

August 2, 2001

Via Hand Delivery

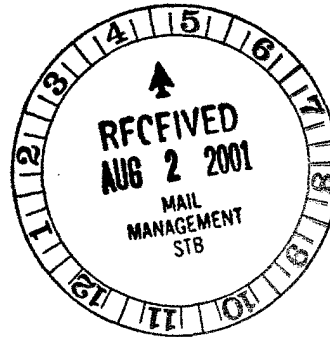
The Honorable Vernon A. Williams
Secretary
Surface Transportation Board
1925 K Street, N.W.
Washington, D.C. 20423-0001

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Office of the Secretary

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USS-4



RE: Finance Docket No. 34000; Canadian National Ry. Co., Grand Trunk Corp. and WC Merger Sub, Inc. - Control - Wisconsin Central Transp. Corp., Wisconsin Central Ltd., Fox Valley & Western Ltd., Sault Ste. Marie Bridge Co., and Wisconsin Chicago Link.

Dear Secretary Williams:

On behalf of United States Steel LLC ("U.S. Steel"), this letter is in response to the July 31, 2001 letter filed by Great Lakes Transportation LLC ("GLT"). As GLT clearly recognizes at the outset of its letter, the Board does not permit a reply to a reply; nor does the procedural schedule provide for the receipt of any comments after July 25, 2001. GLT's letter clearly does not correct "misunderstandings," but rather improperly argues GLT's position in reply to U.S. Steel's July 25 Reply Comments. The Board therefore should reject GLT's letter as inconsistent with the procedural schedule in this case. If the Board chooses to accept GLT's letter, U.S. Steel asks the Board also to accept this letter in response.

GLT asserts a variety of reasons why the Board should impose the Settlement Agreement as a condition, none of which Board precedent recognizes as legitimate. Every element of the Agreement, except antitrust immunity, can be accomplished through a private agreement that does not require a condition upon the CN/WC merger. In Finance Docket No. 30,000, *Union Pacific Corp. et al. - Control - Missouri Pacific Corp. et al.*, 366 I.C.C. 462, 601 (1982) ("UP/MP"), the ICC, after recognizing that it favors the private negotiation of settlements, further stated: "To the extent that the settlement terms involve only private contractual matters between the parties, however, we will not usually make those terms conditions of our approval of the transaction. See CSX, 363 I.C.C. at 581." The ICC then set forth its criteria for imposing settlement agreements as a condition:

Criteria. We will review and specifically approve or disapprove settlement terms (rather than simply allow them to become effective as contractual matters without action on our part) in two circumstances. First, we will act on settlement terms providing for actions or operations, such as trackage rights or pooling, requiring our approval under the statute. Second, we may act on settlement terms which affect the public's interest in a sound and efficient national transportation system, and will approve them if they are consistent with the public interest and the terms

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require immunity from the antitrust laws or other laws in order to be implemented effectively. Because our approval of settlement terms confers immunity from the operation of the antitrust laws, we will not indiscriminately approve any agreement reached by the parties.

Id. The ICC then refused to impose a settlement on the transaction at issue. In an earlier decision, the ICC also refused to impose an agency agreement as a condition because “[t]his is the type of agreement parties should negotiate and implement themselves.” Finance Docket No. 28905, *CSX Corp. – Control – Chessie System, Inc. et al.*, 363 I.C.C. 521, 581 (1980).

The Settlement Agreement does not satisfy the Board’s criteria for imposition as a condition. It does not encompass actions or operations that require the Board’s approval and GLT does not so allege. Although GLT contends that the Agreement is in the public interest and is not anti-competitive, it is wrong. GLT simply wishes to insulate the Agreement from antitrust attack. This is not a proper reason to impose the Agreement as a condition, since it would constitute the kind of indiscriminate approval that the ICC cautioned against in *UP/MP*.

Moreover, GLT ignores the fact that compliance with the Settlement Agreement is not necessary to remedy any anti-competitive harm caused by the CN/WC merger. The only harm alleged by GLT is to itself as a competitor. This is not a valid reason for imposing a condition unless the harm to GLT is harm to an essential service. 49 C.F.R. § 1180.1(c)(2)(ii). Yet, even in its most recent letter to the Board, GLT has not made such a claim in this proceeding, nor has it presented any evidence to support such a claim. Without such evidence, the Board cannot impose a condition to protect GLT because it provides an essential service.

GLT suggests, however, that, because it has refrained from submitting evidence it otherwise would have submitted, “failure to impose the Agreement as a condition would be unfair to GLT and would discourage future settlements.” GLT Letter, p. 4. This suggestion is absurd. GLT had every opportunity to submit evidence to support its request to impose the Agreement as a condition, or in the alternative to oppose the merger, in its June 25, 2001 submission to the Board. It had a second opportunity to do so in its July 25, 2001 submission, by which time it was abundantly clear that U.S. Steel and other parties would raise strong objections to the Agreement as anti-competitive. In its July 25th Comments, CN/WC took no chances and filed comments that address GLT’s claims despite having a Settlement Agreement with GLT. CN/WC also attempted to anticipate U.S. Steel’s comments based upon depositions conducted by U.S. Steel of CN and GLT officials. GLT, however, elected not to do either of these things. If GLT refrained from submitting certain evidence, it has only itself to blame.

GLT’s contention, on page 2, that its purpose in entering into the Settlement Agreement is not to extinguish all-rail options is irrelevant. The Agreement effectively allows GLT to favor its rail-

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water movement and handicaps all-rail competition, and that by itself is anti-competitive. Moreover, GLT's acknowledged purpose of precluding "below-cost" pricing by CN/WC is anti-competitive because the Agreement gives GLT discretion to decide if any all-rail movement that includes CN/WC's revenue factor in the rate is "commercially feasible." Furthermore, GLT is not in a position to determine if CN/WC is pricing below its costs, unless CN/WC also has agreed to provide GLT with its cost information in addition to its revenue requirements. That would make the Agreement even more anti-competitive than it already is. But, if CN/WC is not providing cost information to GLT, then the Agreement does not even enable GLT to accomplish its acknowledged objective to preclude below-cost pricing by CN/WC.

On page 3, GLT grossly misinterprets U.S. Steel's concern about the effect of the Settlement Agreement upon its existing Transportation Services Agreement ("TSA") with GLT. DMIR's bottleneck rate already is set under the TSA. That rate is adjusted up or down by changes in the rates that U.S. Steel is able to negotiate with other rail carriers on the route. Although the final rate is a joint rate, throughout the 13 year course of performance of this contract and its predecessor, U.S. Steel has negotiated directly with the Class I trunk line carriers. There has been no need for U.S. Steel to negotiate with DMIR at all because the DMIR rate factor automatically is determined by the TSA. But, the Settlement Agreement will preclude CN/WC from negotiating its rate directly with U.S. Steel. There is a significant difference between negotiating a rate directly with CN/WC and simply asking CN/WC to give its rate factor to DMIR so that DMIR can set the through rate, because the latter process eliminates the dialogue between the parties that can lead to more competitive rates. The TSA never contemplated that U.S. Steel would negotiate joint-line rates through DMIR and the DMIR could not accomplish this result absent the Settlement Agreement.

Although GLT states, at page 3 of its letter, that any shipper will be free to discuss rates directly with CN/WC and to encourage it to lower its revenue requirement, GLT glosses over the fact that, under the exclusive agency arrangement, CN/WC will not be able to negotiate directly with U.S. Steel, as it can today. Giles Dep. Tr. at 52-54; Radloff Dep. Tr. at. 66-67 (attached to USS-3). Furthermore, Section II.A.2. of the Settlement Agreement gives DMIR complete discretion to determine if an all-rail, joint-line movement is "commercially feasible," which means that the "aggregate revenue requirements . . . permit a through rate and a quality of service . . . that are competitive with comparable through rate and service offerings otherwise available to the shipper, including any offerings involving maritime transportation." DMIR also will have complete discretion to veto any effort by U.S. Steel to encourage CN/WC to lower its revenue requirement, subject only to the undefined requirement that DMIR act reasonably. It was never the intent of U.S. Steel to give DMIR such authority in the TSA, which under the Settlement Agreement will allow DMIR to discourage CN/WC from competing for U.S. Steel's taconite business.

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In addition, Section II.A.4. requires that CN/WC's revenue requirement must cause the movement to be profitable to CN/WC, but does not define "profitable." U.S. Steel often chooses which trunk line carrier to approach for an all-rail, joint-line rate by which carrier has a large inventory of unused cars. Those carriers tend to price most aggressively, *i.e.*, closer to their variable costs, in order to earn some contribution towards their fixed costs even if the rate does not cover total costs. This is more profitable to the carrier than allowing the rail cars to sit idle. But, the Settlement Agreement allows DMIR to determine what is and is not profitable.

GLT misses the point, on page 4, when it contends that the agency arrangement does not prevent shippers from challenging the reasonableness of "bottleneck" DMIR rates because three other rail carriers still may provide a contract for all-rail taconite movements. GLT's President, John Giles, asserted in his deposition that:

Clearly, CN is, you know, the -- as we speak, the most effective Class 1 in North America. The best operating ratio, the best debt-to-equity situation, the best cash flow. The best -- the most efficient. That's a remarkable difference than WC with its, you know, fairly modest resources pre-merger.

Giles Dep. Tr. at 73-74 (attached to USS-3). The Settlement Agreement therefore removes "the most effective Class 1 in North America," essentially the most effective and efficient competitor for all-rail taconite movements, from the competitive picture.¹

The only benefit to shippers from the exclusive agency arrangement in the Agreement that GLT is able to conjure up is the ability to offer "one-stop shopping." GLT Letter, p. 2. But, U.S. Steel, which ships to three of the five destinations covered by the Agreement, clearly does not view that as a benefit. Otherwise, it would not be objecting to the Settlement Agreement in this proceeding. GLT's insistence that this is a benefit, in combination with its desire to preclude below-cost pricing by CN/WC, is at best misguided and unwanted paternalism, and at worst a subterfuge to justify an anti-competitive condition.

Finally, GLT argues that "[f]ailure to impose the Agreement as a condition would sacrifice all of the benefits as to which no question has been raised." GLT Letter, p. 4. This is just another blatant example of GLT attempting to hold the beneficial portions of the Agreement hostage to a single anti-competitive provision. The Board should not set the precedent of allowing itself to be "railroaded" into immunizing an anticompetitive settlement provision from the antitrust laws just because that provision is tied to other provisions that could offer certain benefits.

¹ It is irrelevant that U.S. Steel could not seek bottleneck relief until 2008, since U.S. Steel still would be adversely affected by the Settlement Agreement for three years.

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In deciding whether to impose the Settlement Agreement as a condition of the CN/WC merger, the Board should be guided by its response to a similar request in the CN/IC merger. In that proceeding, the Board refused to impose the settlement agreement between CN/IC and the National Industrial Transportation League as a condition because DOT expressed concern that formal approval of the agreement "might unnecessarily immunize it . . . from the antitrust laws." Finance Docket No. 33556, *Canadian National Ry. Co. et al. – Control – Illinois Central Corp. et al.*, Decision No. 37, p. 32 (served May 25, 1999). In this proceeding, where the antitrust concerns are much greater, the Board similarly should decline to immunize the Settlement Agreement from the antitrust laws.

Respectfully submitted,



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cc: All Parties of Record