "preferred alternative" under the Study was not, in fact, the preferred alternative under the Study.

The Federal Judge in charge of the Milwaukee Road bankruptcy had been, in fact, specifically misled as to the results of the key study on reorganization. He was never advised that Milwaukee Road's own internal study agreed explicitly and specifically with the virtually identical NewMil plan as the configuration of the Milwaukee Road most likely to succeed.

Hillman, according to the senior executive officer working directly with him on reorganization, became "difficult to work with" after he read the Consulting Report.

- *Michael Sol*