Submission
to the
Canada Transportation Act Review
Covering Rail Freight Transportation

January 29, 2015

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Appendicies

1.0 Introduction

The Freight Management Association of Canada (FMA) appreciates the opportunity to submit its comments and recommendations to the *Canada Transportation Act* Review. While the Review was not required under the law to start until 2015, the transportation issues faced by many sectors of the Canadian economy, particularly by the grain sector, are of concern and the economy will be well-served by advancing the start of the Review.

FMA has been representing the freight transportation interests of Canadian industry since 1916. Our 90+ members include companies, both large and small, from most industrial sectors and from all across the country. The FMA member companies contribute approximately $100 billion annually to the Canadian economy and purchase approximately $6 billion in freight services by truck, rail, marine, courier and airfreight. A list of the member companies can be found on the Association's website at http://www.cita-acti.ca/membership/member-companies .

The Minister's Mandate of June 25, 2014 stresses the recent rail service problems faced by the grain industry with regard to deliveries from the record 2013-2014 crop year. The Mandate states:
"Given the urgency created by the recent backlog in grain deliveries from the 2013-2014 crop-year, grain transportation will be given priority consideration. The Review will consider the provisions of the Act that are relevant to the transportation of grain by rail, some of which could apply more broadly to the rail-based supply chain for all commodities…."

Given this stress on the railway mode, this FMA submission will focus on rail and FMA may provide further comments on other transportation modes at a later date.

1.1 Overview of the Submission

This paper discusses policy, the legislative and regulatory regime that has evolved over the past century, including the deregulation of the rail industry that started in 1967. It then covers recent legislative and regulatory initiatives to re-balance the shipper-railway relationship and follows with eleven recommendations designed to improve the effectiveness of the railway system for shippers and to support the current and future needs of the Canadian economy

2.0 Background – National Transportation Policy

Section 5 of the Act provides the Policy Statement underpinning all of the provisions of *Canada Transportation Act.* Section 5 states, in part:

5. *It is declared that a competitive, economic and efficient national transportation system that meets the highest practicable safety and security standards and contributes to a sustainable environment and makes the best use of all modes of transportation at the lowest total cost is essential to serve the needs of its users, advance the well-being of Canadians and enable*

competitiveness and economic growth in both urban and rural areas throughout Canada. Those objectives are most likely to be achieved when

> *(*a*) competition and market forces, both within and among the various modes of transportation, are the prime agents in providing viable and effective transportation services;*
>
> *(*b*) regulation and strategic public intervention are used to achieve economic, safety, security, environmental or social outcomes that cannot be achieved satisfactorily by competition and market forces and do not unduly favour, or reduce the inherent advantages of, any particular mode of transportation;*

The emphasis in section 5.(a) on *"competition and market forces"* to meet the objectives is appropriate and is working well in all modes except rail.

For example, even though the *Shipping Conferences Exemption Act (SCEA)* permits shipping lines to enter into legal cartels, (shipping conferences), SCEA allows confidential contracts and there are enough shipping lines serving Canadian ports that there is effective competition in ocean freight services.

The situation with rail freight is unique.

3.0 The Railway Problem

There are approximately 50 railways in Canada, but the rail freight industry is dominated by the two Class 1 carriers, Canadian National Railways (CN) and the Canadian Pacific Railway Company (CP). These two companies account for approximately 90% of the Canadian rail freight revenues.

The fundamental problem is that there is not effective competition within the rail mode and the barriers to new entrants are so high that this situation will not be rectified through market forces. Where the fundamental problem cannot be rectified, the best that can be done is to provide a legal and regulatory regime that is a surrogate for real competition and that re-balances the bargaining power of the buyers and sellers in the rail freight market.

While there is limited competition between CN and CP in a few markets (primarily intermodal), for many shippers, the rail market can be best characterized as being a "dual monopoly", rather than even a "duopoly". That is, each of CN and CP is the only railway available to shippers at many locations. It should be noted that this is not just a western Canadian problem, but exists in the east as well.

Rail Freight is not a normally functioning competitive market and this fact has been acknowledged in Canadian Railway Law for over 100 years. The following excerpts from Canadian law, regulations and regulatory decisions, confirm that point as follows.

3.1 *Railway Clauses Consolidation Act, 1851* – Pre-Confederation[1]

This Act states:

[1] Canadian Transportation Agency Case No. 14-02100

The trains shall….furnish sufficient accommodation for the transportation of all such passengers and goods as shall within a reasonable time previous thereto be offered for transportation…and the party aggrieved by any neglect of refusal in the premises, shall have an action against the Company.

3.2 The Railway Act, 1906 [2]

The level of service provisions of the 1906 Act are almost identical to the comparable provisions in the current Act, including the authority of the Board of Railway Commissioners (a predecessor to the Canadian Transportation Agency) to intervene by ordering the railway to take specific action to rectify the problems.

3.3 Decision of the Supreme Court of Canada, Docket 35145 (May 23, 2014)

This case was triggered by an FMA petition to the Governor-in-Council (the Cabinet of the Canadian Government). In its decision, the Supreme Court stated (in section 23):

In certain circumstances, the railway companies were seen to have superior market power to shippers. This superior market power of the railway companies, combined with the complaints of shippers over railway service and rates, led to Parliament's efforts to respond to these concerns (Standing Committee on Transport, Infrastructure and Communities, November 22, 2007, at p. 1). As the Honourable Lawrence Cannon, Minister of Transport, Infrastructure and Communities explained: "I believe the time has come to rebalance the legislative framework in favour of shippers"

3.4 The Competition Bureau

While the railways are not subject to Sections 78 and 79 of the *Competition Act,* these provisions are instructive in terms of the Competition Bureau's approach to the market dominance by a small number of sellers within a specific market.

The Bureau's general approach in evaluating allegations of abuse of dominance is as follows:

- *A market share of less than 35 percent will generally not give rise to concerns of market power.*
- *A market share of 35 percent or more will generally prompt further examination.*
- *In the case of a group of firms alleged to be jointly dominant, a combined market share equal to or exceeding 65 percent will generally prompt further examination*.

In the case of the rail freight market, CN and CPR together control approximately 91% of the market by revenue.

Based on 2010 annual reports of CN, CPR, and the Railway Association of Canada (RAC), total rail freight revenues in Canada were $10.224 billion, CN's Canadian freight

[2] Canadian Transportation Agency Case No. 14-02100

revenues were $5.630 billion and CPR's Canadian freight revenues were $3.635 billion. CN alone accounts for 55% of the market based on revenues and CPR for 36%.

3.5 Canadian Transportation Agency Decision, Case No. 14-02100

In this decision, rendered October 3, 2014, the Agency, in ordering CN to comply with its service obligations pursuant to the terms of the Confidential contract with Louis Dreyfus Commodities Canada Ltd., stated in section 28:
The retention of these provisions (level of service) in federal legislation reflects Parliament's acknowledgement that regulatory intervention in railways level of service matters continues to be necessary.

CN has been granted leave to appeal this decision to the Federal Court of Appeal.

3.6 The Implications for the Review

The evidence over the past 150 years, as noted above supports the need for need for continuing legislative and regulatory constraint on railways to compensate for market dominance of the carriers. The legal and regulatory burden on the railways has been significantly reduced over the past fifty years, and they have gained pricing freedom over that time, leading to much improved net revenues. As stated by the Honourable Lawrence Cannon, Minister of Transport, in 2007, *"I believe the time has come to rebalance the legislative framework in favour of shippers".*

4.0 Recent Investigations and Reviews

Since the passage of Bill C-8 in 2008, following from the last Statutory Review, there has been significant investigation by the government in response to the chronic complaints of shippers, primarily about service. The following sections discuss these recent initiatives and the resulting legislative and regulatory actions.

4.1 Statutory Review of 2000-2001 and Bill C-8, 2008

The report of the last Review was submitted in June 2001, and amendments to the Act, following from the Review were finally passed in 2008.

The Report, entitled *Vision and Balance* was comprehensive and made observations and recommendations covering transportation broadly, but it is instructive to note that of 312 pages in the report, rail freight chapters took 67 pages, airline industry 17 pages, marine transport, 14 pages, and trucking 8 pages.

On page 56 of *Vision and Balance,* the Panel states:
In the Panel's view, Canada's rail freight transportation system works well for most users, most of the time". That is a subjective comment that was questionable in 2001, and was even more questionable later in the decade, when the government convened the Rail Service Review in 2009 as part of its response to *Vision and Balance* when it passed amendments to the Act in 2008. The Rail Service Review was established to address the wide-spread complaints about rail service from the shipper community.

However on page 87 of *Vision and Balance*, the 2001 Review Panel acknowledged as follows.
The Panel believes, however, that there are cases where market forces are inadequate; in these situations, appropriate recourse is necessary to protect shippers against potential abuse of market dominance by the carrier.

The legislation, responding to the Statutory Review of 2001 was Bill C-8, *An Act to Amend the Canada Transportation Act (railway transportation),* which received Royal Assent on February 28, 2008.

The significant changes in Bill C-8 affecting shippers are as follows:

- Sections 27 (2), (3), and (5) were repealed. These provisions required a shipper to prove "substantial commercial harm" before such shipper could access several of the "shipper protection" provisions of the Act, e.g. competitive line rates, and extension of interswitching limits. There was no definition of "substantial commercial harm" in the Act. Removal of this provision eliminated a hurdle for shippers.
- Section 119 was amended to require that railways give at least 30 days-notice when proposing to increase "a rate in a tariff for the movement of traffic".
- A new section 120.1 was added that, for the first time proved a vehicle for shippers to file complaints to the Agency on service, penalty, and incidental charges, and associated terms and conditions, imposed by a railway, where such charges "are found in a tariff that applies to more than one shipper". It should be noted that the first such complaint, brought by FMA member, Peace River Coal, against CN, had to be fought all the way to the Supreme Court of Canada to confirm that a shipper who has a confidential contract has access to this provision.
- A new section 169.2(1) was added that allowed groups of shippers, "dissatisfied with the rate or rates charged…or with any conditions associated with the movement of goods," could submit the matter jointly to the Agency for final offer arbitration. The matter submitted must be common to all shippers so applying. It is understood that this provision has never been used as the "commonality" barrier is too high.

The items in the first three bullets above have been of value to shippers, the fourth bullet has not.

4.2 The Rail Freight Service Review and Bills C-52 and C-30

The Rail Service Review (RSR) Panel was appointed by the Minister of State (Transport) in September 2009. This was part of the government's commitment to the shipper community made with Bill C-8. The RSR Panel was appointed in response to wide-spread and growing complaints about unreliable rail service, primarily in terms of car supply and consistent transit times.

The Panel issued its final report in January, 2011 and the government made the report public on March 18, 2011 along with its commitment to take action in response to the report.

As with all previous and subsequent findings of independent investigators, Parliament, and the courts, the RSR Panel found that rail freight is not a normally functioning competitive market and stated on page 41 of their final report as follows.
"…the Panel concludes that railways continue to have market power over some of their customers and that there are sectors and regions where competitive alternatives are lacking altogether. This railway market power results in an imbalance in the commercial relationship between the railways and other stakeholders.

The Panel made eight recommendations, some of which found their way into Bill C-52.

4.2.1 Bill C-52, the *Fair Rail Freight Service Act*

Bill C-52, the *Fair Rail Freight Service Act,* received Royal Assent on June 26, 2013. The primary purpose of Bill C-52 was to give shippers the right to a Service Level Agreement (SLA) through arbitration if one could not be obtained by direct negotiation with the railway.

What C-52 does for shippers:

1. It gives all shippers the right to obtain a service agreement on Canadian traffic, covering the service elements described in Section 113 of the *Canada Transportation Act.* The first step is for shippers to attempt to do so by direct negotiation.
2. Should the negotiation fail, the shipper can ask the Agency for arbitration to obtain an SLA. The Agency then appoints an arbitrator to decide the matter.
3. Where the railway does not meet its commitments under an arbitrated agreement, it can be subject to fines of up to $100,000 for each violation.

What C-52 does not do for shippers:

1. It does not mandate dispute resolution within a service agreement obtained either through direct negotiation or arbitration, although the section 116 complaint process is available. The shipper can, in its proposal to the arbitrator, specify the dispute resolution mechanism to apply.
2. It does not include shipper-carrier communications notifying shippers on service changes or disruptions as a matter to be included in a negotiated service agreement, but it does specify that communication protocols can be included in the list of matters to be addressed in a service agreement achieved by arbitration.
3. It does not provide for penalty provisions in a negotiated service agreement
4. It covers only the Canadian portion of cross-border moves.
5. It allows the railways to apply to the Agency for an order declaring a matter may not be included in a shipper's submission for arbitration.

While sections 113-116 of the *Act* (level of service provisions) provide recourse for shippers after a service failure, the import of Bill C-52 is to provide a framework designed to prevent or minimize failures from happening.

4.2.2 Bill C-30, the *Fair Rail for Grain Farmers Act*

Bill C-30, the *Fair Rail for Grain Farmers Act* received Royal Assent on May 29, 2014. It followed from an *Order-in-Council* issued by the Cabinet on March of 2014 directing each of CN and CPR to move at least 500,000 tonnes of grain per week to export positions.

While the focus of Bill C-30 was on grain transportation, it contained several provisions of value to all shippers, and added new provisions to improve access to SLAs, following from Bill C-52.

Section 5.1 of C-30, amending Subsection 116(4) of the *CT Act* addresses one of the shortcomings of Bill C-52, i.e. the need to compensate shippers for "expenses" incurred because the railway is in violation of its service obligations under SLA or a confidential contract. The definition of "expenses" in the Agency regulations will be an issue in determining the effectiveness of this provision.

Section 7 of C-30 provides authority for the Agency to extend interswitching limits "*for the regions or goods that it specifies".* This amendment to the interswitching regulations will allow the Agency to give effect to the government's policy announcement to extend the maximum interswitching limit on the Prairie Provinces from 30 km to 160 km for all shippers. The interswitching regulations have been useful to shippers over many decades and provide competitive access in the absence of effective competition. Regulated interswitching is an effective surrogate for real competition.

The other significant provision of C-30 relevant to all shippers is Section 8, which authorizes "*The Agency to make regulations specifying what constitutes operational terms"* to be included in a SLA achieved through arbitration.

The Agency has now published its regulations pursuant to Bill C-30 as follows.

a) Interswitching Regulations- including rates for extension from 30 km to 160 km on the three Prairie Provinces.
b) Regulations on Operational Terms for Rail Level of Service Arbitration.
c) Rules of Procedure for Rail Level of Service Arbitration.

It should be noted that the provisions of Bill C-30 will automatically terminate on August 1, 2016, unless the government extends any of them before that date.

With Bills C-52 and C-30, and their regulations now in place, the Agency has begun to receive requests from shippers to obtain SLAs through arbitration, and several of them have now been achieved through that process.

4.3 The Implications of Recent Actions

Some of the recent actions mentioned above, have been helpful to shippers, and to the

functioning of the Canadian economy. However, recent experience with service issues in the winter of 2013-2014 with car supply, with the growth of ancillary and penalty charges, and with communications problems surrounding arbitrary service changes, continue to highlight the need for further action on the functioning of the rail industry and its implications for railway customers and the broader Canadian economy.

5.0 Analysis of Current Shipper Protection Provisions

The Members of the Freight Management Association of Canada have considered the recent actions as described above in light of their current experiences with rail service. While some sectors, e.g. retail importers moving containers by rail, are somewhat satisfied with their relations with their rail carriers, many industry groups have continuing problems in their relationship with their rail carriers.

A fundamental fact is that there is no way to increase real competition within the railway industry. With the vertical integration (i.e. the owners of the infrastructure are also the operators of the service), the entry of new competitors is virtually impossible.

This means that National Transportation Policy, Section 5(b) of the Act must be the overriding policy provision for addressing the relationship between shippers and rail carriers. Subsection 5(b) states as follows:

"(b) regulation and strategic public intervention are used to achieve economic, safety, security, environmental or social outcomes that cannot be achieved satisfactorily by competition and market forces…"

5.1 What Works and What Doesn't in the *Canada Transportation Act*

While some of the "Shipper Protection" provisions of the Act work for some shippers some of the time, most of the provisions are difficult and expensive for small and medium sized shippers. The costs, uncertainty of the outcome, and the threat of retaliation from the railway are significant barriers for many shippers. With this caveat, the following three lists are an indication of what works, what does not work, and where there has not been sufficient experience with respect to the recently added provisions for which to evaluate their usefulness.

5.1.1 What Works

- Sections 113 – 116: the *Level of Service* or Common carrier provisions. These provide a mechanism for shippers to file complaints on service failures and possibly obtain relief from the Agency for such failures.

- Sections 161-169: Final Offer Arbitration (FOA). This provision provides a method for binding arbitration of freight rates and associated conditions where direct negotiations are at an impasse.

- Section 128: Regulated Inter-switching. This provision is an effective competitive access provision where it applies. It allows a shipper to obtain competing rates from an origin served by one federally regulated railway, if the interchange with the second

railway is within 30 km of the origin point, (with limited expansion to 160 km as discussed above).

5.1.2 What Does Not Work

- Section 129 -136: Competitive Line Rates (CLR). CLR's are a surrogate for real competition by permitting shippers to obtain competing rates from an origin served by one federally regulated railway, if the interchange with the second railway is more than 30 km from the origin point. Before the Agency will mandate a "regulated" rate from origin to the interchange point with the second railway, the shipper must obtain a rate from the connecting railway through direct negotiation. Where either CN and CPR is the "connecting railway", they refuse to quote rates from the interchange point for CLR purposes. The Rail Freight Service Review Panel concluded in its report that CN and CPR had rendered this remedy inoperative.

- Section 169.2: Group FOA. This provision, added in 2008 was designed to allow a group of shippers to jointly request a resolution of rate disputes where their situations are very similar. The determination of what constitutes a "group" with virtually identical conditions is so high that it is an effective barrier to its use.

5.1.3 To Early to Tell

- Section 120.1: Complaints on Ancillary and Penalty Charges, provides a mechanism for shippers to challenge the arbitrary and growing list of ancillary and penalty charges imposed by the railways in tariffs that apply to more than one shipper. In the first case, brought by FMA member, Peace River Coal, a dispute arose with CN as to whether or not this provision could be used by a shipper if the tariff was referenced in a confidential contract. FMA had to fight this to the Supreme Court of Canada to clarify that reference in a confidential contract is not a barrier to the use of this provision. There is an additional hurdle with this remedy. Subsection 120.1(7) states that the remedy does not apply to "a rate for a movement of traffic". This means that the Agency must determine, in each case, whether the charge that is the subject of the complaint, falls within the meaning of that subsection.

- Section 169.31-169.43 Arbitration on Level of Services.
  This provision was added in 2013, following from the Rail Service Review. Its purpose is to provide a mechanism for the service level details to be defined in a written agreement between the railway and the shipper and, if such SLA cannot be directly negotiated, to obtain such an agreement through arbitration. In an arbitrated SLA, where the railway is in violation of its service commitments, it is subject to fines imposed by the Agency.

- Section 116(4) (c.1): Strengthening the SLA provisions by providing for compensation to shippers for direct expenses incurred due to service failures by the railway. This provision was added as part of Bill C-30 *Fair Rail for Grain Farmers Act* passed in 2014. This Act also provides for regulated inter-switching up to 160 km on the three Prairie Provinces, up from the maximum limit of 30 km that is in effect in the remainder of Canada. Bill C-30 also mandated the Agency to determine the amount of export grain each of CN and CP must carry each week during the crop year. The

provisions added by Bill C-30 are all temporary and will expire on August 1, 2016 if not explicitly extended by Parliament.

5.2 The Implications for the Review

After three decades of deregulation of the commercial framework of railway activity, the railways have made significant gains in their profitability and have leveraged their market dominance in ways that would not be possible if there was effective competition. Changes to the *Canada Transportation Act* in 2008, following from the last statutory review, and the subsequent passage of Bills C-52 (2013) and C-30 (2014) have acknowledged the market power of the railways and the need to provide a legislative and regulatory framework that re-balances the bargaining power.

The extraordinary actions of the government with the Order-in-Council and Bill C-30 in 2014 in response to major service problems for grain shippers demonstrated that the right balance has not yet been achieved. The FMA recommendations in Section 6, below, are designed to continue this trend to finding the right balance between the railways and their customers.

6.0 Recommendations by FMA

Following from the railways' market dominance and the preceding analysis, and after consultation with our member companies, FMA makes the following recommendations. It should be noted that we are not recommending legislative wording, except recommendation 1, but stating the desired result of each recommendation.

1. Sections 113-116 of the Act, the *Level of Services,* or "Common Carrier" provisions are of fundamental importance and have been part of railway law for over a century. Section 113. (1) (b), states: "…*furnish adequate and suitable accommodation for the carriage, unloading and delivering of traffic*". Section 113 (2) states *"Traffic must be taken, carried to and from, and delivered at points referred to in paragraph (1) (a) on payment of the lawfully payable rate".* There is nothing in Section 113 that requires the railway to specify the time to effect delivery. To provide greater certainty for shippers, it is recommended that the term "*suitable and adequate accommodation"* should be defined in the Act as follows:
   "For the purposes of sections 113 and 114, a railway company shall fulfill its service obligations in a manner that meets the rail transportation needs as may be reasonably defined by the shipper".

2. The Canadian Transportation Agency cannot act on its own initiative, it must respond to complaints. The Agency should have the power to undertake investigations on its own initiative and require corrective action by the rail carriers. This is an issue of broad continental concern and there is currently a Bill before the U.S. Congress that would give the U.S. Surface Transportation Board the authority to undertake investigations of pricing and service matters on its own initiative. (See Appendix 1)

3. The Competitive Line Rate (CLR) provision is not working. This is one of the provisions that is a "surrogate" for real competition. Where a shipper is captive to one railway, and the first interchange is beyond the 30 km regulated inter-switching limit, the shipper can obtain a regulated rate imposed by the Agency on the originating railway to the interchange, but only if the shipper can negotiate a rate from the connecting carrier.

Both Class 1 railways have refused to quote such rates, rendering this provision unworkable. This provision could be remedied by removing the requirement for the shipper to first obtain a rate from the connecting carrier. The Agency has the knowledge, experience and data to compute such rates on a fair and equitable basis. In addition, in the event that the connecting carrier refuses to quote a fair and reasonable rate, it is recommended that the Agency should then set the rate that the connecting carrier may charge from the connection to destination.

4. The costs of Final Offer Arbitration (FOA) to solve rate disputes can be a barrier to its use for small and medium sized shippers. It is recommended that Transport Canada be authorized to investigate the application of FOA with a view to making this important shipper protection provision more accessible to small and medium size shippers.

FOA decisions are currently authorized for one year. It is recommended that such decisions be authorised for a minimum of two years, or as included (either longer or shorter) in the shipper's offer, should the shipper's offer be accepted by the arbitrator. The longer minimum term will help minimize the longer-term financial burden on shippers and may lead to a more realistic offer by the railway.

5. The Class 1 freight railways have market power, and the financial markets look favorably on the pricing power of the North American Class 1 railways, (see Appendix 2). This pricing power is real and there needs to be some control on rates that can be charged, as is the case with other comparable industries. For example, the Ontario Energy Board regulates various aspects of electrical generation and the distribution of electricity and gas, including pricing.

There is frustration among rail shippers with the difficulty in directly negotiating competitive rates with the railways and a belief among some shippers that some constraint on railway pricing is necessary. The report from *Blacklock's Reporter,* January 20, 2015 is an example of shipper frustration with the current situation; see Appendix 4.

With the passage of the *National Transportation Act, 1967,* giving the railways a degree of pricing freedom, there were both minimum and maximum limits on the rates that could be charged related to "Long-Term-Variable-Cost" as determined by the regulator. There has been a long-term trend to deregulation of the railway industry, including almost unlimited pricing freedom. It has been reported by some FMA members that, after the 2008 downturn in the global economy, their

rail service providers continued to increase rates while their trucking service providers, an industry where there is effective competition, were reducing rates.

It is recommended that railway pricing freedom should be constrained by establishing a regulated rate of return on capital invested. This will continue to provide reasonable pricing freedom for the railways while providing some constraint on abusing their pricing power. .

6. The Shipper Need for Transparency of Rail Data

The railways know their pricing to a large number of customers. The customers do not have access to similar comparative information. A needed change is access to market information that will provide transparency for rail customers with regard to financial and operational data which is needed in their direct negotiations with railways, and provide them essential information in utilizing the Final Offer Arbitration (FOA) remedy to settle rate disputes.

The U.S. Surface Transportation Board (STB) data sources provide a useful model in the supply of railway data that is available to shippers and other supply chain participants using U.S. railroads. The STB has three data sources that it makes available publically.

a) Quarterly Commodity Statistics (QCS)
-Volume and revenue by commodity for Class 1 carriers
b) Public Use Waybill Sample (PUWS)
- Annual random sample of freight bill data with confidentiality safeguarded
c) Commodity Revenue Stratification Report (CRSR5)
- Comparison of rail revenues to the Uniform Rail Costing System costs aggregated to five digits of the Standard Transportation Commodity Code (STCC)/AAR1 equipment type combination used throughout North America

It is noted that the Canadian Class 1 carriers supply this information to the STB for the QCS (U.S. portion only) and for the PUWS on cross-border moves, as well as on their U.S. domestic traffic. The CRSR5 data is developed by the STB from a random sample of freight bills.

This data is used by shippers and consultants supporting the shipper community, to assist them in transportation planning and in their price negotiations with U.S. railroads.

Data from aggregated waybill samples, and other comparable commodity flow information should be collected by the Agency and made available to shippers. This is necessary to bring balance to rate negotiations.

In addition, with the commencement of arbitration to obtain service level agreements from railways, it would be helpful for operational and service data to be collected by an independent party and made available to shippers in order to achieve fair and balanced arbitration decisions.

It is recommended that the *Canada Transportation Act* be amended to require the railways to provide the appropriate information to the Canadian Transportation Agency and that relevant information is made available to Canadian shippers to bring balance to the negotiations between shippers and railways.

7. Bill C-30, introduced several temporary provisions that will expire on August 1, 2016 unless Parliament takes further action before that date. One of these provisions, new section 116 (4) (c.1), authorizes the Agency to order the railway "*to compensate any person adversely affected for any expenses that they incurred as a result of the company's failure to fulfill its service obligations…."* It is recommended that this provision be made permanent.

8. Short Line Railways are an important part of regional transportation markets but their finances generally limit the availability of capital to invest in the fixed plant and to upgrade to the latest standards, e.g. to handle 286,000 lb. cars on four axles. Short-line railways are specifically mentioned in the *New Canada Building Fund: Provincial-Territorial Infrastructure Component –National and Regional Projects (PTIC-NRP).* Eligible recipients include private sector bodies who can apply to a provincial government. It is recommended that Transport Canada, in cooperation with Infrastructure Canada, undertake a specific communications program with both short-line railways and provincial governments to encourage them to take advantage of the PCIT-NRP program.

9. Retaining railway branch and spur lines for freight use can be important to industries in some locations. Under the Division V of the *Act,* the Class 1 railways may convey such lines to government or private buyers who wish to continue operation as a short-line. A potential buyer may request an evaluation of the "Net Salvage Value", including the value of the land under section 144 (3.1) of the *Act*. The Agency's determination of the land value may consider adjacent land values related to the current use of such land. This may lead to land values that make acquisition of such branch-lines uneconomic to potential short-line operators, passenger and commuter operators, or industrial users. It is recommended that the government should give policy guidance to the Agency with regard to determining land values of branch lines where there is a possibility of maintaining railway operations.

The railways will have enjoyed tax benefits from the rights-of-way being evaluated as rail lines and not related to the valuations of adjacent properties. Selling prices of branch lines should be based on the value as a railway right-of-way.

10. The use of shipper supplied cars has become more difficult for shippers in recent years. The railways are controlling the shippers' ability to acquire and use private rolling stock as contemplated in s. 113 (3) of the CTA. The railways accomplish this by requiring the shipper to essentially get permission or approval through a process called AAR Circular No. OT-5, effective January 2009.

Section III (b) of OT-5 states: “the railroads’ use of private cars other than tank cars is not required unless railroad provided cars are not available”.

As a result, shippers are not able to gain the benefit associated with an adequate car supply as defined by the shipper to meet its obligations to its customer. The railways are using the AAR to restrict the shipper’s ability to manage its supply chain efficiently. It is recommended that Section 113 (3) of the *Act* be amended to state explicitly that where the shipper intends to supply its own cars, it will not be constrained by unilateral railway action. (See appendix 3)

11. Contracting away rights: Railways are increasingly using their market power to obtain contract terms from shippers that prevent a shipper from accessing the full shipper protection provisions of the *Act* and some terms are contrary to the *Act*. For example, a railway might require a term in a shipping contract, or even a simple siding agreement, that says the shipper can’t use regulated interswitching to access other railways within the 30 km limit. A shipper would almost always have to agree to this since going to an expensive FOA process over one or two items is not reasonable. This practise should be declared unlawful with financial penalties if such contract terms are discovered in existing contracts, and if discovered, should be declared null and void.

As the Agency has no authority to oversee confidential contracts, the *Act* would have to be amended to give the Agency the power to ensure contracts do not include such terms. It is recommended that the Agency be given the power (on application by an affected party) to determine whether any contract contains such a provision. Any such amendment should explicitly state that the provision is retroactive and applies to existing contracts when the provision comes into force.

8.0 Concluding Remarks.

In the Discussion Paper, issued by the Hon. David Emerson, P.C., it stresses the need to look at Canada’s transportation needs over the next 20 – 30 years. That is, what will Canada’s economy need from its transportation system in terms of investment, infrastructure, overall transportation capacity, information systems, laws and regulations, productivity improvements, and policies to facilitate effective global supply chains for Canadian industry? This paper focuses exclusively on rail freight and, while most of the recommendations address current issues, the long-term efficiency of the rail freight system, finding solutions to these current issues is a necessary building block in ensuring that our freight transportation system will be able to effectively meet the future needs of the Canadian economy.

FMA will be making a second submission within the next few months addressing marine, trucking, and air cargo issues and will also include comments on the longer-term strategic needs, including infrastructure, to effectively support

Canadian competitiveness in global markets.

FMA and representatives of its member companies would be pleased to meet with the Chair of the Review and the Advisory Panel to discuss the shipper-railway relationship and the recommendations that the Association is putting forward in this paper.

Appendix 1

From the U.S. Senate

Coalition Support for S.2777

September 15, 2014

Dear Members of the Committee on Commerce, Science and Transportation:

We are writing to you on behalf of a broad range of manufacturing, agricultural, and energy industries, urging you to support S. 2777 "The Surface Transportation Board Reauthorization Act of 2014" which would improve how the Board operates. The reforms in this bill would help make the STB a more timely, efficient and equitable regulatory agency and we strongly support this bill's passage.

Congress created the STB to evaluate the reasonableness of rates when a railroad has market dominance over a customer. Unfortunately, STB policies make the agency virtually inaccessible for many rail customers. The Board estimates that their main remedy, a stand-alone cost challenge, takes 3.5 years and $5 million to litigate, and requires the plaintiff shipper to create from scratch an entire fictional railroad to prove the rates are excessive.

The bill introduced by Chairman Rockefeller and Ranking Member Thune would reauthorize the STB for the first time since it was created, and would make the Board a more viable forum for handling freight rail issues. The legislation would streamline rate case procedures, create a meaningful alternative dispute resolution process, and require an analysis of the rules under which the agency operates. Other common sense improvements include allowing the Board members to discuss agency matters with each other, launch their own investigations, and create timelines for cases.

The Staggers Rail Act of 1980 envisioned an STB that would "allow, to the maximum extent possible, competition and demand to establish reasonable rates… and to provide expeditious handling and resolution on all proceedings." We agree with this vision. However, the current policies fall far short of this shared goal. Even the Chairman of the STB recently said in a published opinion that "we should never be satisfied with a process that is so expensive and time consuming."

Please support the Surface Transportation Board Reauthorization Act of 2014. The vitality and success of the U.S. railroad industry is in no way inconsistent with having, and in fact will support a well-functioning STB. The reforms proposed by the Chairman and Ranking Member will make important and necessary improvements that are consistent with the direction Congress set under the Staggers Rail Act.

Appendix 2

The Investors' Perspective

Attractive Competitive Environment

- The railroad competitive environment is arguably the envy of most industrial sectors, boasting limited competition and steep barriers to entry. …. with CN and CP both enjoying a comfortable duopoly that prevents excessive competition
- This position is further sweetened by the fact that rail remains the only cost effective alternative for several freight categories…

(Raymond James Financial Inc. report to investors, May 2009)

Appendix 3

Background on Railway Constraints with Shipper Supplied Cars

Railways have adjusted the private car process over the years by changing the requirements as indicated on the evolving OT-5 form. At one time the shipper's cars had to only meet a technical specification and since they are all built to the AAR standard this was a simple formality. Railways then added requirements such as having sufficient parking space for the all the cars and later only allowing a shipper to acquire (and use) cars if the railways cars are not available. This latter requirement is particularly concerning because car availability is different when viewed by the railway as opposed to the shipper. For example, the shipper needs a timely supply of cars whereas a railway does not have such a high standard and the railway supply of cars can be dynamic (available today but not tomorrow) and thereby unreliable given the demand by other shippers for the same cars.

It is the railways intention to compel the shipper to use the railway cars (and pay a higher rate) when available and park the shippers cars, this is an unworkable and inefficient situation for the shipper. The exact opposite is how the system must operate.

Appendix 4

Blacklock's Reporter January 20, 2015

Feds Faulted On Rail Policies

Cabinet initiatives to improve rail service fail to address "high-level" challenges that threaten the export trade, says one of the country's largest private grain shippers. Parrish & Heimbecker Ltd. of Winnipeg made the appeal after winning a federal court judgment on rail regulation.
"We're damaging Canada's long-term competitiveness," said John Heimbecker, vice-president; "The government has never been able to rationalize what shareholders want out of railroads, and what shippers want."

"It's a dichotomy that is not resolved by shipping quotas or rules on interswitching," Heimbecker said in an interview. The company earlier won a Court of Appeal ruling compelling Canadian Pacific Rail Co. to switch its grain cars at a Coutts, Alta. border crossing at regulated interswitch rates of less than a quarter CP's regular freight charges, $315 per car compared to $1,373 a car.

Heimbecker said interswitching regulations, and 2014 rules compelling CP Rail and Canadian National Rail Co. to ship a minimum weekly quota of grain, were useful but failed to address fundamental problems in rail transport.

"The problem in my view really flows from the government getting out of the railroad business," he said. Canadian National, formerly a Crown railway, was privatized in 1995.

"The government has never been able to rationalize what shareholders want out of railroads, and what shippers want," he said. "They made an assumption that railways want to ship as much freight as possible, and so do shippers – and that was a clear governmental miscalculation."

"The needs of shareholders are vastly different," Heimbecker continued. "They are not there for the benefit of shippers. They are there for the benefit of shareholders. Railways don't add new assets into the system because it's a cost at the expense of shareholders"; "If it is in the strategic interest of Canada to have a rail duopoly, we have to put in shipper protection which at the same time is not going to punish investment by shareholders. This is very hard."

"Nobody Wants To Address This"
"The government has introduced quotas and interswitching regulations, but it doesn't close that gap," he said. "That's my view. They are short-term solutions to a long-term problem. Nobody wants to address this at a high level."

Cabinet last March ordered the two largest railways to ship a minimum 500,000 tonnes of grain a week to ease a massive backlog from a record harvest. Quotas have been extended twice under threat of $100,000 fines on railways.

Western Canadian Wheat Growers had urged cabinet to let tonnage rules expire due to a smaller crop last summer. Shippers of other goods, and port authorities, also protested the quotas as an unfair restriction on their own traffic.

“If you accept that railway shipping in Canada as an export country is the most important infrastructure that we have, then the question becomes: how can we bridge that gap between the interests of shippers and railway shareholders?” Heimbecker said. “They can try to bridge it with quotas, but the quotas hurt one side. It means shareholders receive less return.”

Parrish & Heimbecker Ltd. operates flour and feed mills; production lines including Butterball turkeys; grain trading offices in Vancouver; Lethbridge, Alta.; Winnipeg and Toronto, and 20 elevators, shipping more than two million tonnes of grain annually, by company estimate.

By Tom Korski