

**BEFORE THE
SURFACE TRANSPORTATION BOARD**

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Finance Docket No. 36514

**CANADIAN NATIONAL RAILWAY COMPANY, GRAND TRUNK CORPORATION,
AND CN'S RAIL OPERATING SUBSIDIARIES**

—CONTROL—

**KANSAS CITY SOUTHERN THE KANSAS CITY SOUTHERN RAILWAY COMPANY,
GATEWAY EASTERN RAILWAY COMPANY, AND THE TEXAS MEXICAN
RAILWAY COMPANY**

**COMMENTS OF THE NATIONAL INDUSTRIAL TRANSPORTATION LEAGUE
ON THE JOINT MOTION FOR APPROVAL OF VOTING TRUST AGREEMENT**

The National Industrial Transportation League (“NITL” or “League”) hereby submits its comments in opposition to the Joint Motion for Approval of Voting Trust Agreement resubmitted on May 26, 2021 by the Canadian National Railway Company, Grand Trunk Corporation, and CN’s railroad subsidiaries (“CN”) and Kansas City Southern and its operating railroads (“KCS”) (collectively “Applicants”) in connection with CN’s proposed acquisition of control of KCS.¹ NITL members are generally opposed to additional rail mergers due to

¹ On May 17, 2021, the STB denied CN’s motion to approve its proposed Voting Trust Agreement as incomplete and without prejudice to resubmit its request for approval. See *Canadian National Railway Company et al.- CONTROL – Kansas City Southern Railway*

significant concerns that rail-to-rail competition may be further reduced and service may be adversely impacted. NITL opposes the Applicants' request for approval of the voting trust because the risks of competitive harm that may occur if the merger is not approved and CN must divest KCS outweigh the Applicants' alleged voting trust benefits.

In order for the voting trust to satisfy the public interest, the benefits must outweigh the potential harm.² To satisfy this test, NITL believes that the Board must define with greater clarity the meaning of "enhanced competition" and "improved service", which the Applicants must establish will be achieved from their proposed merger.³ As explained below, NITL has developed principles for each of these critical merger review standards and has engaged in preliminary discussions with CN and KCS, as well as the Canadian Pacific Railway ("CP") who also seeks to acquire KCS. However, due to the short timetable for comments on the voting trust NITL and the Applicants, as well as CP, were not able to progress their discussions toward a mutual agreement. Thus, NITL requests the Board to extend the procedural schedule on the voting trust by an additional 10 days for both comments and the Applicants' reply.

NITL's current position on the voting trust should not be construed as opposition to the acquisition of KCS by CN (or any other railroad suitor), since NITL has not yet determined its formal position on the merger itself.

I. The Voting Trust Must Be Consistent with the Public Interest.

Under 49 C.F.R. 1180.4(b)(4)(iv), the Applicants "must explain how the [voting] trust would insulate them from an unlawful control violation and why their proposed use of the trust,

Company et al., STB Docket No. FD 36514, slip op. at 3 (STB served May 17, 2021) ("STB Voting Trust Decision").

² *Major Rail Consolidation Procs.*, 5 S.T.B. 539, 568 (2001).

³ 49 C.F.R. §1180.1(c).

in the context of their impending control application, would be consistent with the public interest.” In its May 17 decision, the STB clarified the standard of review applicable to voting trust agreements under the applicable merger review standards. The STB remarked that when the agency promulgated its review standards for “major” rail mergers in 2001, the intent was not to codify prior actions on voting trusts but rather the Board was adopting a “much more cautious approach to future voting trusts in order to preserve our ability to carry out our statutory responsibilities.”⁴ Citing to its decision in Major Rail Consolidation Procedures, the Board recited that:

to gain approval for the use of a voting trust, applicants would have to demonstrate either that any harm to the public interest associated with the divestiture process would be relatively small or that some countervailing public benefit would be associated with their proposed use of a voting trust that would outweigh this risk.” Major Rail Consolidation Procs., 5 S.T.B. at 568. The Board noted that “while voting trusts can serve some public purpose, they should not be used routinely, but rather should be available only for those rare occasions when their use would be beneficial,” id. at 568 n.29, that “use of a voting trust is a privilege, not a right, and that [prospective applicants] may not employ a voting trust until we have authorized its use,” id. at 568. As such, **the Board expects to take a more cautious approach to a voting trust here, and its consideration of whether the proposed use of a voting trust in a potential CN-KCS transaction is “consistent with the public interest” would be informed by argument on both the potential benefits and costs of such use.**⁵

Thus, the current merger review standards for major transactions impose a higher standard on voting trust approvals than existed in prior mergers. In order for the Board to approve the voting trust agreement requested by the Applicants, it must find that the harm from the potential divestiture of KCS that would occur if the merger is not approved is outweighed by the voting trust benefits.

⁴ Major Rail Consolidation Procs., 5 S.T.B. at 567.

⁵ STB Voting Trust Decision at 7 (emphasis added).

II. The Competitive Risks Associated with the Voting Trust Outweigh the Potential Benefits.

The U.S. Department of Justice (“DOJ”) has expressed serious concerns regarding the Applicants’ voting trust, despite the lack of “actual control” by CN of KCS during the merger review period and pendency of the trust. Because the voting trust would allow CN and KCS to consummate the merger subject to regulatory approval (but not integrate during the review period), DOJ believes that the “unity in ownership” will reduce the Applicants’ incentives to aggressively compete as they did prior to such ownership. Specifically, DOJ commented that “CN managers would have diminished incentives to compete aggressively against KCS in areas served by both railroads because winning business away from KCS would now hurt CN’s shareholders, and vice versa.”⁶ DOJ explained that increased competitive concerns exist with the Applicants proposed transaction since both railroads currently operate competing routes between New Orleans and Baton Rouge, LA.⁷ It noted further that, even where parallel lines do not serve the same O-D pairs, they may be used to compete with build-outs from a shipper served by one railroad to the network of the other, such as on north-south routes through much of Mississippi.⁸

NITL shares DOJ’s concerns, as well as its goal that this transaction must be carefully evaluated to “protect[] and promot[e] competition in the railroad industry.”⁹ NITL also has concerns based on the premium CN has offered to KCS, which may also create incentives to

⁶ Comment of the United States Department of Justice at 2, STB Docket No. FD 36514 (May 14, 2021).

⁷ *Id.*

⁸ *Id.*

⁹ *Id.* at 1.

reduce rail competition and maximize differential pricing wherever possible. Moreover, if divestiture of KCS was to be required if the merger was not approved ultimately, CN would maintain substantial control over this process and may divest KCS in a manner that reduces rail competition that exists today, as well as the current strength and value of the KCS network, by selling portions of the system to different railroads and/or private equity suitors.

The Board has expressed its own concerns regarding the potential financial risks posed to CN if divestiture of KCS was required. In its May 17 decision, the Board stated that “while CN contends that there is ‘no cause for concern’ as to whether a sale out of divestiture would ‘harm CN’s financial integrity,’ the level of debt being utilized by CN to fund the proposed merger, as well as the substantial premium CN has offered for KCS, call this assumption into question.”¹⁰

Further, NITL does not believe that the CN claimed voting trust benefits outweigh the potential harms. CN claims that the voting trust is needed to place CN on equal footing with other potential railroad and private equity suitors. However, CN’s argument relates to the more rigorous and lengthy regulatory review process that it must endure as compared to private equity suitors or other railroad suitors who would have greater flexibility to consummate the merger sooner and at less cost. This is because such transactions would not qualify as “major” under the Board’s rules or may otherwise have been determined to qualify under the less stringent pre-2001 rules. CN also argues that a voting trust is required to provide greater certainty to KCS shareholders. Thus, the voting trust structure plainly has significant advantages and benefits to *CN and KCS* but this does not necessarily equate to benefits that are consistent with the *public interest*, especially when balanced against the potential competitive and financial risks.

¹⁰ *Canadian National Railway Company et al.- CONTROL – Kansas City Southern Railway Company et al.*, STB Docket No. FD 36514, slip op. at 6 (STB served May 17, 2021).

Although CN has claimed that the merger is mostly end-to-end and would produce significant merger benefits, NITL is not able to fully validate the impacts of the merger at this preliminary stage of the review process. The Applicants' merger application has not yet been filed and many more details concerning the merger scope and impacts need to be explained and scrutinized. As noted, the CN transaction unquestionably will reduce competition in the Gulf region. The manner and details by which CN proposes to address this and other losses of competition are unclear. Thus, even if the Board were to approve the merger, it is highly likely, that approval would be subject to protective conditions. This only creates further uncertainties, since it is plausible that the protective conditions could upset the anticipated merger benefits.

III. The Public Interest Requires the Board to Clarify the Meaning of Enhanced Competition and Improved Service, Prior to Approval of the Voting Trust.

In order for the benefits of the voting trust to exceed the potential competitive harms, the public interest requires greater clarity on the meaning of at least two key review standards included in the Board's 2001 merger rules, namely, "enhanced competition" and "improved service."¹¹ Because this is the first merger transaction that is subject to these standards, there is no precedent to help guide the Applicants, the rail industry, or their customers as they evaluate the merger and the voting trust. Given the enormous impact that these standards have on whether this transaction is consistent with the public interest, and what conditions may be necessary to satisfy these standards, the League does not believe that the Board should rely upon the Applicants' broad and general statements of merger benefits as sufficient to outweigh the risks of competitive harm inherent in the voting trust.

Rather, NITL strongly believes that clarifying the meaning of "enhanced competition" and "improved service" now as part of the evaluation of the voting trust could prevent such

¹¹ 49 C.F.R. §1180.1(c).

competitive harm and reduce the risk of a future KCS divestiture if the merger is not approved by the Board (or conditions imposed by the Board make the merger undesirable). This is because the Applicants would have a better understanding of the scope of potential protective conditions that could be imposed by the Board and, assuming that rail customers supported the interpretation of those concepts, the risk of shipper opposition to the CN/KCS transaction would be greatly diminished.

A. NITL Proposal on Enhanced Competition and Service Protections.

Accordingly, a NITL working group has developed a proposal containing principles and concepts defining enhanced competition and service improvements in connection with its position on the voting trust. The principles address some of the Applicants' statements regarding enhanced competition and an intent to maintain open gateways. However, the NITL believes that the new merger review standards require more than preservation of the pre-merger status quo. Rather enhancing competition should require competitive *improvements*. Thus, the NITL principles seek to protect gateways beyond those directly affected by the merger. They also seek to address gateway pricing, which is key to protecting gateways both physically and commercially. In this regard, NITL intends to work with the Applicants or another railroad merger suitor on the development of a rule 11 tariff rate structure. NITL members favor rule 11 rates based on a mileage scale that would vary for different commodities and/or car types and would be subject to an escalation index. NITL's proposal contemplates that shippers and the post-merger combined railroad could incorporate these rates into contracts or negotiate alternative contract rates potentially using the rule 11 rates as a benchmark. The rule 11 gateway rates could be used by a shipper to combine with a connecting carrier's rule 11 rate; but the post-merger combined railroad could still offer a competing joint line rate. The NITL's proposed rule

11 pricing would be an option regardless of the pre- or post-merger long-haul rights of the merged railroad.

Additionally, because rail service is also a critical factor related to any rail merger, the NITL proposal includes service protections. The protections concern switching schedules, switching performance and metrics, interchange and terminal dwell, and preserving service types (manifest, unit train, etc.), with an expedited dispute resolution process.

B. NITL Discussions.

NITL has shared its enhanced competition and service proposals with both CN and KCS, as well as CP, and has engaged in preliminary discussions about the principles.¹² However, due to the expedited schedule for comments on the voting trust, the parties need more time to engage in more meaningful discussions in order to reach potential agreements. Based on the feedback it has received from the Applicants, NITL believes that meaningful progress could occur if more time was available for further discussions.

However, based on the expedited filing periods on the voting trust and its concerns noted above, NITL currently opposes the voting trust. NITL believes that the risks to competition inherent in the voting trust, i.e. the disincentive for CN to compete aggressively with KCS or the incentive to potentially impact KCS' connections with other railroads, and the uncertainties if the merger ultimately was not approved and KCS were to be divested, outweigh the voting trust benefits touted by CN. However, NITL intends to continue discussions with the Applicants and if an agreement is able to be reached in the near term that causes NITL to believe that the voting trust would be consistent with the public interest, based on the Applicants' commitments to

¹² NITL is also beginning to discuss its proposal with other industry groups.

enhanced competition and service post-merger, then NITL would inform the Board at the earliest possible time.

Respectfully submitted,

/s/ Karyn Booth

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CERTIFICATE OF SERVICE

I hereby certify that I have caused the foregoing Comments of the National Industrial Transportation League on the Joint Motion for Approval of Voting Trust Agreement to be served electronically or by first class mail, postage pre- paid, on all parties of record in this proceeding.

/s/ Karyn Booth

Karyn Booth

June 28, 2021