BEFORE THE
SURFACE TRANSPORTATION BOARD

Canadian National Railway Company et al. --CONTROL-- Kansas City Southern Railway Company, et al.	Finance Docket No. 36514

COMMENT OF THE UNITED STATES DEPARTMENT OF JUSTICE

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The United States Department of Justice ("Department") appreciates this opportunity to again share its views with the Surface Transportation Board ("Board"). The Department commends the Board for its intention to carefully scrutinize the proposed merger of Canadian National Railway Company ("CN") and Kansas City Southern ("KCS"), just as it intended to do with a proposed merger of Canadian Pacific Railway Company ("CP") and KCS. The Department is committed to collaborating with the Board in the evaluation of this proposed transaction to pursue our shared goal of protecting and promoting competition in the railroad industry. As with a potential CP-KCS merger, the Department has an interest because of the Attorney General's statutory right to intervene in Class I merger proceedings. *See* 49 U.S.C. § 11325(b)(1).

I. The Board Should Not Permit CN to Utilize a Voting Trust

At this time, the Department is only beginning to evaluate the potential competitive concerns raised by a proposed acquisition of KCS, and for this reason, the Department does not yet take a final position on the merits of a proposed acquisition of KCS by CN. However, this proposed acquisition raises sufficient competition concerns on first blush that the CN should be prohibited from using a voting trust.

On May 6, 2021, the Board approved the proposed CP-KCS voting trust in Finance Docket No. 36500. Notwithstanding this decision, the Board should not permit the proposed CN voting trust because CN's proposed acquisition of KCS appears to pose greater risks to competition than the risks posed by a CP-KCS merger. Thus, even though the terms of CN's proposed voting trust are similar to the terms of CP's proposed voting trust, the Board has good reason to hold CN's proposed voting trust to a higher bar. The Department continues to respectfully disagree with the Board's precedents on the use of voting trusts for the reasons explained in the Department's April 12, 2021 comment (attached as Exhibit A) and urges the Board to reconsider whether its longstanding practice on voting trusts is consistent with sound

competition policy. Nevertheless, even under the Board's own existing precedents, the Board can recognize the distinctions between the proposed CN-KCS and CP-KCS mergers and reach a different conclusion about the appropriateness of a voting trust.

The Department's concerns regarding the use of a voting trust in the proposed CP transaction apply with greater force to CN's proposed acquisition of KCS because it raises additional potential competitive concerns. As the Department explained in its prior submission, even two railroads that are "end to end"—i.e., that do not compete to offer parallel single-line service between the same origin and destination pairs—may still compete with one another in important ways. *See* Exhibit A at 8-10. CN insists that these competitive concerns are irrelevant to the analysis of the voting trust because the trust is structured so as to prevent the acquiring firm from exercising any control during the pendency of the Board's review. This argument misses the point: the unity in ownership will diminish the parties' incentives to continue to engage in such competition *even if* the trust successfully prevents the acquiring firm from exercising any actual control.

Even though the Board was not persuaded that these incentive concerns should preclude the use of a trust in a CP-KCS merger, a CN-KCS transaction poses additional dangers to competition stemming from the potential elimination of direct, "parallel" competition on routes served by both railroads, for example between Baton Rouge and New Orleans. In addition, even parallel lines that do not presently serve the same origin-destination pairs may be used to compete to attract "build outs" from a shipper served by one railroad to the network of the other, for example on north-south routes through much of Mississippi. These threats to competition would be present immediately after the CN voting trust is consummated. 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. These specific competitive concerns presented by CN's proposed transaction magnify the general risks associated with voting trusts described in the Department's prior filing.

Given the larger number of competitive concerns presented by CN's proposed acquisition, the Department respectfully submits that CN's use of a voting trust would be even more problematic than the use of a voting trust by CP. Also allowing CN to utilize a voting trust would thus appear inconsistent with the Board's view that trusts should "not be used routinely," and only be available on "rare occasions when their use would be beneficial."[1] In order to preserve the Board's ability to protect competition and to thoroughly review the issues presented by a CN acquisition, the Board should not permit CN to enter into a voting trust.

II. The Department's Reply to CN

In its April 26, 2021 filing, CN responded to the Department's April 12, 2021 filing by raising two primary arguments. First, CN argues that a voting trust structure is necessary to put CN on a level playing field with financial buyers that do not hold railroad assets, and thus would not be subject to the Board's review. Second, CN argues that a voting trust is necessary given the length of the Board's review process. Neither of these arguments is persuasive.

[1] *Major Rail Consolidation Procedures*, 2001 WL 648944, at *19 n.29 (STB June 7, 2001).

A. Prohibiting the Use of a Voting Trust Does Not Unfairly Advantage Non-Railroad Buyers

CN contends that the Department's position on voting trusts would inappropriately favor private equity buyers, but in fact it is CN's position that would inappropriately favor buyers that threaten competition. In any industry, a bid by a non-competitor generally will offer greater certainty of deal clearance because a bid by a competitor raises the potential for competitive harm and thus warrants more stringent regulatory review. This is an inherent feature of any competition review, not a unique attribute of the Board's process for railroad mergers. CN's flawed reasoning assumes that private equity would always be the favored buyer in all transactions, in any industry, because a private equity buyer would always face a shorter, less burdensome review, whether reviewed by the Department, the Board, the Federal Trade Commission, the Federal Communications Commission, the Federal Reserve, the Federal Energy Regulatory Commission, or any another federal, state, or foreign authority.

This clearly is not the case. As in any situation where a seller has received acquisition offers from both private equity and strategic buyers, it is up to KCS as the seller to weigh the potential benefit of shorter, less burdensome antitrust or regulatory review against potential benefits that CN, CP, or any other competing Class I railroad may provide, such as a higher purchase price based on projected synergies or expected higher margins from the elimination of a competitor. Strategic buyers, including Class I railroads, can also make their offer more attractive by offering deal terms that confer greater certainty, such as a "hell or high water" clause or a reverse breakup fee. Similarly, to the extent CN has concerns about exclusivity, that is a common provision that CN is free to negotiate with KCS.

But a strategic buyer should not be permitted to structure the deal in a manner that could give rise to anticompetitive effects simply because the alternative would be more expensive. At its core, CN's argument boils down to a desire to use a voting trust to avoid paying more to negotiate alternative terms, such as interim operating covenants, material adverse effects clauses or a breakup fee, or to lose the money that it has already sunk if the deal falls apart. Like any other buyer that competes with its target, CN voluntarily assumed the risks associated with the regulatory review of the proposed transaction. CN should not be permitted to use a deal structure that may cause anticompetitive effects simply because it may save CN money.

B. Railroad Buyers Have Viable Alternatives to a Voting Trust

CN contends that the alternative deal terms identified by the Department are impractical due to the length of the Board's review process, but CN greatly exaggerates the differences between the Board's review and the reviews faced by companies in other industries. It is true that reviews of benign mergers under the Hart-Scott-Rodino Antitrust Improvements Act of 1976 ("HSR Act") can be much quicker than a Board review of a rail merger. But that certainly does not mean all HSR investigations proceed faster than the Board's reviews. In the vast majority of transactions notified pursuant to the HSR Act, the antitrust agencies can determine very quickly that there are no competitive concerns presented, and those transactions are cleared within thirty days. But where the merging parties have overlapping businesses in a concentrated industry or where the merging parties may deny suppliers a key customer or customers a key supplier, the transaction is routinely subject to a Second Request, and thus, a longer review timeline to assess

potential competition issues.[2] Many merging parties in a multitude of industries assert, as CN has, that their transactions will not harm competition and will benefit customers. Whether the facts bear out those assertions requires investigation and verification. In the Department's experience, a transaction as significant as a merger of Class I railroads could take a year or more even if it were subject to review solely under the HSR Act.

Many merging parties must also contend with review processes lasting more than one year because of simultaneous regulatory review by other federal agencies or antitrust review by enforcers outside the United States. In just the past several years, many high-profile transactions subject to overlapping reviews took 18 months to two years to close.[3] Far from railroads being unique, they face the same obstacles as do many other merging parties in many other industries. Whether the review timeline is longer because of substantive competition issues or because of overlapping reviews, businesses in other industries routinely rely on interim operating covenants and material adverse effect provisions as well as breakup fees to protect their interests.

These commonly-used terms provide alternatives that raise fewer competitive risks than a voting trust, but still provide protection during a lengthy review period and allow the parties to plan for a successful post-closing integration. Because they do not unify the ownership of the two firms, these deal terms better protect both firms' incentives to compete vigorously and to continue their ordinary course of business conduct. It is particularly important to protect these incentives to compete where, as here, CN and KCS appear to compete head to head on multiple parallel routes.

* * *

The Department remains committed to offering any assistance it can provide as the Board carries out its important mission protecting competition in this industry. The Department appreciates this opportunity to share its views, and looks forward to continuing to work cooperatively with the Board on this proposed transaction and on other matters.

Respectfully Submitted,

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[2] *See, e.g.*, Ardagh-St. Gobain (announced on January 17, 2013; FTC final order entered on June 18, 2014); Aetna-Humana (announced on July 3, 2015; abandoned on February 14, 2017); Tronox-Cristal (announced on February 21, 2017; closed on April 10, 2019).

[3] *See, e.g.*, Exelon-Pepco (announced on April 30, 2014; closed on March 23, 2016); Dow-DuPont (announced December 11, 2015; closed on August 31, 2017); Bayer-Monsanto (announced on September 16, 2016; closed on June 7, 2018); AT&T-Time Warner (announced on October 22, 2016; closed on June 15, 2018); Siemens-Alston Rail JV (announced on September 27, 2017; European Commission prohibition decision on February 6, 2019); T-Mobile-Sprint (announced on April 29, 2018; closed on April 1, 2020).

CERTIFICATE OF SERVICE

I certify that on May 14, 2021, I caused a copy of the forgoing Comment of the United States Department of Justice to be served via email on the parties of record in this docket.

/s/ Seth Wiener

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