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**U.S. Department of
Transportation**

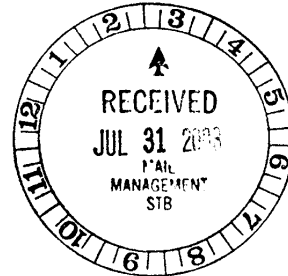
Office of the Secretary
of Transportation

GENERAL COUNSEL

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

July 31, 2003

Office of the Secretary
Case Control Unit
Financial Docket No. 34342
Surface Transportation Board
1925 K Street, N.W.
Washington, D.C. 20423-0001



Attention: Phyllis Johnson-Ball
Environmental Project Manager
Environmental Filing

Dear Ms. Johnson-Ball:

Enclosed please find an original and twenty-five copies of the "Comments of the United States Department of Transportation on the Environmental Appendix and Safety Integration Plan" in Finance Docket No. 34342. Also enclosed is a diskette containing a version of our comments saved in WordPerfect.

We have also enclosed a service copy of our comments, and would appreciate it if you would time-stamp that copy and return it to the courier delivering our comments.

Sincerely,

Dale C. Andrews
Deputy Assistant General Counsel
for Litigation

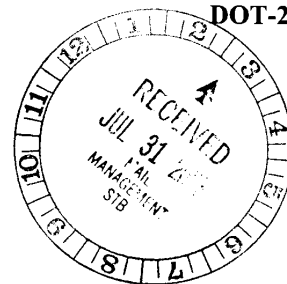
cc: All parties of record

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Public Record**

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



_____)
Kansas City Southern -- Control -- The Kansas City)
Southern Railway Company, Gateway Eastern)
Railway Company, and The Texas Mexican)
Railway Company)
_____)

Finance Docket No. 34342

**Comments of the United States Department of Transportation
On the Environmental Appendix and Safety Integration Plan**

Introduction

The Surface Transportation Board ("Board" or "STB") in this proceeding is considering whether to approve the combination of the Texas Mexican Railway Company ("Tex Mex") and the Kansas City Southern Railway Company ("KCS").¹ The STB is assessing as well the implications for the United States of a separate but related transaction, the addition of a large Mexican carrier, TFM, S.A. de C.V. ("TFM"), to the above two railroads to form NAFTA Rail. Decision No. 2, served June 9, 2003.

Pursuant to the Board's order, the Applicants submitted an Environmental Appendix ("Appendix") and a Safety Integration Plan ("SIP"). KCS-13/TM-13. *Id.* Their Supplement to Application ("Supplement"), intended to address the TFM transaction, also briefly discusses environmental and safety issues. KCS-10/TM-10.

The United States Department of Transportation ("DOT" or "Department")

¹ KCS and Tex Mex are collectively referred to herein as "Applicants."

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hereby submits its comments on the Appendix and the SIP, with one caveat. The Canadian National Railway Company ("CN") has petitioned the Board to reject the application in this case on the basis that the Applicants have not properly set forth in the record the full implications of the TFM transaction. CN-3. CN contends that the Supplement does not offer the requisite "full system competitive analyses and operating plans," that the Applicants used a "static model" in their analyses (which erroneously assumes no change in traffic growth), and that the proffered analysis of source competition is faulty. *Id.* Most pertinent for present purposes, CN also avers that the shortcomings of the Supplement prevent the Board from examining the "cumulative impacts" of this related transaction under the National Environmental Policy Act ("NEPA"). *Id.* at 11-12.²

DOT takes no position on the merits of this dispute at this time. We *do* believe that CN and UP have raised a potentially serious question for the Board to resolve after consideration of all relevant pleadings. Since these comments must be filed beforehand, however, the Department's comments are necessarily based only upon the information submitted by the Applicants in the record to date on environmental and safety matters. DOT will, of course, consider and submit comments upon the relevant effects of any additional data that the STB may require.

Environmental Impacts

The Applicants have asserted consistently in this proceeding that the KCS-Tex Mex transaction and the KCS-TFM transaction (to the extent the latter is before the STB)

^{2/} The Union Pacific Railroad Company ("UP") supports CN generally, but raises no environmental or safety issues. UP-4.

are not subject to NEPA review because they pose such minimal environmental impacts that they qualify for a "categorical exclusion." KCS-13/TM-13 at 9-13, and Exhibit B; KCS-10/TM-10 at 31. The Board agreed that the information contained in the original application was "sufficient to create a presumption" that a categorical exclusion applied, but directed the Applicants to produce an environmental appendix "providing additional details and explanation" in support of their contention. Decision No. 2 at 16.

The Applicants estimate that both the KCS-Tex Mex transaction and the KCS-TFM transaction would together divert only 6,313 carloads annually -- some 17 or 18 cars per day -- to the combined KCS-Tex Mex system. KCS-3/TM-3 at 43; KCS-13/TM-13, Exhibit B at 2; KCS-10/TM-10 at 31, and Verified Statement of Gerald K. Davies at 16-17. Such small amounts of additional traffic, they report, would be accommodated on existing trains. KCS-13/TM-13, Exhibit B at 2. The Applicants also point out that this traffic would not affect operations in their rail yards, that they have no plans to abandon track or facilities, and that historic preservation requirements do not apply. *Id.* at 2-3.

To the extent these are the only changes brought about in the U.S. by both transactions, the Department largely agrees with the Applicants' assessment. Based on the existing record, it is likely that the transactions do not warrant specific action to ameliorate adverse impacts.³

The only potential exception of which DOT is aware concerns the slightly longer trains anticipated by the Applicants. These could ordinarily be expected to have relatively minor impacts, but here they could exacerbate existing circumstances in the

^{3/} Again, we will review any additional information required of the Applicants or submitted by other parties and offer comments, if appropriate, in subsequent submissions.

City of Laredo, Texas. Laredo has already experienced significant traffic delays and congestion as a result of growing cross-border traffic. If longer trains suffer the same kinds of delays in Laredo, it is possible that they will block either more highway-grade crossings or the same crossings for longer periods of time. We urge the Applicants to work with the City of Laredo to minimize any such potential consequences of their transactions.

Safety Integration Plan

The Federal Railroad Administration ("FRA") has worked to assist the Applicants in the development of their Safety Integration Plan within a fairly compressed time frame. On June 3, 2003, KCS proffered a draft SIP to FRA; on June 20 FRA provided extensive comments; eleven days later the SIP was filed with the Board. KCS-13/TM-13, Exhibit D; *see also* KCS-10/TM-10 at 31-32.

Transactions like these present issues that require careful attention to ensure the safe integration of railroads. In particular, FRA notes that successful integration requires a detailed action plan, with dates for completion of all action items, the commitment of specific resources, and the identification of accountable persons and offices.⁴ The SIP submitted by the Applicants is responsive to a number of the comments raised by FRA, but others remain unaddressed.

For example, the Applicants responded to FRA's request for a table identifying planned safety action item(s), implementation timetable, resource allocation, and personnel accountability. KCS-13/TM-13, Exhibit D. However, the financial and other resources to be

^{4/} For example, the SIPs in the following rail consolidation proceedings all contained such action plans: Finance Docket Nos. 33388 (CSX/Norfolk Southern/Conrail) 33556 (Canadian National/Illinois Central); and 34000 (Canadian National/Wisconsin Central). [IS THIS TRUE??]

committed for several important components (such as "Computer Based Training" and "Remote Control Technology") are labeled "TBD" -- presumably, To Be Determined -- and thus utterly unknowable. Id. Moreover, although the SIP notes that various Tex Mex capital projects are dependent upon financing, the implementation table indicates that the source of funding is in the form of a \$50 million loan from FRA, and neither of the Applicants has yet submitted a formal application. Id. The prospects and timing of any such financing are thus speculative at best.

Another critical issue in rail consolidations generally is the integration of different information systems. KCS recently adopted what it calls a Management Control System ("MCS") that, as the application candidly explains, ushered in "a period of service disruption" when first adopted. KCS-3/TM-3, VS of Michael R. Haverty at 67 note 7. KCS believes its MCS is now functioning as intended, but expanding it to other carriers requires very careful planning and execution. Yet the resources to be devoted to this pivotal task are again listed in the SIP implementation table as "TBD." KCS-13/TM-13, Appendix D.

FRA is also not yet satisfied that the Applicants have addressed all of the safety implications of the TFM transaction. FRA informed the Applicants that their original draft SIP did not reflect sufficiently detailed attention to issues raised by the expanded coordination with TFM generally, and in particular with those arising from common control of the International Rail Bridge at Laredo. That is still the case.

Finally, FRA has had general, non-merger-related concerns about various safety issues with respect to the KCS system. Regulatory concerns regarding track conditions and mechanical equipment defects have resulted in increased monitoring of KCS. Our

concerns make it all the more important that the final SIP be as thorough as possible, to help ensure a safe and successful consolidation.

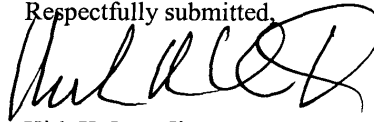
The Department wishes to be entirely clear on the matter of safety in this proceeding. The Applicants have cooperated with FRA to date, and we fully anticipate that this will continue through both the preparation of an appropriately detailed final SIP and (if approval is granted) a successful and safe integration of the different rail systems comprising NAFTA Rail. But the SIP at this point is in need of significant further development.

Conclusion

A potentially significant issue is still pending concerning the completeness and accuracy of the materials submitted thus far by the Applicants, especially as regards the implications of the TFM transaction. Because that issue will not be resolved before the instant comments are due, DOT's views are necessarily based only upon the information now contained in the record regarding the likely changes in the U.S. brought about by these transactions. Additional information may lead us to amend our comments.

Based on the record as it now stands, the Department believes that the projected changes present very manageable environmental issues. We urge the Applicants to work with the City of Laredo to avoid adverse impacts there. The remaining safety issues are also certainly manageable, but much serious development of the SIP is still necessary. FRA will continue to refine the SIP and will cooperate with the Applicants in its safe implementation.

Respectfully submitted,

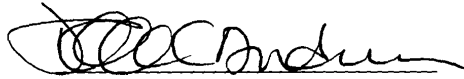
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Kirk K. Van Tine
GENERAL COUNSEL

July 31, 2003

Certificate of Service

I certify that on this date copies of the foregoing document were served on all parties of record in this docket by first class mail, postage prepaid.

A handwritten signature in black ink, appearing to read "Dale C. Andrews", written over a horizontal line.

Dale C. Andrews
Deputy Assistant General Counsel
for Litigation
United States Department of Transportation

July 31, 2003