

MINUTES

BOARD OF DIRECTORS MEETING OF THE SAN DIEGO & ARIZONA EASTERN RAILWAY COMPANY

July 16, 2013

A meeting of the Board of Directors of the San Diego & Arizona Eastern (SD&AE) Railway Company, a Nevada corporation, was held at 1255 Imperial Avenue, Suite 1000, San Diego, California 92101, on July 16, 2013, at 9:00 a.m.

The following persons, constituting the Board of Directors, were present: Brad Ovitt, Matt Domen, and Paul Jablonski. Also in attendance were members from:

San Diego Metropolitan Transit System:	Tim Allison, Karen Landers, Wayne Terry, Tom Lynch
Pacific Southwest Railway Museum:	Diana Hyatt
Pacific Imperial Railroad, Inc.:	Ernest Dahlman, Chas McHaffie, Sheila LeMire
Burlington Northern Santa Fe:	John Hoegemeier

1. Approval of Minutes

Mr. Jablonski moved to approve the Minutes of the April 16, 2013, SD&AE Railway Board of Directors meeting. Mr. Domen seconded the motion, and it was unanimously approved.

Mr. Ovitt offered his congratulations to Mr. Domen who was promoted from Assistant General Manager to General Manager of SD&IV.

2. Statement of Railway Finances

Tom Lynch, MTS Controller, presented the report for Linda Musengo (who was unable to attend the meeting). The financial statement for the second quarter of 2013 was distributed at the meeting (attached).

Action Taken

Mr. Jablonski moved receive a report for information. Mr. Domen seconded the motion, and it was unanimously approved.

Karen Landers added that there was also an action to forward a recommendation to the MTS Board of Directors to elect Erin Dunn, MTS Assistant Finance Manager, as Treasurer to replace Linda Musengo (who is retiring). Ms. Landers stated that Ms. Dunn will be assuming the position of MTS Finance Manager. Mr. Lynch reported that Ms. Dunn is a CPA and is very well qualified.

Action Taken

Mr. Domen moved to forward a recommendation to the MTS Board of Directors to elect Erin Dunn as SD&AE Treasurer to replace the position being vacated by Linda Musengo. Mr. Ovitt seconded the motion, and it was unanimously approved.

3. Report on San Diego & Imperial Valley Railroad (SD&IV) Operations

Matt Domen reviewed the report of activities for the second quarter of 2013 (attached to the agenda item).

Action Taken

Mr. Jablonski moved to receive the report for information. Mr. Domen seconded the motion, and it was unanimously approved.

4. Report on Pacific Southwest Railway Museum Operations

Diana Hyatt reviewed the second quarter of 2013 report (attached to the agenda item).

Action Taken

Mr. Jablonski moved to receive the report for information. Mr. Domen seconded the motion, and it was unanimously approved.

5. Report on the Desert Line

A written report (attached) was not submitted in time for the meeting. Chas McHaffie stated that milestones (for the Desert Line) that are timely today include the half-million-dollar fee paid (by PIR) in June (to MTS). The proposals for J. L. Patterson to do bridge inspections have been signed and paid. Watkins Environmental and Watkins Construction have been retained to operate the construction program on the Desert Line.

Mr. McHaffie reported that PIR is in negotiations with Pacific Imperial Railroad de Mexico to consolidate the operating lease with Mexican business authorities. Mr. McHaffie will report back at the next meeting regarding the success of that endeavor.

Ms. Landers stated that PIR's report must be submitted prior to the meeting. She reiterated that the meeting schedule and due dates are preset, and reports should be submitted without prompting. Ms. Landers added that she does not want to have to make this request at every meeting and expects these reports well in advance of the meetings. Mr. McHaffie agreed and stated that he would send the updated report to the clerk via e-mail right after the meeting.

Mr. Jablonski asked about the schedule for Desert Line rehabilitation. Mr. McHaffie responded that weed clearing will begin next week, and payment will be made this week to Watkins Construction. Tim Allison added that he has not received any right of entry permit requests from Watkins Construction. Mr. Allison stated that last week, he prompted Damon Barone (Chief Operating Officer) of Watkins Construction to get a right of entry application submitted for Watkins to work on the line and that no one other than PIR employees should be out there working without a permit.

Mr. Jablonski asked for clarification of the priorities of work on the Desert Line. Mr. McHaffie responded that weed abatement is the top priority due to fire risks. Sheila LeMire added that in order to run the ultrasound machines on the line to test the ties and rail, the line must be cleared of brush before repair work can commence. It was noted that PIR is responsible for 70 miles of line, and the Museum is responsible for 6 miles.

Mr. Allison reported that there was a kickoff meeting at Don Stoecklein's office last week with

J. L. Patterson representatives and Damon Barone of Watkins Construction (hereinafter referred to as "contractors"). A baseline schedule will be modified and resubmitted, which will show all of the different work services. The contractors are going to clear the gauge so they can run the ultrasound machine and process the entire line. Mr. Allison stated the contractors have contacted the Federal Railroad Administration (FRA) and California Public Utilities Commission (CPUC) regarding the proposed work so they can get onboard prior to commencement. Mr. Allison added that he feels that J. L. Patterson has a good handle on the duties.

Wayne Terry clarified for Mr. Jablonski that a private contractor is hired to perform the ultrasound on the Desert Line rails. Mr. Allison added that Fred Byle, MTS Superintendent of Wayside Maintenance, is available as a resource.

Mr. Jablonski requested a copy of PIR's schedule for work on the Desert Line. Mr. McHaffie clarified for Mr. Ovitt that the schedule for brush clearing begins next week (a right of entry permit will be required).

Action Taken

Mr. Ovitt moved to receive the report for information. Mr. Jablonski seconded the motion, and it was unanimously approved.

6. Real Property Matters

6a. Summary of SD&AE Documents Issued Since April 16, 2013

Since the April 16, 2013, SD&AE Railway Company Board of Directors meeting, the documents described below have been processed by staff.

- S200-13-559: Right of Entry Permit to SDG&E for a transformer removal at the Lemon Grove Depot in the City of Lemon Grove.
- S200-13-562: Right of Entry Permit to Navy Region Southwest for the Bay Bridge Run/Walk.
- S200-13-563: Easement to SDG&E for power service to a new traction power substation at Seaward Avenue in the City of San Diego.
- S200-13-564: Easement to SDG&E for power service to a new traction power substation at 27th Street in the City of San Diego.
- S200-13-565: Easement to SDG&E for power service to a new traction power substation at Market Creek Plaza in the City of San Diego.
- S200-13-567: Easement to SDG&E for power service to a new traction power substation at 13th Street in the City of San Diego.
- S200-13-568: Right of Entry Permit to PAR Electrical Contractors Inc. for electric facilities removal at 24th Street in the City of San Diego.
- S200-13-569: Right of Entry Permit to the City of La Mesa for the La Mesa Flag Day Parade.

- S200-13-570: Right of Entry Permit to COMM22 Family Housing L.P. to construct residential housing at 24th Street in the City of San Diego.
- S200-13-571: Easement to SDG&E for power service to a new traction power substation at Palm Avenue in the City of San Diego.
- S200-13-572: Right of Entry Permit to Flatiron West, Inc. to construct the Blue Line Low-Floor Station Improvements project.
- S200-13-577: Right of Entry Permit to Aguirre Engineering for general land surveying on SD&AE right-of-way.
- S200-13-578: Right of Entry Permit to the San Diego County Bicycle Coalition for the Bike the Bay fun bike ride.
- S200-13-579: Right of Entry Permit to SDG&E for pole removal and overhead wire transfer at Moss Street in the City of Chula Vista.

Action Taken

Mr. Ovitt moved to receive the report for information. Mr. Jablonski seconded the motion, and it was unanimously approved.

6b. Easements for an At-Grade Crossing at the U.S./Mexico Border in San Ysidro

Tim Allison showed an overhead of the proposed easement to the Department of Homeland Security (DHS) for a commonly used access road (by DHS and the U.S. Border Patrol) at the south line on the San Ysidro border known as the Durand Gate. Mr. Allison explained that the Board previously authorized two similar easements on the Desert Line to access the border fence. He reviewed the overhead and explained the layout of the area.

Mr. Allison explained that the San Diego Association of Governments (SANDAG) is requesting a quit claim deed from the U.S. Government for property near Beyer in relation to the San Ysidro Intermodal Yard Expansion Project. DHS wants to make sure that this easement is in place. Mr. Allison and Ms. Landers have been working on the language for the indemnification to address the U.S. Government's issues.

Mr. Allison clarified for Mr. Jablonski that this request will be in addition to the other two easements. Ms. Landers clarified that this request is tied up with the San Ysidro Intermodal Yard Project, which may not be able to move forward unless some of the issues are resolved.

Discussion ensued regarding the layout of the easement. Mr. Ovitt clarified that although the easement has been accessed for years, we will now get compensation for its use. Ms. Landers added that it's the indemnification that will have the most value as the easement fees are fairly nominal. Ms. Landers stated that she recommends being cooperative in granting the easement agreement.

Mr. Domen stated that the Baja Railroad is going to replace the rail between the border fences. He reported that the Border Patrol cemented over the rails years ago without permission, and now it needs to be repaired. Mr. Domen asked who will pay for that expense. Mr. Jablonski stated that the Border Patrol should be required to make a legitimate track crossing. Mr. Allison agreed, and conversation continued about needed improvements to the easement.

Ms. Landers added that the time is now to have this discussion (before granting the easement). It was agreed that terms would be included in the language requiring repairs if there is any damage to the easement. Ms. Landers explained that the U.S. Government says it can't agree to a contract that's not already appropriated by Congress and states that you have to file a federal tort claim for liability claims outside of its contract.

After discussion regarding the property and the upcoming improvement project, it was agreed that property-line research of the proposed easement area should be conducted to determine ownership, and improvements or damage repair by DHS should be incorporated into the permanent easement agreement. Mr. Allison will schedule a meeting with DHS to address these issues. He added that there will also be an at-grade construction and maintenance agreement.

Action Taken

Mr. Jablonski moved to approve issuing an easement to the U.S. Department of Homeland Security (DHS) for an at-grade crossing over SD&AE tracks located at the U.S./Mexico border in San Ysidro contingent upon resolution of the terms of crossing-improvement criteria. Mr. Domen seconded the motion, and it was unanimously approved.

7. Board Member Communications

There were no Board member communications.

8. Public Comments

- Denis LaSalle – Representative of Consejo De Desarrollo Economico De Tijuana

Mr. LaSalle stated that Donald Stoecklein (of PIR) made a presentation a few weeks ago at Toyota and said that the Desert Line will be operable in January 2014 to move cargo to the maquiladoras. Mr. LaSalle added that businesses in Mexico are interested but won't sign on until the SD&AE Board approves the contract. He added that they are also concerned about the security of the cargo headed for the maquiladoras and the number of milestones required in the contract. He asked for confirmation by the SD&AE Board of the January 2014 start date.

Mr. Jablonski responded that the January 2014 start date is not listed as a milestone in the contract between SD&AE and PIR. He added that PIR can keep its deadlines and milestones, but he is not going to speak for PIR. Mr. Jablonski stated that the SD&AE Board will hold PIR to its contractual schedule. Mr. Jablonski reported that test trains and limited service aren't scheduled to start until around March or April 2014.

Mr. Jablonski explained that from the SD&AE Board's standpoint as owners leasing to PIR, the focus is on the safety of operating the Desert Line, which includes bridge and track inspections, and that security is another issue. Ms. Landers added that PIR is required to have a plan with the Border Patrol and customs and has to meet all of the terms of the contract before operating. Ms. Landers added that if PIR is able to complete the milestones ahead of schedule, there should not be a problem. She clarified that MTS will receive the reports from the construction managers and the inspectors, and if necessary, will conduct additional inspections. Mr. Jablonski added that MTS will review the plans for deficiencies or otherwise accept them as satisfactory if there are no deficiencies.

Ms. Landers clarified for Mr. LaSalle that the miles-per-hour standard for train operations is set by the FRA. Mr. Jablonski added that Class 1 is set at 10 or 15 miles per hour. He stated that he feels that it is not the FRA's long-term intent to have the line operating at that speed. He stated that the Class 1 speed is a reasonable objective initially because the line hasn't been operated in a long time, and a lot has to happen on the Mexico side (to address tunnel damage across the border and other issues).

Mr. LaSalle inquired as to when the damaged tunnel will be repaired. He stated that representatives from ADMICARGA will not invest in repairing the tunnel until a start date is set for operations. Ms. Landers responded that PIR staff reported today that they are beginning work on the Desert Line on the U.S. side next week. Mr. Jablonski added that it will depend upon PIR's completion of milestones in the schedule.


Mr. LaSalle informed the Board that his organization would send a letter to memorialize its safety and security concerns.

9. Next Meeting Date

The next meeting of the SD&AE Railway Company Board of Directors is on October 15, 2013.

10. Adjournment

The meeting was adjourned at 9:37 a.m.



President

General Counsel

Attachments: Statement of Railway Finances (handout at meeting)
PIR's Periodic Report (2nd Quarter)

Handout at meeting

Agenda Item No. 2

San Diego and Arizona Eastern (SD&AE)
Railway Company
Board of Directors Meeting

July 16, 2013

SUBJECT:

STATEMENT OF RAILWAY FINANCES

RECOMMENDATION:

That the SD&AE Board of Directors receive a financial report for four quarters ended June 30, 2013.

Budget Impact

None.

DISCUSSION:

Attached are the unaudited financial results for four quarters of fiscal years 2013 and 2012, which includes the periods ended June 2013 and 2012. These statements are subject to adjustment for depreciation and other revenue or expense items that may occur during the annual financial audit to be completed before the end of December 2013.

The current year-to-date income is \$638,878 favorable to budget due to sale of property resulting in a \$642,214 unbudgeted gain on sale. Revenue for the SD&IV freight fee was not received during the year but has been accrued as a receivable as of June 30, 2013. SD&AE has received \$500,000 from Pacific Imperial Railroad in payment of the first installment under the Desert Line Lease and Operating Agreement dated December 20, 2012. Additional payments in accordance with the lease schedule will be due semiannually until limited operations begin after which payments will be due quarterly. The initial payment will be recognized as of July 1, 2013. Management, in consultation with the auditors, will analyze the lease terms to determine when the lease payments should be recognized; as a result, subsequent adjustment to the June 30, 2013, financial statements may be required.

Income has increased by \$684,129 compared to the same period last year due to the property sale cited above and a significant increase in Right of Entry permits. Finally, SD&AE received \$683 from the Secretary of State related to checks sent to us in 1995 that were never cashed.

Expenses are \$15,051 unfavorable to budget due to increased personnel costs and fees paid to PGH Wong for engineering services, both related to increased Right of Entry

permits activity; and \$4,733 paid to RL Banks for consulting services related to the Desert Line project.

Expenses have increased by \$28,255 over the same period last year due to a \$20,156 increase in personnel costs and a \$29,728 increase in Outside Services as stated above. Net income for FY13 was \$650,560 compared to a net loss of \$(5,313) for the same period in FY 12.

Attachment: SD&AE Operating Statement 4th Quarter FY 13

	FY 2013							FY 2012	
	Q1 2013	Q2 2013	Q3 2013	Q4 2013	YTD	Budget	Variance	Q1 - Q4	Variance
Right of entry permits	\$ 13,400	\$ 29,689	\$ (5,040)	\$ 17,850	\$ 55,899	\$ 50,000	5,899	9,121	46,778
Lease income	19,563	16,497	22,826	14,196	73,081	80,000	(6,919)	78,762	(5,681)
Other income	-	-	683	-	683	-	683	-	683
SD&IV 1% freight fee	-	-	-	32,000	32,000	35,000	(3,000)	31,866	134
Gain on sale of property	-	-	-	642,214	642,214	-	642,214	-	642,214
Total revenue	32,963	46,186	18,469	706,260	803,878	165,000	638,878	119,749	684,129
Personnel costs	25,179	30,410	21,379	27,196	104,164	91,966	(12,198)	84,008	(20,156)
Outside services	-	-	29,740	(13)	29,728	20,000	(9,728)	-	(29,728)
Energy costs	-	-	-	-	-	-	-	-	-
Risk management	5,752	5,752	3,637	3,751	18,892	22,300	3,409	23,543	4,651
Misc operating expenses	534	-	-	-	534	4,000	3,466	431	(103)
Depreciation	-	-	-	-	-	-	-	-	-
Total expense	31,465	36,162	54,757	30,934	153,317	138,266	(15,051)	107,982	(45,335)
Net income/(loss)	\$ 1,498	\$ 10,025	\$ (36,288)	\$ 675,326	\$ 650,560	\$ 26,734	623,826	\$ 11,767	638,794

Reserve balance 2012	\$ 916,413
Estimated interest earnings	1,651
Operating profit/(loss)	650,560
Improvement expense 2013	-
Reserve balance 2013-est	\$ 1,568,624



PERIODIC REPORT

June 30, 2013

The periodic report to the SD&AE Railway Company is produced quarterly by the Pacific Imperial Railroad for the SD&AE Board, in fulfillment of contractual requirements and to document activity in the restoration of the line to regional service along with its ongoing improvement for future generations.

Pacific Imperial Railroad

Second Quarter 2013

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- VI. MTS OPERATING AGREEMENT REQUIREMENTS**

I. GOVERNMENTAL

- a. No developments during this quarter.

II. DESERT LINE STATUS

a. Reconstruction Plan

- i. **Inspections** – PIR received a proposal to provide bridge inspection, Bridge Management Program, Track Inspection and Tunnel Inspection from J.L. Patterson & Associates, Inc. PIR accepted the proposal and is now working with J.L. Patterson to provide initial repairs to the Desert Line to enable operations of freight service.
 - ii. **Construction** PIR has executed an agreement with Watkins Environmental, Inc. wherein Watkins Environmental, Inc. shall perform the necessary repairs on the Desert Line, as determined by the J.L. Patterson inspection(s).
- b. **Financing Plan** – PIR is continuing its fundraising efforts through the CEO Ernie Dahlman and is considering agreements with other investment bankers.

III. REPORTABLE

INJURIES/ACCIDENTS/ENVIRONMENTAL INCIDENTS

- a. There have not been any reportable accidents.
- b. There have not been any reportable injuries.
- c. There have not been any reportable environmental incidents.

IV. MARKETING

- a. PIR finalized its Marketing Plan by utilizing information gathered in surveys generated from the numerous Maquiladora manufacturers. In May 2013, PIR implemented aspects of the marketing campaign outlined in the Marketing Plan.

V. FREIGHT ACTIVITY

- a. Currently PIR has not commenced revenue generation pending completion of the Inspections and Construction above.

VI. MTS OPERATING AGREEMENT REQUIREMENTS

- a. Pursuant to the Amended and Restated Desert Line Lease and Operating Agreement between PIR, San Diego and Arizona Eastern Railways Company and the San Diego Metropolitan Transit System, the following Performance Milestone Requirements fell within First Quarter:

- i. **Business Plan.** Submittal of Business Plan to SD&AE within 30 days from the effective date of the Agreement; and

- 1. PIR Timely submitted the Business Plan on January 19, 2013

- ii. **Reconstruction Plan.** Desert Line Reconstruction Plan submitted to MTS within 90 days of the effective date of the Agreement.

- 1. PIR Timely submitted the Reconstruction Plan on March 20, 2013.