

BEFORE THE
SURFACE TRANSPORTATION BOARD

STB FINANCE DOCKET NO. 35081

CANADIAN PACIFIC RAILWAY CO., *et al.* – CONTROL –
DAKOTA, MINNESOTA & EASTERN RAILROAD CORP., *et al.*

COMMENTS OF THE
U.S. DEPARTMENT OF AGRICULTURE

Bruce I. Knight
Under Secretary
Marketing and Regulatory Programs
U.S. Department of Agriculture
Washington, D.C. 20250

Date: March 4, 2008

AUTHORITY AND INTEREST

The Secretary of Agriculture is charged with the responsibility under the Agricultural Adjustment Act of 1938 and the Agricultural Marketing Act of 1946 to represent the interests of agricultural producers and shippers in improving transportation services and facilities by, among other things, initiating and participating in Surface Transportation Board (Board) proceedings involving rates, charges, tariffs, practices, and services.

On December 5, 2007, Canadian Pacific Railway Company (CP) and Dakota, Minnesota & Eastern Railroad Corporation (DM&E) filed an amended control and merger application, which the Board accepted for consideration as a significant transaction.

Since 1986, the DM&E has been a particularly important rail line to agricultural shippers. DM&E preserved railroad competition, improved grain producer access to other markets, increased its traffic base, improved the level of rail service, and upgraded the condition of its track. With the purchase of the Iowa, Chicago & Eastern Railroad (IC&E) in 1997, the DM&E system became the largest regional railroad in the United States and the only regional railroad having interchanges to all seven U.S. major railroads. The system operates 2,500 route miles, serving 8 states (IL, IA, MN, MO, NE, SD, WI, and WY), and has obtained Board approval to construct an additional 262 miles of new rail line into the Powder River Basin (PRB). The importance of the DM&E system to agricultural shippers is demonstrated by the quantities of agricultural products that the DM&E system hauled during 2006:

- Nearly 100,000 carloads of grain
- 13,000 carloads of forest products
- 33,000 carloads of food products
- 7,800 carloads of fertilizer

In addition, the total annual ethanol production capacity on the DM&E system could expand to 1 billion gallons, which would require the presence of a railroad capable of providing reliable rail service. The DM&E serves 6 existing ethanol plants and will serve 5 additional plants that are currently under construction. Another 7 ethanol plants have announced plans to build on the DM&E system. DM&E also serves 3 flour mills and 6 soybean processing plants.

The CP rail system offers a competing route to the Pacific Northwest in addition to rail access to the Canadian cities of Calgary, Montreal, Toronto, and Vancouver and U.S. cities of Detroit, New York, Philadelphia, the Twin Cities, and Duluth/Superior. CP handles approximately 25 percent of the grain rail movements in North Dakota, providing rail-to-rail competition to BNSF which is the only other major railroad serving the state. During 2007, CP originated more than 240,000 railcars of grain in both the United States and Canada, which is 14 percent of total U.S and Canadian Class I railroad grain originations. CP operates more than 13,260 route miles, including 3,267 miles in the United States.

Continued improvements in rail service and capacity on the DM&E system will be critical in serving the future needs of agricultural shippers. The CP purchase of the DM&E system is expected to provide access to additional markets, more efficient single line service for some shipments, and the financial resources needed to improve DM&E lines and build the proposed PRB line.

POTENTIAL BENEFITS OF THE PROPOSED MERGER

The presence of DM&E has preserved railroad competition in those regions it serves, resulting in agricultural shippers benefitting from lower rail rates. Furthermore, DM&E has improved grain producer access to markets through its connections with all the major U.S. rail lines. These important connections with other rail carriers and the improved condition of DM&E rail lines have allowed agricultural shippers located on DM&E to competitively access Pacific Northwest (PNW), Texas, and eastern U.S. markets.

USDA believes the CP purchase of the DM&E system could benefit agricultural shippers by:

- Preserving 2-railroad competition in South Dakota and northern Iowa which would preserve competitive rail rates.
- Providing savings for energy consumers by reducing the transportation costs for coal.
- Allowing construction of a second rail route into the PRB which would provide more efficient and direct movements to some power plants serving rural communities.
- Decreasing the risk associated with having only one route serving the PRB if weather, catastrophic, maintenance, or terrorist events were to result in interrupted electricity production and service.
- Resulting in a safer railroad through improvement of the tracks, signaling, and communications systems.
- Creating more efficient and safer rail transportation for increased ethanol and bio-fuels production.
- Reducing the cost of inputs used by farmers through the movement of anhydrous ammonia and other agricultural chemicals by rail.
- Providing higher paying railroad, ethanol production, and manufacturing jobs for the region.

THE LINE INTO THE POWDER RIVER BASIN

Due to the larger financial resources of CP, the proposed merger is expected to result in the construction of a new rail line into the PRB. Since November 1998, the USDA has strongly supported the proposed DM&E construction of 262-miles of new rail line into the PRB and the reconstruction of 600 miles of existing rail lines in South Dakota and Minnesota. In addition, many of the farm organizations representing agricultural producers in the geographic area of the merger strongly support the DM&E expansion. This strong support is echoed by other organizations and interests such as South Dakota economic development groups, shippers, electric generating companies, and 55 of the 56 affected cities.

The construction of the new rail line into the PRB would benefit the economy of the region by providing a more efficient and direct route to the electrical generating plants serving the region and creating new and higher paying jobs. The additional volume on the DM&E system is expected to improve rail service to agricultural shippers because the rail lines would need to be upgraded to allow higher speeds than current volumes of traffic could justify. In addition, the Nation would benefit from additional energy security and capacity that an alternative rail route from the PRB would provide.

USDA recognizes, however, that the Board would need to approve movements of coal originating on the new PRB line before that coal could be moved on the U.S. lines of CP and IC&E. Before giving this approval, the Board is required to conduct an appropriate review of the environmental impacts associated with such routings.

KEEP CONNECTIONS TO OTHER RAILROADS OPEN AT COMPETITIVE RATES

Agricultural shippers on the DM&E system currently have cost-competitive access to connecting railroads in Chicago and to connecting railroads that serve PNW and Texas destinations. The CP acquisition of DM&E also provides agricultural shippers with an additional routing option to the PNW.

Cost-competitive access to markets is extremely important to agricultural producers as the price they receive is net of transportation costs. In addition, access to several markets results in several buyers competing for the same product, allowing agricultural producers to receive the best possible price.

Cost-competitive and non-discriminatory access would be particularly important on movements to Chicago and existing routes to connecting carriers serving destinations in the higher density routes to the PNW and Texas. Cost-competitive access is also important at many other connections even though they are lower density than those to the PNW and Texas. Some existing rail rates on the DM&E system to connecting carriers that serve other geographic markets currently tend to foreclose the movement of substantial volumes of agricultural products to those markets due to arbitrarily high rates. One of these markets is Cedar Rapids, Iowa, which would require economically competitive rail rates to the interchange with Iowa Northern Railway at Nora Springs, Iowa. At shippers' request, IC&E reduced the non-competitive rate rates to the Nora Springs interchange through the end of May.

USDA recognizes that a Class I railroad may not be able to provide competitive rates to every interchange, but encourages CP to maintain economically competitive rates to those

connections whenever it is able to cover the costs associated with the lines serving those connections.

USDA requests that the Board condition this acquisition with the requirement to maintain cost-competitive and non-discriminatory connections to other railroads. The basis for this request is the importance of preserving rail-to-rail competition. Further, this condition is consistent with the language of the application, which states, “At the local level, Applicants will seek to smooth volumes and traffic flows by increasing the availability of unloading and loading, and *maintaining an open gate policy*.” (Application CPR-2 DME-2, Volume I, Exhibit 13, page 31, emphasis added).

STRIVE TO MAINTAIN OR IMPROVE RAIL SERVICE

In 1986, DM&E acquired a rail line on which maintenance had been deferred for many years and freight volume had declined. At one point, nearly all of the line was restricted to speeds of 10 miles per hour or less—consequently, it took 9 days to haul goods from one end of the line to the other. Some observers expected that DM&E would eventually be forced to abandon these lines after extracting any remaining value. Instead, DM&E was able to gradually improve the condition of the line and train speeds, increase freight volumes, improve agricultural shippers’ access to markets, and improve service to shippers located on the line. A great deal of the success of short line and regional railroads has been due to their willingness to search for solutions to shipper transportation requirements.

Some shippers have expressed that with the proposed merger, the level of service and reliability could decrease because they are concerned that major railroads have less of a customer

service orientation than smaller railroads. Although many agricultural shippers support the merger in expectation of improved rail service, some shippers on the IC&E recall when CP operated the line and service was less than adequate. These shippers have indicated to USDA that they are concerned that service may be reduced when CP operates these lines again. Furthermore, when CP operated these lines in the past, these shippers claim its market share of grain transportation decreased.

USDA encourages CP to strive to maintain or improve service levels to shippers on the DM&E system. USDA recognizes the service reputation of CP has improved since CP last operated the IC&E lines and we are hopeful that improved service to shippers will continue to be a high priority under the proposed merger.

PROVIDE AN ADEQUATE SUPPLY OF GRAIN CARS

Some IC&E shippers also are concerned about adequate grain car supply. These shippers have stated that CP did not provide an adequate supply of grain cars when it operated the current IC&E lines.

Thus, USDA requests that the Board encourage CP to maintain the number of grain cars available to agricultural shippers on the DM&E system at the levels provided during 2007 and that CP not favor Canadian shippers over those from the U.S.

INVESTMENT IN BRANCH LINES

In addition, some IC&E shippers who had formerly been served by CP also have indicated to USDA that CP failed to adequately invest in branch lines to maintain or improve their condition. USDA notes that the IC&E line between Mason City and Sheldon, IA, is worn 90-lb jointed rail. In addition the line between Ramsey and Jackson, MN, is in poor condition. Loss or abandonment of these lines could result in a Union Pacific (UP) rail monopoly in that region because these lines provide the only rail competition. Thus, USDA believes that it is important that these lines be preserved through adequate investment.

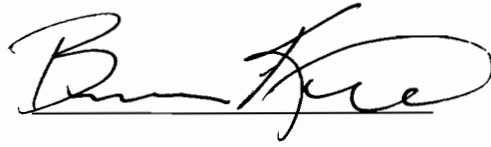
For this reason, USDA encourages CP to make sufficient investment in current branch lines to maintain or improve their current condition. This is particularly important for those branch lines for which abandonment would result in only one railroad serving a region.

CONCLUSION

The DM&E system is particularly important to agricultural shippers. With the purchase of the Iowa, Chicago & Eastern Railroad (IC&E) in 1997, the DM&E system became the largest regional railroad in the United States and the only regional railroad having interchanges to all seven U.S. major railroads.

Continued improvements in rail service and capacity on the DM&E system will be critical in serving the future needs of agricultural shippers. Thus, USDA supports this merger on the condition that CP keeps all current connections to other railroads open (including those in Chicago and to the Pacific Northwest and Texas) at economically competitive and non-discriminatory rates.

Respectfully submitted,

A handwritten signature in black ink, appearing to read "Bruce Knight", written over a horizontal line.

Bruce I. Knight
Under Secretary
Marketing and Regulatory Programs
U.S. Department of Agriculture
Washington, D.C. 20250

CERTIFICATE OF SERVICE

I, Bruce Blanton, certify that on this 28th day of February, 2008, I caused a copy of the foregoing document to be served by first-class mail, postage prepaid, on all parties of record in STB FD No. 35081.

A handwritten signature in black ink, appearing to read "B. Blanton", is written over a horizontal line.

Bruce Blanton
Director
Transportation Services Division
U.S. Department of Agriculture
Washington, D.C. 20250