Keystone Agricultural Producers Submission Canada Transportation Act Review

Please contact Keystone Agricultural Producers general manager, James Battershill, with questions about the information or recommendations included in this submission at the address below.

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Executive Summary

A reliable and competitive grain handling and transportation system (GHTS) is critical to the financial success for farmers, grain shippers, class 1 railway companies, and the Canadian economy as a whole. There have been rail industry reforms over the past three decades that have acted to increase railway profitability, but have not delivered cost and service improvements for grain shippers and farmers. In the future, Canadian farmers will export more grains, oilseeds, and pulse crops through increased global trade, industry investment into crop varietal development, and the resulting increase in harvest sizes.

Lack of meaningful competition is the root cause of Canada's GHTS challenges, including poor service and a lack of incentive to invest in capacity, infrastructure, and labour. In order to overcome the lack of competition, government must develop regulations that simulate a competitive market environment. KAP recommends that this be accomplished through enhanced investigative powers for the Canada Transportation Agency, and continued support for the Maximum Grain Revenue Entitlement program. Further, KAP supports government action that encourages competition in the GHTS as a means of encouraging improved service levels for farmers, including support for producer car shippers and shortline railways.

Summary of Recommendations

<u>Recommendation #1:</u>

That the Canada Transportation Agency be mandated to independently investigate rail freight service problems and initiate meaningful action to improve railway performance.

<u>Recommendation #2:</u>

That the Canada Transportation Agency be provided with the operational resources necessary to fulfill an expanded mandate.

<u>Recommendation #3:</u>

That level of service provisions be strengthened and specific definitions, obligations and requirements be set out in regulation.

<u>Recommendation #4:</u>

That service level agreements be required to include provisions for penalties to be paid by the railway company for failure to deliver to the agreed upon service levels.

<u>Recommendation #5:</u>

Arbitration options be offered for dispute resolution between shippers and railways.

<u>Recommendation #6:</u>

Monitoring of railways performance be increased and this information be made publicly available.

Recommendation #7:

That future minimum volume requirements be allocated to specific shipping corridors.

Recommendation #8:

That the CTA Review support the continued application of the MGRE program when considering any legislative or regulatory changes.

Recommendation #9:

That the penalty on railways for exceeding the maximum revenue cap be increased threefold from 5% to 15%, and that this money continue to be paid to the WGRF.

Recommendation #10:

That a costing review be performed with respect to the railways to take into account the efficiencies they have gained over time so that increases to the MGRE can be kept in check.

Recommendation #11:

Ensure that farmers have a reasonable ability to ship producer cars and receive adequate service from class 1 railway companies, recognizing that this may require unique provisions not provided to larger shippers.

Recommendation #12:

Support shortline railways to operate trains and solicit traffic in regions underserved by class 1 carriers.

Recommendation #13:

That chickpeas and soybeans be added to the list of Schedule 2 grains under the CTA.

Introduction

Keystone Agricultural Producers (KAP) is Manitoba's general farm policy organization. KAP policy is set by members from more than 7,000 farm families from across Manitoba and by 19 commodity group members.

KAP's preliminary submission to the Canada Transportation Act Review has been developed using policies established over our 31 year history. Information presented is based on consultation, discussion and debate by KAP members, and input from KAP's Transportation Committee, the CTA Review Coalition, shortline railway operators, and producer car shippers.

Every issue that shippers experience, from lack of accountability and transparency, to poor service levels on the part of the railways, are also impacting smaller shippers, producer car shippers, and shortlines. We have devoted a section to this topic in our submission to highlight their unique position in Canada's grain handling and transportation system (GHTS).

KAP also participated in the development of the CTA Review Coalition submission, and we endorse its recommendations.

Reason for Rail Freight Industry Reform

Rationalization

During the late 1980's and the early 1990's a variety of regulatory reforms were introduced that were intended to usher in a 'new era' for Canada's railway transportation system. The reforms were focused on competition, reducing regulatory intervention, and developing more innovative transportation services. The rail network rationalization provisions enabled the railways to become more efficient through improvements in productivity. Streamlined branch line abandonment procedures included the transfer of lines to independent operators and funding of improvements for alternative transportation facilities.

More reforms were introduced during the late 1990's, and an *Act to Amend the Canada Transportation Act* came into force in 2000. Among the changes were amendments that facilitated branch line rationalization through: transitional compensation for affected municipalities; operation of the remaining part of the branch line for three years; discouraging de-marketing through maintenance deferrals; and identification of lines for discontinuance within a three year time frame.

Railways consider rationalization a success and total productivity of both railways increased throughout the reform period. Total factor productivity of both CN and CP increased on average between 3.5% and 4% between 1990 and 2007. The operating ratio of both railways indicates that they have succeeded in reducing their expenses while increasing their revenue throughout the 1990s and 2000s. At the same time, employment for both railways decreased by approximately 35,000 employees or 50% of their work force (*Railways in Canada and the*

Experience with Regulatory Reform – With Emphasis on the Competitive Provisions, Joseph Monteiro & Gerald Robertson).

The impact of railway rationalization on farmers continues to be experienced. The discontinuance of grain dependent branch lines means increased transportation costs for farmers to truck their grain to delivery points and it reduced competition between grain companies. In 1999 there were more than 1000 licensed grain elevators in Western Canada; by 2014 that number dropped to 342. The railways have seen the benefits of rail reform, through greater profitability, but the promises made that rationalization will lead to better service for farmers, and rail freight shippers generally have not been fulfilled.

Industry Investment and Change

The total volume of grain harvested in Manitoba continues to grow, along with the need to move grain to Canada's export markets. The current growth rate of grain production in Western Canada is approximately 3.3% per year and current trends indicate that will continue to increase. In 2013, five of the six major grains and oilseeds growing in Manitoba set new yield records (the sixth, canola, tied a yield record from 2009).

Crop production will continue to increase in Manitoba and across Western Canada as farmers see the benefits of increased investment in varietal research and crop production techniques. When the *Agricultural Growth Act* comes into force in 2015, it is expected to enable a more competitive environment that will attract investment in variety development for better yields, crop quality, and disease resistance.

The market for identity preserved (IP) crops is expected to increase in coming years. Identity preservation is a process or system of maintaining the segregation and documenting the identity of a product. These are primarily bulk commodities that are designated identity persevered to access certain markets and accommodate certain buyer's needs. The most common use to date has been seed production and distribution but IP sales are expected to increase with the growing demand for non-traditional products. One of the most important components for identity preservation is traceability. There needs to be documentation relating to the crop showing where it comes from and where it has been, and therefore the ability to accurately track the shipments and movement of goods through rail is critical.

Trade

Growing Canada's export market and developing trade relationships across the globe are priorities of the Government of Canada. CETA, the Comprehensive Economic and Trade Agreement, will remove up to 98% of tariffs between Canada and the European Union. It is being called the most ambitious cross border trade agreement for Canada since NAFTA and will allow Canada to sell agricultural commodities, including wheat and canola oil, to European Union countries without an import tariff.

Canada is also actively participating in negotiations under the Trans-Pacific Partnership (TPP) and is looking to increase its export markets in the Asia-Pacific region. In March of 2014 Canada signed the Canada-Korea Free Trade Agreement which is expected to boost Canada's economy by $1.7 billion and increase Canadian exports to South Korea by 32%.

The Government of Canada is committed to advancing trade as a means of growing Canada's economy and contributing to long term prosperity. As trade opportunities continue to grow, so too will demands on our transportation system to export high value Canadian grain and other products. The only way Canadians will experience long term success and see economic returns will be if Canada demonstrates that it is a reliable supplier of products. This will only be achieved through a reliable GHTS, which we currently do not have.

2013-2014 Grain Shipping Crisis

Manitoba farmers grew a record crop in 2013-2014. In late summer, farmers were celebrating a record harvest but by late fall, issues with our GHTS were already becoming apparent and limiting farmers' opportunities to market their crop. By early winter, we had entered a full on crisis in grain shipping. National railways, rather than investing in increased capacity, had continued down a path focused solely on efficiency as the only driver of success and limitations of the system were made clear.

In 2012, CP rail cut approximately 1,700 jobs through layoffs, attrition and the use of fewer contract positions. They plan to eliminate up to a total of 4,500 jobs by 2016 - about 23% of their 19,500 employees and contractors. CP's entire system underwent a restructuring with the end goal of increasing efficiency. To do this, they moved their head office and re-evaluated their real estate holdings, laid off employees, and planned to use 195 fewer locomotives and lease 3,200 fewer freight cars.

These efficiency measures coupled with a cold winter and the bumper crop made grain movement stall throughout the Prairies and farmers and grain shippers experienced some of the worst levels of rail service in Canadian history. As a result of the lack of shipping capacity, farmers experienced record high basis levels that Richard Gray from the University of Saskatchewan estimates were 250 to 300% higher than normal basis levels based on costs between primary elevators and free on board (FOB) positions.

The Western Grain Elevator Association (WGEA) notes that average unloads during the shipping weeks 1-13 of 2013 were significantly below weekly railcar capacity which is directly linked to limited cars and service supplied by CN and CP. The data the WGEA collected demonstrates that the loading and unloading capacity of the current rail systems contradicts the service levels the Canadian railways argue they are providing.

Quorum, as Canada's grain monitor, looked very closely at the numbers as the grain crisis emerged. They note that the 33.4% increase in crop size from 2012 presented a number of challenges for the grain handling and transportation system in Canada, and that even though there was a drastic increase in crop production, the total grain supply handlings during the same period actually declined. Their quarterly report for the second quarter of 2013-14 states,

> "By mid-September 2013 the demand for carrying capacity in the country was outpacing what was being supplied by a factor of 10%, leaving the equivalent of about 1,000 carloads of traffic going unmoved each week. The effects of this were also beginning to spread, with terminal elevator stocks declining by as much as 20% from what had been observed during the same period a year earlier. More importantly, the number of vessels waiting to load at port had begun to climb. For its part, the carrying capacity supplied by the railways proved roughly equivalent to that supplied during the same period a year earlier. The situation was made all the worse given the urgency to sell grain in a market already characterized by declining prices… By the close of the second quarter country elevators stocks had risen to 3.7 million tonnes; uncommitted railcar orders had increased to over 50,000; and the number of ships waiting to load at west-coast ports had topped 40."

Government Response

KAP supported the actions of the Government of Canada when they introduced an Order in Council on March 7, 2014 to help address the grain transportation crisis. The minimum volume requirements for both CN and CP were a welcome action. KAP continues to support the use of minimum volume requirements at this time, however, our members want more comprehensive actions taken to address the root causes of the crisis that will result in the entire GHTS working more efficiently and competitively to ensure that immediate government intervention is not needed in the future.

Uncompetitive Markets

In competitive markets, economic forces balance the service needs of customers with the financial cost of adequate service delivery. When customers have service choices, they take their business where they determine that the quality of service they receive is worth the price they are charged. On the other hand, a duopolistic or oligopolistic marketplace refers to a market structure where there are only a few firms (in this case two) that make up an industry. The service that the oligopolistic firms provide is nearly identical, making the companies interdependent in competing for market share. This creates the potential for a non-competitive marketplace, as the two firms have no reason to compete on price or service when they each have such a significant share of the market.

The rail freight industry is one such marketplace. While rail deregulation has been successful in that CN and CP are financially viable and have achieved gains in productivity, Prairie farmers, and the Canadian economy as a whole, have not seen similar benefits.

As mentioned in the Rail Freight Service Review, published in 2011 by Transport Canada, there is still little competition and a high degree of captivity that exists in the rail-based supply chain.

Producers are almost exclusively reliant on rail to move their products to port, and even when they have the option to choose between CN and CP, a duopoly does not provide them with the necessary leverage to achieve adequate service or alleviate service problems. Railways have no reason to invest in capacity because they very rarely compete for business. Satisfaction with rail service has in fact been in decline for the past decade. A survey done in conjunction with the 2001 CTA Review Panel Report found that 71% of carload shippers and 85% of non-intermodal users were satisfied with overall service provided by the railways. A similar survey carried out in 2009 by the University of Manitoba Transport Institute found that just 17% of respondents still rated railway service as satisfactory.

As a result, government has a responsibility to mandate certain basic service levels, especially in an industry that is critical to the overall health of the Canadian economy. This is done in many industries where barriers to entry are high and competition is limited, including telecommunications and passenger air travel. The Government of Canada has taken a two-pronged approach to improving service in these uncompetitive industries by introducing programming and regulations that help simulate a competitive marketplace; and using policy tools to encourage competition. In the case of telecommunications, the Government of Canada is actively encouraging competition by limiting access to new wireless spectrum auctions for established companies. They are also regulating basic service standards when necessary, including the 2013 decision to limit cellular phone contracts to two years.

KAP supports this dual approach to managing uncompetitive industries and encourages the Government of Canada to apply this same philosophy when addressing rail freight shipping industry challenges. Our recommendations will focus on these two areas, recognizing that it is very difficult to encourage competition due to barriers to entry into the marketplace.

Simulating a Competitive Market through Programs and Regulations

The following recommendations are made based on the principle that in an uncompetitive market, government has a responsibility to ensure that market power imbalances are kept in check through programs and regulation. The goal of these programs should be to ensure that customers have access to adequate service at a cost comparable to what they would pay in a competitive industry.

The Canada Transportation Agency

The Canada Transportation Agency (the Agency) plays a valuable role in overseeing the GHTS including administration of the Maximum Grain Revenue Entitlement (MGRE) program and investigating service level complaints against carriers. For reasons below, KAP recommends enhancing the independent investigative powers of the Agency.

The current service level complaint process is not an effective tool for the majority of shippers because of the financial cost and time associated with launching a formal complaint. Many shippers KAP consulted with, both large and small, indicated that their limited legal resources made launching a level of service complaint an impractical tool for solving service problems.

Further, every shipper that KAP consulted with independently identified fear of railway retaliation as a reason for not wishing to file a complaint. With no meaningful shipping alternative, intentional delays in car delivery or pickup can have a devastating impact on the operations of a single shipper.

Shippers, if they so choose, should continue to have a formal service level complaint process available to them. The Agency however should be tasked with advanced system performance monitoring, either internally or through the Grain Monitor Program. When performance metrics including total outstanding car orders, car cycle times, and national average basis levels do not meet a specific threshold, KAP recommends that the Agency be empowered to respond by investigating the cause of the issue.

The Competition Bureau sets a precedent for government to take both responsive and proactive action in this manner. The Bureau is mandated to independently launch investigations into issues that it deems to be of concern, respond to specific complaints launched by Canadians, and investigate specific market transactions that meet specific criteria. The Bureau has this authority specifically because there is no actor in the marketplace willing or able to address problems related to lack of market competition. The Agency should be empowered in a similar way for the same reason. KAP further recommends that the Agency be provided with the resources necessary to fulfill their mandate and obligations. Given the losses to the Canadian economy associated with railway service failures, this investment in system oversight is viewed as critically important by shippers.

Recommendation #1

That the Canada Transportation Agency be mandated to independently investigate rail freight service problems and initiate meaningful action to improve railway performance.

Recommendation #2

That the Canada Transportation Agency be provided with the operational resources necessary to fulfill an expanded mandate.

Level of Service

There is presently a basic legislated level of service in Section 113(1) of the *Canada Transportation Act*. It states:

> "A railway company shall, according to its powers, in respect of a railway owned or operated by it,
>
> > (b) Furnish adequate and suitable accommodation for the carriage, unloading and delivering of the traffic."

The challenge is that this is a subjective standard for measuring service levels, and it has traditionally worked to shield the railways from allegations of service level problems. If a railway fails to meet its service obligations a shipper has the option to embark on a lengthy complaint process through the Agency to determine if the railway has met the standard of 'suitable and adequate'. This requirement is currently open to interpretation, and KAP recommends this provision be strengthened through a more explicit definition and specific criteria defined in regulation.

The recent level of service complaint filed by Louis Dreyfus against CN sets legal precedent for what should be included in this definition. In the CTA's interlocutory decision they acknowledge that the wording of 'suitable and adequate' dates back to 1906, and the Supreme Court of Canada has historically interpreted statutory level of service provisions using a test of reasonableness. The CTA states,

> "It is clear that *Patchett* [*Patchett & Sons Ltd v. Pacific Great Eastern Railway Co.*, (1959) S.C.R. 271 (*Patchett*)] and the reasonableness test do not stand for the proposition that the level of service obligations only impose a soft obligation on railway companies. Railway companies must furnish adequate and suitable accommodation for the carriage, unloading and delivering of traffic that meets the requirements of the shipper, as long as the shipper has properly triggered the level of service obligations. In this regard, the railway company must comply with those obligations unless it demonstrates that it cannot reasonably do so."

The CTA's decision of October 3, 2014 looks at the legislative history and intent and purpose of service level provisions within legislation, and it also looks at how the courts have interpreted these provisions. They also go even further and expand on an 'Evaluation Approach' to determining whether a railway company has breached its service level obligations.

The evaluation approach works very simply. It asks,

1. Is the shipper's request for service reasonable?
2. Did the railway company fulfill this request?
3. If not, are there reasons that could justify the service failure?

    (a) If there is a reasonable justification, then the Agency will find that the railway company has not breached its level of service obligations;

    (b) If there is no reasonable justification, then the Agency will find that there has been a breach of the railway company's level of service obligations and will look to the question of remedy.

The CTA would look at the specific needs of shippers in determining what is reasonable, and evaluate effort. It would also assess whether a railway met its statutory obligations. KAP agrees that this approach can be beneficial for shippers.

> Recommendation #3
>
> That level of service provisions be strengthened and specific definitions, obligations and requirements be set out in regulation.

Service Level Agreements

Producers are in a unique and vulnerable position in the grain handling and transportation system. They provide the commodities that are being marketed and shipped, and they also carry the most risk due to system disruptions. Prior to the March 2014 Order in Council grain producers in Western Canada were severely limited in their operations due to the lack of grain movement. Some estimates of farm losses reach as high as $3 billion lost due to the grain backlog. This has a significant impact on a producer's ability to maintain cash flow, balance farm accounts, and contribute to rural economic development.

Another measure that KAP recommends to overcome service level failures is the inclusion of reciprocal penalties in service level agreements (SLAs). Based on the inherent power imbalance between the railways and the shippers, KAP would see the Agency make it mandatory for penalty provisions to be included in SLAs. Currently, the railways have the ability to impose penalties on shippers for non-performance. Strong wording and a contractual obligation of a penalty incurred by the railways within an SLA could provide a significant shift in the market power imbalance between shippers and class one railway companies.

We want to briefly recognize that amendments to the *Canada Grain Act* in the *Fair Rail for Grain Farmers Act* allow for penalty provisions in grain contracts, including financial penalties in case of breach of contract. We would like to see the same principles applied to protect shippers from breaches of contract on the part of the railways. The Government of Canada has given farmers a way to recover losses, but still have not addressed the root cause of the problem.

Another amendment in the *Fair Rail for Grain Farmers Act* gives greater powers to the Canadian Grain Commission to appoint an arbitrator to settle disputes between producers and elevators and also allows for suspension of an elevators license should an agreement not be reached. We recommend that the same bold provisions for dispute resolution be included in the *Canada Transportation Act* to settle disputes between shippers and the railways. By having an effective third party arbitration system the shippers can have more confidence in their contractual agreements which transfers to more reliable service for farmers. KAP recommends offering different types of arbitration. Final offer arbitration processes might discourage shippers from coming forward, but a mediation or conflict resolution style of arbitration may provide more positive outcomes.

Recommendation #4

That service level agreements be required to include provisions for penalties to be paid by the railway company for failure to deliver to the agreed upon service levels.

Recommendation #5

Arbitration options be offered for dispute resolution between shippers and railways.

Transparency and Information Reporting

Accurate and timely information relating to car allocation, spotting, and loading is necessary to address market power imbalances in the GHTS. If everyone is able to work from the same precise information many situations where shippers and producers become frustrated over lack of cars or capacity can be alleviated.

Elevators plan their operations and staffing around car allocation and spotting information provided by the railways. Any variation in this information causes elevators to quickly alter their plans leading to more work hours for employees, and inefficiencies in car loading. This trickles down to the farmer who makes a plan to market grain based on the information provided by the elevator/shipper.

Transparency is critical to effectively functioning markets. Farmers consistently provide Statistics Canada with information related to production and farm stock levels, and railways and grain companies should be required to supply information to a public forum.

The United States Department of Agriculture (USDA) has been mandated to obtain information conducive to more efficient market operation. Additionally, the U.S. Surface Transportation Board (STB), which operates as a regulatory body overseeing railroad conduct in the United

States, has recently become stricter in requiring railways to submit additional information on grain movement and rail service. It is seeking to expose rail service deficiency with a public spotlight. The railway companies in Canada should be held to a similar standard.

The information that we would see railways, grain handlers, and port authorities submit to the CTA on a weekly basis includes:

1) Five year, annual and seasonal operating plans including factors such as targeted asset levels and expected traffic and performance levels.
2) Confidential contracts and agreements affecting operations between railways.
3) Waybills on all traffic handled on Canadian railways.
4) Weekly car allocation by all corridors and crops.
5) Weekly port updates.
6) Vessel line ups by port.
7) Producer car allocations and outstanding orders.
8) Ocean freight rates with demurrage/despatch levels.
9) Weekly rail car movement by corridor.
10) Weekly backorders of rail cars by province, by railroad, by destination.
11) Weekly future orders for rail cars by province, by railroad, by destination.
12) Performance measures for all industry participants including dwell times.

We also recommend that the CTA publish annual railway revenue summaries and costs by both corridor and commodity.

Finally, we recommend that the railways provide detailed capacity and performance data to an independent monitor to support the development of a comprehensive series of timely railway capacity and performance measurements. This monitor will publish performance measurements for all commodities and corridors, as well as provide support for the CTA with respect to railway performance analysis.

Recommendation #6 Monitoring of railways performance be increased and this information be made publicly available.

Corridor Specific Allocation

Manitoba's geographic position in Canada makes it an ideal place from which to move grain. Trains can move east to Thunder Bay, west to the port of Vancouver, north to the port of Churchill, and south to the United States. The 2013-14 bumper crop should have provided increased activity in each of those corridors, benefiting all ports, producers, shippers and customers. KAP members supported the Order in Council, and were grateful for the relief it provided to the grain backlog. Unfortunately, there was an unintended consequence of the Order in Council in that it mostly served west coast ports due to shorter car turnaround times. Any corridor specific issues that were prevalent prior to the government mandated volume requirements increased after the Order in Council was implemented. As well, ports in Prince Rupert and Vancouver experienced challenges with the increased car deliveries while other Canadian ports saw a decline in productivity.

KAP recommends that the government increase transparency around corridor allocation. We want to see a grain monitor track railway allocation against demand, by corridor, and destination on a weekly basis. If a better job is done in tracking where specific commodities are going, all shippers, big and small, and producer car shippers will benefit from increased service and capacity.

Farmers and shippers will benefit greatly from appropriate service levels, and fair corridor allocation. When those conditions are not met, minimum volume requirements become necessary. If the Government of Canada does have to mandate service levels to maintain grain movement, it must be done based on fair corridor allocation to ensure the equitable distribution of service.

Recommendation #7
That future minimum volume requirements be allocated to specific shipping corridors.

Open Running Rights

Open running rights is often discussed by farmers in Manitoba. This option to increase rail freight competition was considered extensively prior to 2000 as a potential option in lieu of a program option like government subsidies or the Crow Rate. Ultimately, the MGRE program was agreed upon as an alternative at the suggestion of both CN and CP. Open running rights potentially offer a means of increasing competition shipper competition within the grain transportation industry. KAP is willing to investigate and consider open running rights as an option to increase competition in Canada's rail freight shipping industry and solve challenges currently being experienced by shippers.

Maximum Grain Revenue Entitlement (MGRE) Program

It is important to note that the MGRE program was originally proposed and designed by the railway companies. The suggestion stemmed from a push for open running rights by Arthur Kroeger, who was hired by the federal government to come up with a proposal on how to improve the movement of prairie grains and reduce cost. The railways argued that running rights would not be possible, and put forth the MGRE program as an alternative. They advised that the MGRE program would grant them a fair and reasonable return on their investments while simulating competitive market conditions.

KAP emphatically supports the MGRE program and deems it essential to farmers for a number of reasons.

- First, it protects against an unreasonable increase in freight costs when economic conditions create opportunities for arbitrary increases in years where commodity prices are high.
- Second, the MGRE program provides stability in freight costs from year to year.
- Third, it guarantees that CN and CP generate sufficient profit from grain movement that should be reinvested in infrastructure.
- Finally, it helps to mitigate the disadvantages that Canadians face with respect to international competition. Specifically, Canadian producers must compete with Australian farmers' significantly shorter distances to port. In Australia, the average distance to port is approximately 250 km, whereas the average in Western Canada is roughly 1400 km. The MGRE program provides all of these benefits while guaranteeing a healthy profit for railways.

Since the MGRE was introduced it has increased from $394,775,887 to $667,128,937 (CN), and from $366,009,437 to $625,273,950 (CP). During that same period, the railway operating costs have decreased substantially, as previously discussed. The volume related composite price index (VRCPI) has allowed CN and CP to increase grain freight rates, but does not include a way to address efficiencies that were originally supposed to be passed on to grain farmers through rationalization.

KAP has two specific recommendation to enhance the MGRE program that will to better simulate a competitive marketplace.

- First, KAP supports an increase in penalties imposed on the railways for exceeding the maximum allowable revenue from 5% to 15% of the amount by which CN or CP exceeds the cap, to be paid to the Western Grains Research Foundation (WGRF).
- Second, we would see a costing review preformed to take into account the efficiencies gained by railways over time.

Recommendation #8

That the CTA Review support the continued application of the MGRE program when considering any legislative or regulatory changes.

Recommendation #9

That the penalty on railways for exceeding the maximum revenue cap be increased threefold from 5% to 15%, and that this money continue to be paid to the WGRF.

Recommendation #10

That a costing review be performed with respect to the railways to take into account the efficiencies they have gained over time so that increases to the MGRE can be kept in check.

Encouraging Competition

The following recommendations are based on the principle that the Government of Canada should actively encourage new market entrants to create a more competitive marketplace. In many instances, KAP knows that this will benefit all stakeholders, including the mainline railway companies by allowing them to focus their activity where their operational efficiency is highest.

Producer Cars

The use of producer cars is a critical marketing and shipping tool for prairie farmers. In the fall of 2014 farmers were receiving $1.00/bushel premium on local basis level using producer cars. In the winter of 2013/14 the producer car savings were about $1.50 - $2.00 / bushel and producer car shippers indicate they could have accommodated double the total movement had car supply been available. This represents a significant economic loss for Manitoba farmers.

Noting that the right to ship producer cars is included in the Canada Grain Act, it is important that the Canada Transportation Act support producer car shippers by creating an environment where farmers who wish to load and ship producer cars are reasonably able to do so and receive adequate service from class 1 railway companies. In addition to being a meaningful shipping alternative, producer car shipping provides a competitive option to conventional grain handling companies, where the market power between grain companies and farmers is also unbalanced.

Producer car shippers, unlike other grain shippers, have no means of recovering added costs incurred due to poor rail service. In all instances where protection is offered to grain shippers, producer car shippers must be included and meaningful provisions put in place that ensure reasonable ongoing access to producer cars as a shipping option for Prairie farmers.

Recommendation #11

Ensure that farmers have a reasonable ability to ship producer cars and receive adequate service from class 1 railway companies, recognizing that this may require unique provisions not provided to larger shippers.

Shortline Railways

In 2010, the Railway Association of Canada (which represents over 50 railways companies) released a document called "Investigating the Social Benefits of Short Line Freight Railways in Canada". The document highlighted the challenges facing shortlines in Canada, including their ability to meet their long term capital requirements, and acknowledged that without certainty, the long term investments in rail infrastructure are very difficult to facilitate. The Class 1 railways have the traffic density required for profitability, but shortlines struggle in this regard.

Shortlines play an important role in the GHTS. They employ thousands of workers nationally, and pay over $30 million annually in property, fuel, capital, and income taxes. They are also able to operate at lower average costs than class 1 operators, mainly due to less restrictive labour agreements. Their key role, for grain transportation is their ability to service low density tracks that would have otherwise been abandoned through rationalization. They provide a significant service for farmers not only through moving grain, but through the maintenance of rural communities and continued rural economic development. Shortlines need to be empowered to do short haul work on CN and CP track that CN and CP cannot do efficiently. This will provide an invaluable service for farmers, shippers, and the communities within which they live and work.

One example that was shared with KAP about broader rural economic challenges created by poor rail service, involves a small manufacturer from southern Manitoba. It built its company facility and loading system around rail transportation, but has had to move supplies and finished product by truck due to unreliable rail service. The manufacturer has asked a local shortline railway in its area to service its facility, but the shortline is unable to do so because it currently is not allowed to solicit traffic along 26 miles of track between its end of the line and the interchange point where service problems originate.

In this instance and others, a shortline railway is able to fill the capacity to service gaps. Shortlines generally have the locomotive capacity to be moving more cars than they do, but are restricted by track ownership. Shortlines in Manitoba argue that they bolster the system and they provide a service to rural communities that has been declining over the years. They provide a check and balance to the system in that they are accountable to producers and are open and willing to discuss their operations and operating capacity.

> Recommendation #12
>
> Support shortline railways to operate trains and solicit traffic in regions underserved by class 1 carriers.

Schedule 2

Manitoba farmers reported a 23.8% increase to 1.3 million soybean acres in 2014 (from 2013), while Saskatchewan reported 300,000 acres, up from 170,000 acres in 2013. Farmers in the Prairies will continue to adapt and grow different crop. As these crops become more significant, KAP recommends that they be treated the same as other major commodities and thus be added to the list of Schedule 2 grains under the CTA. Presently, KAP recommends the additions of chickpeas and soybeans to Schedule 2.

> Recommendation #13
>
> That chickpeas and soybeans be added to the list of Schedule 2 grains under the CTA.