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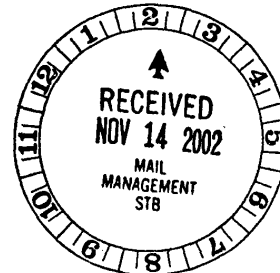
U.S. Department of
Transportation
Office of the Secretary
of Transportation

GENERAL COUNSEL

400 Seventh St., S.W.
Washington, D.C. 20590

November 14, 2002

Vernon A. Williams, Secretary
Surface Transportation Board
Suite 700
1925 K Street, N.W.
Washington, D.C. 20423-0001



Re: Finance Docket No. 34178

Dear Secretary Williams:

Enclosed herewith are the original and twenty-five copies of the Initial Comments of the United States Department of Transportation in the above-referenced proceeding. There is also a computer diskette of this document, convertible into Word Perfect. I have included as well an additional copy of the Department's comments that I request be date-stamped and returned with the messenger.

Respectfully submitted,

Paul Samuel Smith
Senior Trial Attorney

Enclosures

cc: Parties of Record

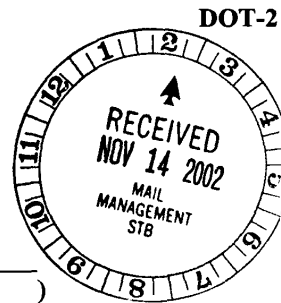
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206631

Before the
Surface Transportation Board
Washington, D.C. 20590



Dakota, Minnesota & Eastern Railroad Corporation and
Cedar American Holdings, Inc. -- Control -- Iowa, Chicago
& Eastern Railroad Corporation

Fin. Dkt. No. 34178

**Initial Comments of the
United States Department of Transportation**

Introduction

The Surface Transportation Board ("Board" or "STB") in this proceeding is considering the application of the Dakota, Minnesota & Eastern Railroad Corporation and related entities (collectively referred to herein as "DME") to acquire indirect control of the Iowa, Chicago & Eastern Railroad Corporation ("ICE") through a wholly-owned subsidiary of DME.¹ Related filings seek trackage rights, contingent upon approval of the primary application.

The United States Department of Transportation ("Department" or "DOT") notes that the record at this point contains only the application and related pleadings. In the absence of additional development of factual and legal issues, there is as yet no basis for DOT to take a position on the merits of the transaction. Consistent with past practice and

^{1/} DME and ICE are referred to collectively herein as "Applicants."

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with the schedule adopted for this proceeding,² in these circumstances we will reserve judgment pending a review of the initial comments of other parties, and we anticipate expressing our substantive views on reply.³ The Department offers its preliminary comments below.

The Applicants

DME is a Class II railroad that owns or operates approximately 1,100 route miles of rail lines in the states of Wyoming, South Dakota, Nebraska, Minnesota, and Iowa.⁴ The carrier interchanges traffic with three Class I railroads: the Union Pacific ("UP") (at points in Minnesota and Iowa), the Burlington Northern and Santa Fe ("BNSF") (in South Dakota and Nebraska), and the Canadian Pacific ("CP") (in Minnesota). DME interchanges traffic as well with several smaller railroads in the Upper Midwest. DME-2 at 21-22.

ICE is also a Class II railroad. It owns or operates approximately 1,400 route miles of rail lines in the states of Minnesota, Iowa, Kansas, Missouri, Wisconsin, and Illinois. ICE's lines extend to the major rail centers of Chicago, Kansas City, and Minneapolis/St. Paul. *Id.* at 19-21. ICE recently acquired these lines from I&M Rail Link, LLC ("I&M") in a transaction approved by the STB. Finance Docket No. 34177 (STB served June 12, 2002, June 26, 2002, and July 22, 2002) ("ICE/I&M Transaction"). ICE interchanges traffic with four Class I railroads: CP, BNSF, the Kansas City Southern

²/ Finance Docket No. 345178, Decision No. 2 (served September 26, 2002).

³/ Reply comments are now due December 13, 2002.

⁴/ Class I carriers are those with annual operating revenues of at least \$250 million (in 1991 dollars); Class II carriers are those with annual operating revenues between \$20 million and \$250 million; Class III carriers have annual operating revenues below \$20 million. 49 C.F.R. § 1201 General Instruction 1-1(a).

Railway Company, and the Norfolk Southern Railway Company. ICE interchanges traffic as well with numerous smaller carriers at points throughout the Midwest. DME-2 at 19-21. The lines of DME and ICE cross each other and connect in Owatonna, Minnesota, although the carriers cannot interchange there due to restrictions on DME trackage rights. *Id.* at 22. The Applicants' related filings seek trackage rights in order to allow them to interchange traffic. Finance Docket No. 34178 (Sub-Nos. 1, 2); *See* DOT-2 at 60-61 (Verified Statement of Kevin Schieffer at 5-6), and Exhibit 15 at 7-8.

Following approval of this transaction, the railroads themselves would remain separate entities. However, DME's subsidiary (Cedar American Holdings, Inc.) would exercise common control over both carriers and harmonize operations within the resulting coordinated system. *Id.* at 8-9.

Applicants' Public Interest Considerations

The Applicants contend that their transaction would advance the public interest in numerous ways. They urge that it would strengthen both carriers financially, enhance competition with Class I railroads and other modes of transportation, improve service to shippers on the lines of both carriers, extend single line service to new markets, and introduce greater operating efficiencies. The Applicants also maintain that approval would guarantee neutral eastern routings for coal movements from Wyoming upon construction of the newly-approved DME rail line into the Powder River Basin ("PRB"). *Id.* at 9-12.

The Applicants assert as well that their common control would have no adverse impact on competition. They present this transaction as entirely "end-to-end" in nature, with no shipper losing competitive rail service or access to routing options. The

Applicants report that they serve no common industries or even interchange traffic at any location. *Id.* at 95-99 (Verified Statement of Charles E. Lamberton at 16-20). Neither do they foresee any impact on passenger rail operations. *Id.* at 78. Finally, common control would reportedly not lead to changes in operations that would trigger the Board's regulatory thresholds for environmental review. *Id.* at 22-24. The Applicants include statements of support from shippers, railroads, and government entities. *Id.* at 111 *et seq.*

DOT's Preliminary Comments

The role of the Department in this proceeding is premised on the statutory and regulatory provisions and administrative orders that govern this transaction, as well as on DOT's statutory responsibilities as the Executive Department of the United States established by Congress "to provide general leadership in identifying and solving transportation problems,"⁵ to the end that the Secretary of Transportation "shall provide leadership in the development of transportation policies and programs."⁶

A. Safety

The Department's most fundamental concern in rail consolidation and other cases is safety. Transactions involving railroads of the size of the DME and ICE do not generally present significant safety questions, however, and at this point DOT is unaware of any reason to treat this case as an exception.⁷ We will, of course, carefully review the submissions of third parties and address any safety issues raised therein. Moreover, the

⁵/ 49 U.S.C. § 101(b)(5).

⁶/ 49 U.S.C. § 301(2).

⁷/ For example, federal regulations requiring the preparation of comprehensive Safety Integration Plans in merger cases do not apply to combinations of Class II carriers. 49 C.F.R. Parts 244, 1106.

Federal Railroad Administration ("FRA") will continue to exercise its broad authority over safety in the rail industry to monitor the Applicants' operations.

B. Environmental Issues

As the Board has acknowledged, DME is using a two-step process to acquire control of ICE. ICE/I&M Transaction.⁸ Throughout this process DOT's initial focus has been on environmental issues. The STB recognized that DME's construction of a rail line into the PRB would lead to large volumes of coal traffic on DME's lines, and after considering the impacts of such operations it required mitigation measures for the benefit of affected communities within the DME system. Finance Docket No. 33407, Decision served January 30, 2002. The Board declined to extend mitigation protections to similarly situated communities not on DME lines, in large part because it felt it could not require DME "to take action on property it does not own." Id. at 13, 20-27, Appendix A. The proposed acquisition of ICE would extend the property that DME "owns" and, as noted in our submission in Finance Docket No. 34177, "heretofore 'down-line' communities ... that were deemed ineligible for mitigation measures will now be 'on-line' and therefore should be considered for relief from demonstrable harms." DOT Comments filed June 12, 2002, at 4.

The Board in that proceeding decided that since the PRB line was not in existence and since there were no established plans for routing coal traffic, it was premature to reach any conclusions regarding environmental protections. ICE/I&M Transaction, Decision served July 22, 2002 at 15-16. The STB acknowledged, however, the necessity

⁸/ The first step, already completed, was the acquisition of I&M by ICE, a subsidiary of Cedar American Rail Holdings, Inc. The second is the instant transaction.

for considering the cumulative impacts of its related regulatory decisions, and barred ICE “from handling any trains moving to or from the [approved PRB line] over what are now [I&M] lines until we have conducted an appropriate environmental review.” *Id.* at 17. That condition was reiterated in this proceeding. Decision No. 2, *supra*, at 8 note 11.

The Department agrees with the Board’s approach. The present uncertainty of construction and the multitude of steps that still have to take place before coal may be transported within even an expanded DME system make it premature to impose specific obligations. The STB’s preservation of the *status quo* both avoids potentially unnecessary or unfounded regulatory determinations and demonstrates the proper willingness to consider mitigation measures when and where that appears appropriate.

C. Other Issues

DOT is also interested in other potential issues that parties may raise in this proceeding. One such is likely to concern the options by which a combined DME/ICE system might interchange traffic, including the relative merits of a grant of trackage rights over UP versus construction of a new rail line extension. Another is the precise means through which the Applicants will gain access to Chicago.

The Department submits that, pursuant to applicable statutory provisions,⁹ the following issues also warrant consideration in this proceeding:

- Whether the transaction is likely to substantially lessen competition, create a monopoly, or restrain trade in freight surface transportation in any region of the country.

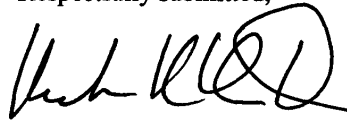
⁹/ 49 U.S.C. § 11324(d).

- Whether the transaction's anticompetitive effects outweigh the public interest in meeting significant transportation needs.

Conclusion

The Department appreciates this opportunity to participate in a proceeding of regional significance to railroads, shippers, and the general public. We look forward to development of the record and to contributing to a sound final decision.

Respectfully submitted,

A handwritten signature in black ink, appearing to read "Kirk K. Van Tine", written in a cursive style.

KIRK K. VAN TINE
General Counsel

November 14, 2002

CERTIFICATE OF SERVICE

I hereby certify that I have on this day caused to be served on all Parties of Record by first-class mail, postage prepaid, a copy of the foregoing Initial Comments of the United States Department of Transportation filed in Finance Docket No. 34178.

A handwritten signature in cursive script, reading "Paul Samuel Smith", written over a horizontal line.

Paul Samuel Smith

November 14, 2002