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Western Grain Elevator Association

Submission to Canada Transportation Act Review Panel

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Introduction

Thank you for soliciting the Western Grain Elevator Association's (WGEA's) views on the movement of grain by rail as part of the overall review of the Canada Transportation Act. The WGEA is an association of nine public and private grain businesses operating in Canada, which collectively handle in excess of 90% of western Canada's bulk grain exports. Members represented by the WGEA account for approximately 15% of railway revenues and pay annual total rail freight of approximately 1.4 billion dollars. Our members are listed on the bottom of our letterhead.

Our submission will take a fact based approach to the reasons why reform in the rail industry is necessary to supporting Canada's economic growth and prosperity. We will explain why existing laws and regulations will neither allow Canada to address the transportation challenges, nor meet the economic opportunities of the next decade. We will explain why the rail freight market does not function in a normal commercial manner and why the resulting lack of balanced accountability is the root cause for the service problems being experienced. We will identify how the WGEA believes existing laws and regulations must be adjusted to allow the level of capacity, flexibility and resiliency to support Canada's international competitiveness.

It is important to note that, while all Canadian shippers have common issues, the grain industry is unique for various reasons. There are many different classes and grades of grain and there is very little homogeneity in the product; grain has a high number of shipping points; it is a seasonal business; and grain producers, who are the backbone of the economy on the prairies, are significantly and directly impacted by rail capacity and rail service for their grain.

Investments in Rationalization

In the mid 1990's, in order to bring more efficiency into the transportation system, the railways began closing some inefficient branch lines while others became short lines, and offered incentives to the industry for loading multiple car blocks. Grain companies responded by replacing traditional wood crib elevators with high throughput elevators. By 1999, thousands of elevators became just over 1000 and today there are 342 licensed elevators across the prairies, handling the same or greater volume of grain. Farmers and grain companies (shippers) have invested heavily in the western Canadian grain handling system in the last 25 years.

Grain Production

While grain production is in large part based on the amount of seeded acres, investments in variety research, improvements in agronomic practices, weather and climate change all contribute to increased yield and available production. We note that figure A.2 of the Canada Transportation Act Discussion Paper identifies grain production in each year for the period of time from 2002 to 2013. Table 2 below reproduces that chart (with the inclusion of the estimated 2014 crop volume) and a trend line over all years. The growth rate in grain production for this period is approximately 3.3% per year. For comparative purposes, we have inserted Table 1, which shows the upward trend in grain production for the previous 12 years, which was approximately 1% per year. Grain production varies from year to year, however, based on this comparison, it is clear that we are seeing not only an upward trend in production volumes, but an upward trend that is increasing in magnitude over time.

There are many initiatives underway that will lead to future increases in the production of some of our traditional crops (i.e. wheat and canola) as well as increasing the production of newer entrants to the Canadian prairies such as corn and soybeans, of which corn especially has the potential for higher yields on the same landmass. This is being driven by the increases in the global population and overall increases in global prices for grains, oilseeds and pulse crops.

Advancements in technology for all commodity types is one major factor that will contribute to increased yields. The removal of Kernel Visual Distinguishability (KVD) as a requirement for the registration of a variety has opened the doors for wheat varieties to be registered into a particular class, without having to meet the visual distinguishability test. This was seen by wheat developers as a major hurdle in bringing forth higher yielding varieties. In the past year some very exciting research done in Saskatchewan has led to the sequencing of the wheat genome to be near completion. This ongoing work is a key step toward generating the knowledge needed to unlock higher productivity in wheat and meet global demand.

Earlier this year the Canola Council of Canada announced their new targets for producing 26 million metric tonnes of canola by the year 2025, based on an average yield increase from 34 to 52 bushels per acre. They expect this to be accomplished primarily through genetic advancements, plant establishment improvements, better fertility management, improved management of weeds, diseases and insects, and improved harvest timing and straight cutting practices.

Corn prices are attractive to Canadian farmers, but the relatively short growing season has led to a focus on wheat, canola, barley, oats and a host of niche crops like mustard and lentils. Last year, Monsanto announced that it was going to invest \$100 million in research into corn varieties better suited to northern growing areas. They are focusing on producing corn that matures earlier than current varieties, making it a seeding option for a Western Canada. Factoring in farmers' crop rotations, corn may annually occupy 8 million to 10 million acres of Western Canada by 2025. Likewise, we have seen soybean acres multiple in past years. Corn and soybeans yield at 2 and 3 times as much as current wheat yields.

The longer term trend has demonstrated an average increase of 1.5% to 2.0% per year in overall tonnage produced in Western Canada. All of the above activities have the potential to show more of an exponential increase in the future. Growth rates are in the order of +3.0% when looking at a shorter (10 year) time horizon. This is a very broad topic largely driven by investment levels, however, the investment seems to be occurring, and we believe the informed observer would predict a significant escalation in productivity.

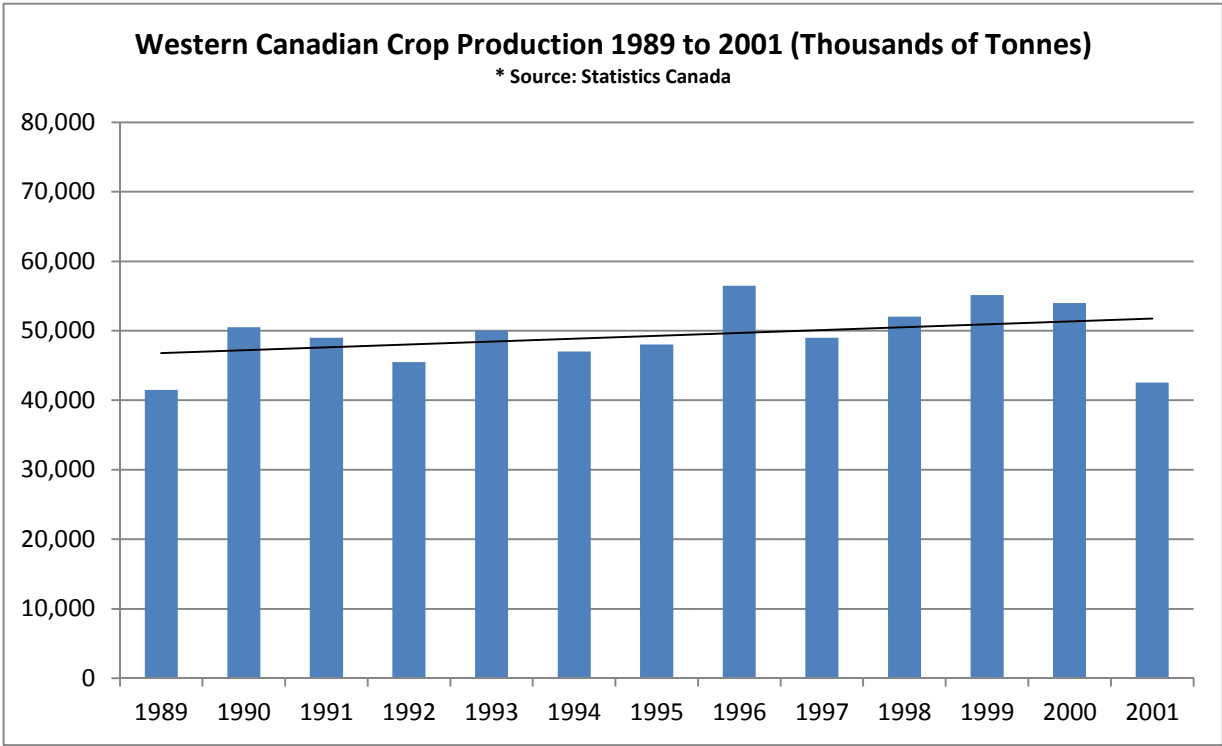


Table 1

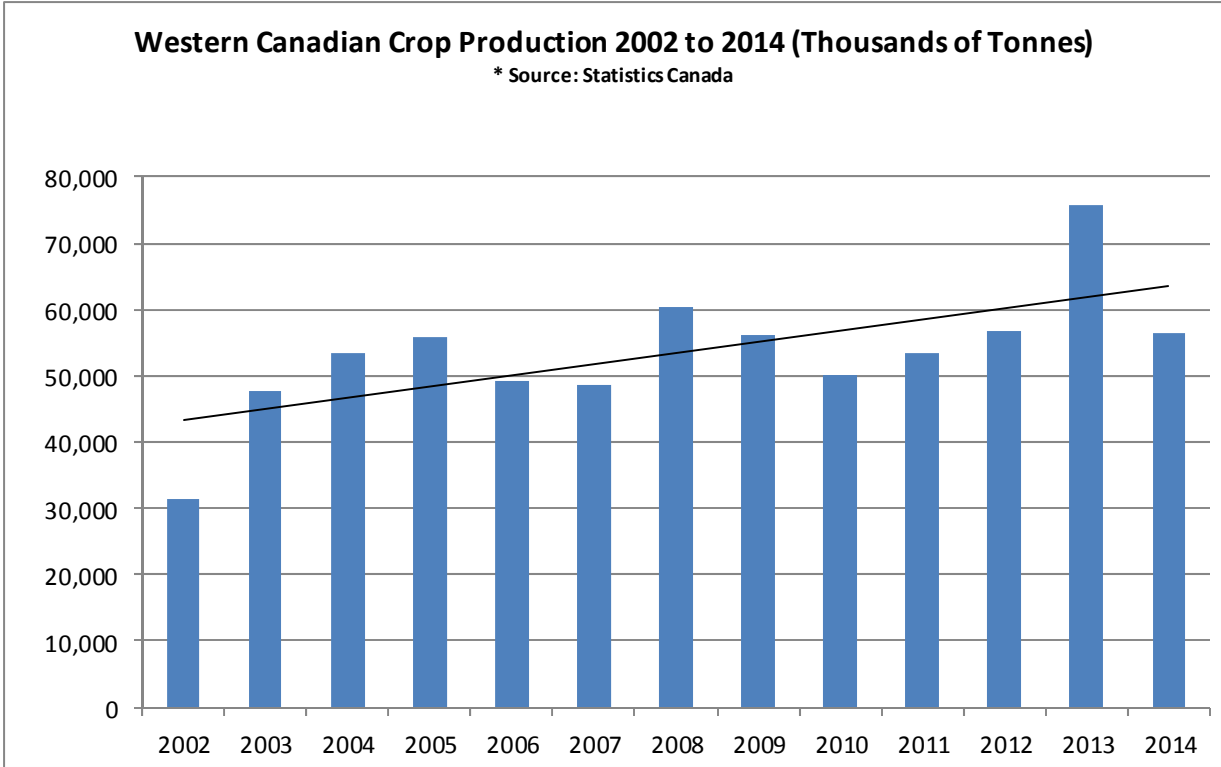


Table 2

Role of WGEA Members in Marketing Canada's Grain

In order to support the growth of the Canadian grain industry, it is important to understand the role that Canadian grain handlers and exporters play in bringing the product to customers. Below is a chart that provides a basic summary of the complete process from production to delivery to the customer.

Crop Production Planning

- Seed development
- Plant nutrient planning
- Agronomic support
- Sale of seed, chemical fertilizer

Crop Progress Monitoring

- Crop evaluation and reports
- Crop estimates

Farmer Marketing

- Cash flow planning
- Risk analysis
- Farmer marketing plans

Sales of Future Production

- Customer interaction to determine demand
- Evaluation of quality requirements
- Futures and foreign exchanges hedges

Freight Booking

- Ocean freight
- Lake freight
- Rail freight
- Truck freight

Terminal Capacity Planning / Booking

- Unload / storage capacity plan
- Cleaning plans
- Loading plans

Primary Elevator Delivery

- Quality control
- Delivery scheduling to meet sales plan

Shipment to Port / Domestic Consumer

- Railcar orders
- ❖ **Railcars spotted (see below)**
- Loading and billing of railcars
- Tracking
- Unload at port

Vessel Loading

- Berthing plan
- Quality management
- Inspection (mandatory and contracted)

Vessel Unloading at Destination

- Management of unload
- Quality control

Follow-up / Customer Service

- Functionality / conformance to requirements
- Begin the process all over again

❖ **Railcars spotted** – This one part of the supply chain can cause the entire business relationship between Canada's producers and customers to fail. Rail capacity is set at optimal levels for railway efficiency, not based on shipper demand.

(top)

The railcar order fulfillment and railcar spotting component is a small, albeit critical, part of the big picture in getting our product to market. All other segments of the supply chain operate on a commercial and market driven basis. Likewise, Canada requires a market driven rail freight system. A commercial system must be, by definition, a relationship where both parties to a business transaction are well-defined and balanced. Market driven means “demand driven.”

Industry Capacity

In the midst of the grain transportation crisis in 2013-14, the WGEA reviewed rail shipping capacity information for western Canada production volumes (Table 3) with the following breakdown:

- Average actual unloads during the peak shipping period of the fall of 2013 (shipping weeks 9 to 13). This is representative of the average number of railcars actually unloaded by each terminal and each corridor for this period of time. It is important to note that these unloads were limited by the cars and service supplied by CN and CPR.
- Maximum railcar capacity that each terminal can unload in a single given week, barring equipment breakdowns or other unplanned operational issues. These numbers do not take into account restrictions in rail capacity and are meant to answer the question – how much can the terminal/corridor handle in ideal operating conditions? Note that there are no actual maximum capacity numbers for domestic shipments or US shipments since these corridors include numerous receivers across Canada and the US.
- Sustainable weekly railcar unload projections. Not every terminal can run at top capacity for the entire shipping season. Staffing issues, equipment breakdowns and other variables come into play. We’ve used 85% of maximum capacity as the number of unloads a terminal facility can unload sustainably, week in and week out. Using only 85% inherently builds in surge capacity of 15% at the terminals that is available for peak periods. Again, the railcar capacity variable is excluded. It is important to note that, as an increment to the sustainable capacity numbers today, companies could add shifts and would invest in future efficiencies if it would help. However, it is difficult to justify capital expenditures for quicker unloading when rail capacity remains flat at best. The supply of additional and more regular delivery of railcars would allow terminals to bring on additional shifts of labour to add unloading capacity.
- Typical / possible programs. For railcar shipping to eastern terminal elevators by direct rail, or for US or domestic Canada-bound shipments, as stated above, there is no real maximum, or it is unknown. For these corridors, we have instead provided what the industry could realistically see as possible shipping programs, again without rail capacity as a restriction.
- Associated weekly tonnage. This column reflects a mathematical application of 90 tonnes per railcar multiplied by the number of railcars from the previous column

(Sustainable weekly railcar unload projections and typical / possible programs).

- Annual tonnage. This column multiplies the weekly tonnage by the number of weeks each port or corridor typically operates in a year. In the case of Vancouver, Prince Rupert, Eastern Canada, US and Domestic, 52 weeks was used. In the case of Thunder Bay, 40 weeks was used, and Churchill is typically open for approximately 13 weeks.

Corridor Capacity, Sustainable Unloads & Correlating Breakdown of Tonnages						
		Average Unloads Shipping Weeks 9-13, 2013	Max Weekly Railcar Capacity	Sustainable Weekly Railcar Unload Projections (85% of Max)	Associated Weekly Tonnage	Annual Tonnage Based on Structural Capacity of Elevator System
Vancouver (52 wks/yr)	Richardson	1031	1500	1275	114,750	5,967,000
	Cascadia	1240	1540	1309	117,810	6,126,120
	Pacific	450	840	714	64,260	3,341,520
	AGT	438	700	595	53,550	2,784,600
	Cargill	774	1000	850	76,500	3,978,000
	VC TOTAL	3933	5580	4743	426,870	22,197,240
Prince Rupert (52 wks/yr)	PR TOTAL	1401	1700	1445	130,050	6,762,600
WEST COAST EXPORT TOTAL		5334	7280	6188	556,920	28,959,840
Thunder Bay (40 wks/yr)	Richardson	600	1100	935	84,150	3,366,000
	Viterra	520	1000	850	76,500	3,060,000
	Cargill	420	700	595	53,550	2,142,000
	Mission	287	400	340	30,600	1,224,000
	TB TOTAL	1827	3200	2720	244,800	9,792,000
Churchill (13 wks/yr)	CHUR. TOTAL	609	740	629	56,610	735,930
				Typical/ Possible Programs		
DIRECT RAIL EAST (52 wks/yr)	ST. L. TOTAL	0	1800	1530	137,700	7,160,400
EASTERN EXPORT TOTAL		2436	5740	4879	439,110	17,688,330
US (52 weeks/year)	US TOTAL	750	No Max	1500	135,000	7,020,000
TOTAL EXPORT		8,520		12,567	1,131,030	53,668,170
CANADIAN DOMESTIC (52 wks/yr)	DOM - TOTAL	750	No Max	1200	108,000	5,616,000
TOTAL RAIL MOVEMENT		9,270		13,767	1,239,030	59,284,170

Table 3

- * Fraser-Surrey Docks and Kinder Morgan not included
- * Domestic Usage Western Canada by Truck not included
- * 2013 Average Actual movement was limited by railway car supply

It is important to point out that the last four columns of this spreadsheet are based on the structural capacity of the handling system and have nothing to do with rail capacity.

This data shows that the loading/unloading capacity in the system far exceeds the railway service capacity contrary to railway statements suggesting that rail service is matched up to handling capacity. Between Canadian export terminals, US customers and domestic Canadian receivers, the system could handle 13800 railcars per week on a sustainable basis, as identified on the bottom line of Table 3.

Grain Logistics

Prior to the removal of the CWB monopoly on wheat and barley exports, grain logistics for these commodities was in the control of the CWB. Country elevators were unable to plan the movement of grain in advance and found it difficult to combine multiple commodities to one movement in order to take advantage of large block incentives (i.e. unit trains) offered by the railways. At port terminals, storage space was often blocked as the plan for loading vessels was most often not revealed to terminal operators until a short time prior to the actual vessel loading. This made the planning space at both country and port facilities difficult.

The logistics of wheat and durum is not planned and controlled by the grain company who has marketed the product, in much the same manner as has been performed for the movement of canola and other products not previously under the control of the CWB single desk. The logistics plan is not tied directly to the sale with all activities (listed on page 4 under “Role of WGEA Members in Marketing Canada’s Grain) coordinated to the sale and its contract conditions.

The result can be seen in a number of areas. When the last seven quarters of performance (the time since the removal of the single desk) is compared to the five year average prior, the following is revealed:

- A decrease in the average time grain is in store in the country network; wheat 8%, durum 20% and canola 9%.
- An increase in the number of large block movements of 5% and an increase in the average block incentive paid of 9% (from an average of \$6.61 to \$7.20 per tonne).
- A decrease in the average time grain is in store at port; wheat 25%, durum 2%, canola 21%.

These improvements are despite the challenges that were faced in the 2013-14 crop year. In other words, with the CWB single desk in place, two grain logistics systems were operating in the same space, often times not in concert. The removal of the CWB single desk has allowed

grain shippers and exporters to manage their entire pipeline for all commodity types. This resulted in efficiency gains that can be measured.

With the recent change to the CWB, grain marketing has changed to become one that could primarily be characterized as a “demand pull” type of system. Producers of cereal grains are able to more directly use market signals to help them make growing, contracting, selling, and delivery decisions. Farmers now have the freedom to make these decisions in a way that gives them the opportunity to earn as much value for the commodity types they produce. In order for producers to fully capitalize on the benefits derived from this freedom, it also must be designed to allow them to execute in accordance with these market signals. The call by some to build more grain storage at port position follows a “supply-push” economic model. Such a model neither allows the industry to provide the right market signals to producers, nor does it allow the industry to maximize the value for their product.

The members of the WGEA strongly believe that the transportation problems that existed in the 2013-14 crop year would have been worse, had these process efficiencies not already been in place.

Reasons for Reform

Over recent years the railways and their shareholders have benefited from a reduction in the number of loading origins and the consequent reduction in operating costs, especially a reduction in the size of the railway car fleet and associated labour and locomotive power. In addition to capturing these shipper efficiencies, the railways and their shareholders, by virtue of a monopoly position, have been able to transfer freight demand risk almost completely through to their shipper customers who have virtually no means to compel supply levels of rail capacity to meet the shape of that demand.

The rail freight market does not operate in a normal commercial manner because of the monopoly setting. Shippers are captive. A grain company situated on a railway line can only ship product on that railway. Rail service is offered under terms that minimize railway costs, not under terms that meet the transportation needs of the grain industry. It is a fundamental of competitive marketplace that any company must build excess capacity to service the needs of a growing marketplace. It is a fact that shippers do not have competitive options and a fact that existing laws and regulations do not hold the railways accountable to carrying surplus capacity. We find that the railways offer less car supply than required to meet the demand of the grain industry. In times of high demand (i.e. October, November & December) this creates an environment of fierce competition for these cars. The railway companies assume that the grain will move eventually and are neither concerned with the negative effect that untimely movement may have on the operations of grain companies and farmers, nor on the economic impact to Canada of missing the peak pricing periods. Railways are a provider of service to customers. They should not be allowed to dictate the fashion in which Canadian shippers and exporters market their products to the world.

In its October 3, 2014 decision in the application by Louis Dreyfus Canada Ltd. against the Canadian National Railway Company, pursuant to section 116 of the *Canada Transportation Act* (Case No. 14-02100), the Canadian Transportation Agency (Agency) agreed;

[12] The Agency recognizes that transportation is a derived demand. Freight railway companies do not operate except to carry goods that are produced by other economic actors and it is the financial health of these primary economic actors that is protected by sections 113 to 115 of the CTA. However, these actors have competing interests. Essentially, the interests of the shipping community are best served by a transportation system with high capacity and intense competition. The interest of the railway companies is embodied in the industry phrase “sweating the assets,” which implies meeting the demand with the lowest possible cost in terms of infrastructure, car supply, crews and motive power. High efficiency operations with low operating ratios (typically measured by costs as a proportion of total revenues from operations) provide the best return to railway company shareholders. However, running a very lean operation has implications for the railway company’s ability to manage surges in demand or operational challenges such as infrastructure outages or adverse weather.

[13] The Agency is of the opinion that where competitive pressures are low or absent and where there is a relatively low cost to the railway company for delaying traffic or otherwise reducing the level of service, the supply of cars and motive power will tend to be set at a level that favours railway company (producer) preferences over shipper (consumer) preferences.

In a normal commercial setting, competition will respond to opportunity. The rail freight market does not function in a normal manner and this is the root cause as to why the railways do not meet these performance requirements by grain shippers. Railways are not operating in an unpredictable manner. They are simply maximizing their returns under the current legislative environment. They cannot be expected to change their behavior until federal transportation law is amended. In the absence of significant and meaningful railway competition to allow the marketplace to facilitate service, the only option is to artificially re-establish balanced accountability through legislation to enforce the level of service that publicly traded monopolies do not naturally provide. This is much different than what has been described as the “re-regulating” of Canadian railway companies.

Lack of Balanced Accountability

If Canada expects to grow exports of potash, coal, oil, forest products, manufactured goods, grain, and an array of other commodities from numerous other industries, then there must be a competitive or regulatory rail environment to require the railways to provide added capacity and better service in a way that makes the railway companies accountable to shippers.

Under the current Canada Transportation Act (CTA), there is a lack of a balance in accountability between a shipper and a railway and little obligation on a railway to provide adequate service. For example, companies are required to load 100 car unit trains within 24

hours to qualify for the reduced unit train rates. In addition, once cars arrive at port position terminal operators must unload cars within 24 hours, or they are subject to rail car demurrage. However, there is no corresponding accountability on the railway side under the CTA for a failure to spot cars and deliver railcars within a specified time. There is no commensurate penalty for a railway if it fails to provide service or fails to live up to its service commitments. The only recourse for shippers is a lengthy, expensive and often ineffective complaint process to the Agency to determine whether or not the railway has met a vague definition of “adequate and suitable accommodation.” In addition, the type of damages the Agency is able to award, following a decision favourable to the shipper, remains unclear but we understand it not to be all-encompassing.

The structure of the grain and railway industries in Canada lends itself to this imbalanced relationship. One of the most obvious ways in which this manifests itself is the general lack of written contracts between shippers and railways that are the norm for all other facets of the grain industry (i.e., producer’s obligation to supply grain and companies’ obligation to accept contracted grain, commercial trucking contracts and vessel freight contracts), and help to define balanced duties and obligations. Essentially, the railways have no need to agree to balanced contractual terms for the provision of service because they operate in a monopolistic environment. Any resulting contract that would emerge in these imbalanced circumstances would obviously favour the carrier. All attempts to negotiate commercial contracts with fair and balanced penalties between rail carriers and shippers have failed.

The railways unilaterally establish tariffs that define the level of performance they require from shippers. They hold the shipper financially accountable for 24 hour loading and unloading, electronic billing and a long array of other railway efficiency priorities. The benefits from these efficiencies have accrued entirely to the railways in the form of lower costs. They have increased the efficiency of their fleets, improved their operating ratios and reduced the size of their fleets. At the same time, car availability for the shipper has fallen, service in peak / high demand times has decreased and shipper costs have increased for staff on weekends to meet car spot requirements to increase the loading speed of elevators.

Shippers do not have a means available to force productivity changes from the railways that help their own business. They must be provided with recourse to offset the onerous one-sided tariffs of the railways. To help illustrate the lack of balance, below are two examples of the differing consequences to shippers and railways that result from poor performance;

Supply and Acceptance of Railcars

Consequence to shipper for not being able to take delivery of ordered railcars:

- **CN Tariff 9000; Item 1200; Page 6 – Not Used Railcars;** “Railcars that cannot be accepted by the loader on the required loading date at the required loading time are subject to asset use fees. Railcars placed, or constructively placed, for the required loading date/required loading time which are not used and are subsequently released as *Not Used, or if* the railcars were placed at your facility and were subsequently pulled as an empty. **\$150** switch fee per railcar. Note: All railcars ordered from CN and not accepted by a loader located on another rail carrier are subject to a **\$250** per railcar fee.

Consequence to CN for failing to supply ordered railcars:

- Nil

Timeliness of Service

Consequence to shipper for not loading/unloading railcars within the prescribed time:

- **CN Tariff 9000; Item 9000; Page 16 – Asset Use at Loading;** “When you must exceed the time we (CN) provide for loading and unloading. **\$100 and \$140** per railcar per day.

Consequence to CN for failing to deliver railcars (at country elevator or destination) at a time set by CN:

- Nil

A demand driven system is the only way to grow the Canadian economy. The foundation of any commercial solution is accountability. Accountability can only be achieved if the performance expectations of both parties to a business transaction are well-defined and balanced. Recourse for non-performance is an essential element of accountability. Recourse must be fast, effective and affordable. The grain industry has not been able to arrive at commercial solutions due to the railways’ unwillingness to be held accountable to the same degree as shippers. Without a legislative backstop that forces railway accountability, meaningful commercial solutions are not possible.

Symptoms of Lack of Accountability

The problems that lead to poor service are systemic. They manifest themselves to shippers in two general categories, described below. Shippers require railway performance in both of these categories.

1. Cars Requested versus Cars Received

Cars requested versus cars received is an issue of the railways not providing sufficient car supply to meet the shipping needs of manufacturers, processors and grain marketers in servicing domestic and export markets. The railways have natural incentive to keep car supply to *their* level of optimal utilization (minimum cost, maximum revenue). With the relative inelastic nature of car supply and the variable nature of demand for railcars (a function of the variable demand and highly competitive environment of world commodity markets) the railways currently pass the risk of car supply onto shippers. Historically, the level of this car supply tended to be at only a portion of the shipper demand given (a) the lack of competitive alternatives available to shippers, (b) the consequential reality that the railways will get the business sooner or later, (c) the accountability the railways have to shareholders to keep costs down and profits up in a system unencumbered by balanced legislation or effective competition, and (d) because they can – there are no effective legal or financial consequences.

The standard of performance for a railway that the CTA provides attempts to establish a definition that is all encompassing:

[s. 113(1) "A railway company shall, according to its powers, in respect of a railway owned or operated by it, (a) furnish, at the point of origin, at the point of junction of the railway with another railway, and at all points of stopping established for that purpose, adequate and suitable accommodation for the receiving and loading of all traffic offered for carriage on the railway; (b) furnish adequate and suitable accommodation for the carriage, unloading and delivering of the traffic; (c) without delay, and with due care and diligence, receive, carry and deliver the traffic;"

"Adequate and suitable accommodation" of traffic is, in principle, a good standard of service definition. In practice however, its historic lack of specificity leads to a very large grey area that necessitates a broad based effort in a Level of Service complaint to define what is adequate and suitable accommodation in the mind of a shipper and in the mind of a railway. The process of "proving" or defending a shipper's point of view in the context of this broad definition costs large amounts of time, money and resources.

In effect, the railways size the fleet to smooth the utilization through the year to suit their cost model and ignore both the market's need for cars and the intent of the CTA clause requiring the railways to provide "*adequate and suitable accommodation*" of traffic. The profit model, the railway monopolistic industry position, and the lack of a clear definition of what *adequate and suitable* actually means in practice, together with the lack of financial disincentives to do otherwise, sends the railways a clear signal on how to manage their business. Any rational business in this advantaged position would operate in the same manner.

2. Railway Service Performance

Railway service performance is an issue of the railways providing a substandard level of performance on delivery of railcars for loading (empty spotting), pick up, setting estimated arrival times and achieving loaded transit reliability. Among the most relevant measures of railway service quality to the WGEA is that of the reliability of the empty car spot plan. Railways establish and communicate a plan in advance to deliver empty cars for loading at grain elevators to fulfill orders. Elevators plan operations according to these plans, buying in grain, arranging timing of deliveries, allocating time for cleaning and processing of grain, and scheduling staff. Grain producers similarly make plans to load and deliver grain to an elevator based upon the logistics plan as communicated to them by the grain companies (i.e. shippers).

Once car supply plans are finalized with a railway, the issue then goes to the execution of that service. Railcar spotting performance (i.e. the delivery of railcars for loading in accordance with the agreed plan) at country elevator sidings is of extreme importance to grain shippers in this review.

A high level of planning and efficiency is required to assemble a unit train. Normally, the elevator will shut off grain receiving from farmers to dedicate the staff to the train. For 100 cars, a grain shipper has approximately 14 minutes to load and reposition each car. Companies need to know the day and time the cars are arriving and subsequently pulled because:

- **Country Elevator Issues;** When the train does not arrive and if the elevator is full, farmer deliveries have to be turned away and rescheduled to a later date, with the danger of congesting future deliveries. The grain company is also faced with added cost for labour, especially on weekends due to overtime costs. The inconsistency of the railway spotting means added work hours, which can place elevator employees at risk of exceeding the maximum hours of work regulations. There are times a company incurs the added costs and rescheduling of farmer deliveries to load a railcar within the 24 hour window, only to see the grain sit on the elevator siding for days before being picked up. This situation infers inefficient use of labour (i.e. overtime) to meet load time parameters that are, in fact, not required by the railway in many circumstances. In addition, failure to pick up cars when released affects estimated time of arrival at destination which impacts port terminal logistics.
- **Port Terminal Issues;** Like a pipeline, if something goes wrong at one end it has a direct effect on what happens at the other. At the terminal, the vessel has arrived but the grain has not. When the trains do arrive, deliveries can be congested, the commodity mix may be out of order, and the terminal is handling the wrong product. “Grain” cannot be viewed as a homogeneous commodity like other bulk shipments. A shipment of Canadian Prairie Spring wheat is as different from Canadian Western Amber Durum as coal is from potash, and with the multiplicity of grades and quality characteristics within the different classes and commodity types, we end up with hundreds of grain products destined for different customers. Additional complexity arises from the fact that grain is sourced from multiple locations and delivered to many destinations. We could easily end up with railcar bunching, railcar demurrage, added labour costs, vessel demurrage, contract extension penalties, product missing loading to a vessel or, worst case scenario, being in default of a contract.

The poor spotting performance has caused inordinate problems in trying to plan the efficient movement of grain from country elevators to export terminals and has resulted in extra costs through additional country elevator staffing to meet loading requirements when cars finally arrive and through increased export terminal costs due to lack of reliability of arrival times of rail cars. Measuring performance as the delivery of empty cars sometime within a given period is not appropriate for the reasons described above. The grain industry needs spotting performance to be measured to the day.

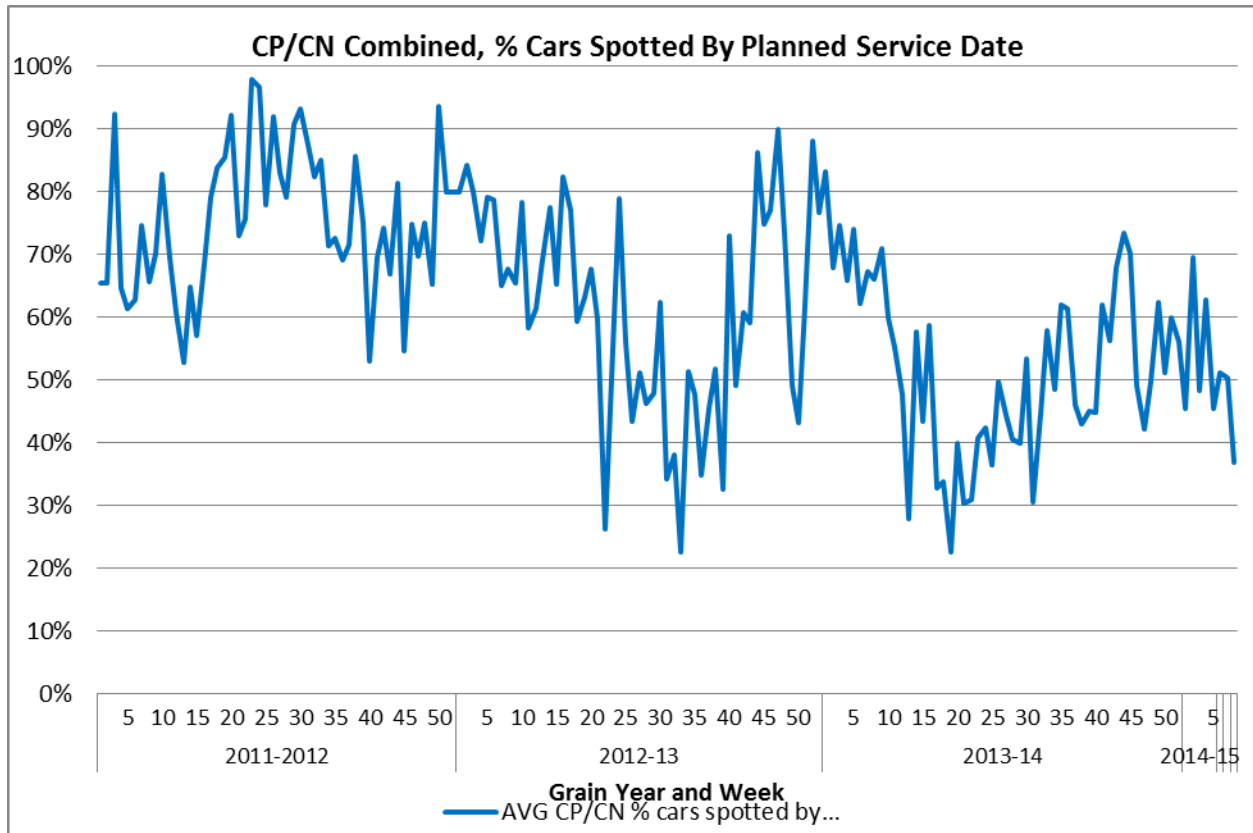


Table 4

Table 4 represents spotting performance by both CN and CP from 2011 to 2014. This data has been collected by grain shippers themselves and is based on a large representative sample of grain movements during this period. To be clear, it does not represent performance relative to demand. It represents performance relative to the car spotting plans the railways themselves issue to shippers which already represent considerable rationing relative to demand. The chart illustrates the very low level of performance and a high variability of performance from week to week. Grain shippers cannot even plan their businesses to account for poor service due to the high level of inconsistency.

Spotting performance in the week ordered, the initial day indicated, car condition and transit times, are all highly variable in execution. The WGEA contends that the railway should be able to spot 100% of cars it has committed to deliver on the day they are supposed to be delivered, failing which they should be required to compensate the shipper. Doing otherwise completely misses the meaning of the word “committed”.

Railway Grain Revenue Entitlement

The members of the Western Grain Elevator Association have explored whether or not a material relationship exists between the Railway Grain Revenue Entitlement (GRE) under section 150 of the CTA, and rail capacity and service for grain shippers.

In understanding if any linkage exists, and more specifically if the railway revenue entitlement has a negative impact on service, we need to first understand how the GRE works. The following is a summary explanation:

- The GRE is an inflationary control mechanism. It ensures that any escalation in the freight rates associated with moving grain is consistent with the rate of inflation.
- It starts with railway revenues on each of CN and CPR in the base year (2000), and is based on revenues the railways generated prior to the GRE being in place. The Canadian Transportation Agency then adjusts the GRE value each year based on the volume of grain hauled, the average distance it is hauled, and inflation. This ensures the railway companies are guaranteed a rate of return that is equal to the base year.
- The inflationary component is indexed based on fuel costs, employment costs, and other factors that were in place in 2000/2001. Any efficiencies generated by the railway companies are captured and retained by the railways themselves. By way of example, the cost of fuel in the GRE is based on a consumption rate of the technology of a locomotive in the year 2000. Today, locomotives use fuel more efficiently. In addition, labour costs are based on the railway labour force in place in the year 2000. Today, both CN and CPR are operating with a much smaller labour force.
- The GRE applies to grain routed for export through Canadian west coast ports, and eastern shipments ending at Armstrong and Thunder Bay. It does not apply to grain originating in Canada and shipped to the United States or Mexico, or east of Thunder Bay. It technically would apply to shipments to Churchill if carried by a prescribed railway company. However, as the carrier currently serving Churchill is not a prescribed railway, this portion of movements to Churchill is not eligible under the GRE.

There are a number of misconceptions about the GRE. Perhaps the most persistent of these centres on the idea that the Grain Revenue Entitlement is a “cap” and a monetary limit on the total revenues the railways can derive from moving grain. The false assumption is that, once this limit has been reached, the railways become naturally predisposed toward moving any commodity other than grain. The assumption is that the GRE dramatically alters the economics of handling grain by rail and removes or reduces the financial means of the railways to properly invest in grain handling and enhance service. This is false.

The GRE does not limit the amount of grain that a railway may handle, nor does it put in place a disincentive for the railway to handle less grain. The GRE formula is, in fact, used to derive the maximum revenue per tonne that can be earned by a railway for the movement of grain in a given crop year. As the volume of grain increases (tonnes), so too does the total revenue earned by the railway company under the GRE. In addition, it does not preclude a railway from pricing differentially – be it in terms of commodity type, equipment, corridor, season, or volume. In fact, the railways do regularly employ differential pricing based on the above factors throughout the year. Any increase in grain volumes results in corresponding increased revenues. The shipping community has invested in efficiencies that have accrued to the railways’ bottom line. Based on these investments, 55-65% of the grain volume currently moves in 100 car unit trains.

There are numerous shippers of other commodities across Canada who have not benefited from the GRE. These shippers have seen their freight rates climb significantly higher and yet continue to report the same service failures as we have in the grain industry. The one exception appears to be certain coal shippers who are serviced directly by both CN and CPR. We understand they experience both lower rates than the grain industry has under the GRE, and better service. We also consider the situation in the United States and our understanding is that rates and service improve the closer the shipper is to the Mississippi River and, therefore, the competition of the US barge shipping system. Perhaps even more telling is to use an example within the grain industry itself: grain shippers do not see better service on shipments originating in Canada that are destined to the United States or Mexico, even though these movements do not fall under the GRE program.

As a result of the above considerations, we have come to the following conclusions about the GRE:

1. Removing the GRE is a risky proposition. There is no evidence to show that shippers would get better service if the GRE were eliminated. In fact, there is existing evidence that poor service and insufficient capacity would remain.
2. If the GRE were removed, the cost to move Canadian grain would certainly increase. A portion of these costs would be passed to producers.
3. An increase in the cost of moving grain would have an effect on Canada's competitiveness internationally.
4. To refer to the Grain Revenue Entitlement as a "revenue cap" is misleading since it does not place an absolute "cap" on railway revenues. The notion that the GRE is an impediment to higher freight rates above the observed rate of inflation is true. The argument that its removal would result in better service is not.

Solutions

With respect to the general supply and allocation of rail cars, many observers of grain rail logistics in Canada conclude that because there is no competition and no commercial market for rail freight in the grain trade, it needs to be controlled by regulation or legislation. The reality is that most primary elevators are captive to one rail service provider and are therefore beholden to the actions of a publicly traded monopolist, and that it is irrational to believe that rail infrastructure would ever be such in Western Canada to allow for anything approaching real competition at these elevators. In the absence of significant and meaningful railway competition to allow the marketplace to drive good service, the best option is to artificially re-establish balanced accountability through legislation/regulation. Commercial solutions are born from a balanced system.

There are two critical pieces to the puzzle of car supply. First, there must be sufficient base of rail service offered in order to meet the ongoing demand that has been communicated in advance by shippers. Secondly, there must be a set of mechanisms by which to ration base car supply among shippers in periods of the year when overall demand exceeds supply.

In considering the overall system for securing car supply, the availability of a base car supply and the way cars are rationed in times of short supply are inextricably linked. Because car rationing deals with the system by which the car supply is divided up when base car supply is insufficient to meet demand, naturally, there can be differing views as to the methodology for making rationing decisions. We envision a process by which a reasonable car rationing methodology can be determined once the first four measures we propose in this paper are in place. For the grain industry, consideration should be given to reviewing these processes in more depth either as part of or in a secondary process to the review. Any review will require participation by grain shippers and railways. Please see the section under the heading “Debit/Credit Model for Railcar Allocation” for additional views on car rationing processes.

It is important to emphasize that car rationing solutions are not intended to replace any of the other proposed solutions from this paper. For the purposes of this submission, we wish to focus on five important elements which we believe would dramatically improve rail service performance; 1) enhancements to the Level of Service provisions to maximize capacity for all industries, 2) provisions related to penalties for failure to perform for both shippers and railways, 3) effective and timely dispute resolution when a matter arises where the parties cannot agree on a solution, 4) proper notification or communication procedures for an event that might have an impact on the service, as well as ongoing monitoring of rail service, and 5) the making of grain transportation and rail service an essential service with respect to potential labour disruptions.

1. Enhancements to Level of Service Provisions to Maximize Capacity for all Industries

Definition of “Adequate and Suitable Accommodation”

The federal government has provided a mechanism in the CTA for shippers and railways to enter into service contracts, or Service Level Agreements (SLA’s). Unfortunately, the SLA provisions do not have the required strength to allow a shipper to arrive at a balanced service contract with a railway. We will expand on this below, however, we must first ensure that systemic solutions are in place to drive toward maximizing the amount of overall capacity, for all shippers of all industries. The WGEA believes that in order to minimize the systemic lack of car order fulfillment relative to demand, we must first make enhancements to the Level of Service provisions of the CTA.

Current rail legislation to a large extent addresses most of the typical concerns around preventing unwanted monopolistic behaviour such as price gouging or collusion. There is however, an effective gap in the legislative and regulatory framework insofar as it has not addressed the overarching question of whether or not the railways are providing an adequate supply of rail service for the grain industry given the structure of its annual demand.

The following excerpts are from the Agency's October 3, 2014 decision in the application by Louis Dreyfus Canada Ltd. against the Canadian National Railway Company, pursuant to section 116 of the *Canada Transportation Act* (Case No. 14-02100);

- [10] Sections 113 to 115 of the CTA are referred to as “common carrier” obligations and they have been designed as a shipper remedy. One of the purposes of the provisions is to enable the Agency to establish the level of service, which, in a normal competitive environment, would be expected to be set naturally by market forces. That is to say, the provisions are intended to ensure that the level of service is not established solely on the basis of a railway company's interests and preferences, especially where railway companies can exercise monopoly power over captive shippers....
- [21] ...the Class 1 railway companies now have sole discretion over the operation of their railways, including the size of the motive power and hopper car fleets, the allocation of cars and assignment of motive power and crews. The means for providing suitable and adequate service lies entirely in the hands of the railway companies.
- [22] ...a railway company's service obligations with respect to shippers are unconditional, subject to a shipper meeting its correlative obligations.
- [25] Further, pursuant to paragraph 113(1)(c) of the CTA, the duty must be undertaken “without delay.” This means that traffic cannot be routinely allowed to build up until the railway company considers it convenient to move.
- [49] It is clear that a railway company's statutory duty to furnish adequate and suitable accommodation for traffic cannot be achieved solely on a reactive basis. Predictability, sustainability and foreseeability are basic requirements for a well-functioning service to individual shippers and for the logistics system overall.
- [51] The statutory level of service obligations placed on a railway company imply that it must make an effort to identify measures in advance of the course of events and to consider necessary arrangements that can address the needs of its customers....These level of service obligations are initiated by a shipper's request for service which, in turn, is to be responded to by the railway company by, when necessary, adding capacity or adjusting frequency or timing, in order to fulfill its obligations.
- [61] The Agency does not consider a railway company's failure to fulfill a service request to be justified when rationing is sustained over long periods, when peak demand periods are prolonged and predictable, or when service shortfalls are a routine aspect of the railway company's operations.
- [71] The Agency recognizes that railway companies are free to make business decisions with respect to asset acquisition and utilization; for instance, by using a smaller car fleet where utilization is optimized, that is “sweating the assets.” However, in light of the level of service obligations set out in sections 113 to 115 of the CTA, a railway company cannot

do so at the expense of service. Business decisions relating to the size of the car fleet must not result in the railway company breaching its level of service obligations.....

[72] To allow a railway company to invoke the limited size of its fleet as a defense for an alleged breach of its level of service obligations would amount to allowing the railway company to refuse to transport traffic, or to hold off providing service until it finds it convenient to do so. This would be contrary to the intent of paragraph 113(1© and subsection 113(2) of the CTA.

[176] The Agency therefore finds that CN has breached its level of service obligations to LDC.

[184]Should CN choose to fulfill its level of service obligations to LDC by reducing the service it provides to other shippers, it may be doing so in violation of sections 113 to 115 of the CTA, with respect to those affected shippers. CN would therefore, on application by an affected shipper, be exposed to the Agency ordering remedies under section 116 of the CTA.

We agree with all of the above statements from the Agency and, in fact, the entire decision for Case No. 14-02100 articulates the perspective the WGEA has been advocating for many years. Unfortunately, earlier decisions by the Agency have created uncertainty and confusion. Furthermore, this decision is still within the time window for a possible appeal by CN and we do not know for certain that it will not be overturned.

In the CTA level of service decision no 488-R-2008, the Agency for the first time attempted to define what *adequate and suitable* meant in practical application. Their award for four of the six complainants required CN to maintain a level of cars requested versus cars supplied at 80%.

The crux of the decision is embodied in paragraph 122 of the decision, which is as follows:

[122] *“The evidence shows that some car orders requested on a weekly basis were confirmed at rates below 60 percent. The Agency finds that this is not a reasonable level of performance and this is consistent with its previous findings. Having determined that 100 percent may be unachievable and 60 percent is unacceptable, the Agency finds that confirmation of at least 80 percent of the cars requested is an acceptable and reasonable level of service standard. Setting a minimum confirmation level of 80 percent will increase the predictability of car confirmations, which will allow shippers to plan their operations accordingly.”*

The WGEA had concerns with the rationale for arriving at the 80% benchmark of minimum confirmation level. It appears to have been arrived at by splitting the difference between the service CN was near providing (60%) and the requirement of shippers (100%). By extension of this logic, if CN was providing service just below 70%, would the decision have resulted in a base level performance established at 85%? It does not seem very reasonable to link the benchmark to how poorly the railway was performing. After all, in the above noted case, CN's poor performance was the entire reason the level of service complaint was initiated in the first place.

Shippers have not been able to secure guaranteed car supply near the 80% level, let alone to meet 100% of their needs. It is difficult to identify another business example where freight supply performance at an 80% level is remotely acceptable. These levels of supply are not acceptable to the WGEA and are not acceptable in other industries such as manufacturing, hydro-electricity or telecommunications. Global competition does not allow a company to work to that low of a standard and survive. Yet this is how the Agency has previously interpreted and applied the shipper protection provisions.

Over the years, the lack of specificity about what it means for a railway to provide “adequate and suitable accommodation” has caused unnecessary controversy. The railway companies’ interpretation has historically differed from that of shippers, and from that embodied in the Agency decision for Case No. 14-02100. The railways furnish traffic and supply service in accordance with their own interpretation and not that of shippers. It is only through an Agency decision from a Level of Service Complaint that we begin to piece together a better understanding of the definition.

There are many deterrents from using the Level of Service provisions such as lack of human resource capacity and financial resources to launch a successful challenge and the extended wait for a decision. However, if the definition were made clear in the legislation, we may avoid the discrepancy in interpretation and the costly complaint processes.

In our view, it should be made clear that the definition of “*adequate and suitable accommodation*” is as interpreted by the Agency in its decision in Case No. 14-02100. The Agency’s interpretation can be captured by making the following amendment;

“115 (2) For the purposes of section 113 and 114, a railway company shall fulfill its service obligations in a manner that meets the rail transportation needs of the shipper.”

Canadian Transportation Agency to have Investigative Powers

As an added measure, the WGEA proposes that the Agency have investigative powers to conduct a Level of Service investigation of its own volition, based on complaints by shippers or observed behaviour, by means of the monitoring provisions discussed in item 4 below. Shippers would retain the right to file Level of Service complaints as they see fit, but there may be circumstances where egregious and systemic service issues would prompt the Agency to use its investigative powers to undertake its own Level of Service process, on behalf of shippers. The authority of the Surface Transportation Board in the United States could be used as a model in this regard.

WGEA members are optimistic that the above amendments to the CTA will, at least in part, put the proper disciplines to enhance the overall rail capacity available for all Canadian shippers, and place Canada in a good position to meet the transportation challenges and opportunities of the next decade in support of Canada’s economic growth.

2. Financial Consequences - Railway Service Performance

The second stream of solutions required by grain shippers would provide a legislative backstop to allow shippers to hold the railway companies accountable to their service plans. To ensure that railway service is, and continues to be, adequate, there must be financial consequences payable by the railways to shippers who have suffered from poor service.

As shippers, we respect the need for railway-established performance standards imposed on shippers for loading and unloading of trains as we understand it has a large commercial impact on the efficiency of the railways and our own businesses. The penalties imposed by railways are, therefore, an extremely effective instrument in ensuring a very high level of performance by shippers to these service standards.

On the other hand, shippers do not have a means available to force the railways to pay reciprocal penalties where they have clearly failed to provide the shipper with reasonable service. This ties in to the central component of the WGEA's long-held position that there needs to be balanced accountability in rail freight service between the railways and shippers. From our perspective, there are several instances that are easily identified where a railway would, in a normal commercial environment, be considered as having failed to perform. For clarity, failure to perform can be narrowed down to two distinct scenarios: 1) once a railway has agreed to provide railcars, penalties should apply if they fail to deliver on time (daily metric for spotting performance must apply), and 2) once the train has been loaded, the railway should be held accountable for arriving at destination within a specific timeframe.

The WGEA is proposing that this be brought about by giving shippers, through legislation/regulations, the right to charge penalties to the railways in instances where the railways have failed to perform, just as the railways currently do against shippers that fail to meet load or unload performance criteria. There are two ways this can be accomplished.

Option #1 - Amendments to Arbitration Provisions for Service Level Agreements to include Financial Consequences for Non-Performance

Shippers are seeking a way to have meaningful commercial negotiations with the railways. The Canadian rail system makes it nearly impossible for even the largest shippers to negotiate service agreements that reflect what would happen in a competitive marketplace. Negotiations are one-sided and service disputes are won by the party that holds the market power, either because the shipper fears retribution or because the carrier can withhold or diminish service and harm the shipper's business.

As described earlier in this submission, the railways have the unilateral ability, through legislation, to set tariffs for non-performance of a shipper. The commensurate ability for a shipper to impose balanced financial consequences in the form of penalties, payable from a railway company to the shipper for non-performance, is absent. Shippers want to be empowered to negotiate balanced commercial contracts, rather than having to rely on government to take extreme measures such as the setting and enforcing of weekly volume thresholds. Instead, the federal government must provide shippers with the tools they require to arrive at reasonable

volumes and service terms for their own operations, and the means to hold railways accountable to these terms, through Service Level Agreements.

In the regulations pursuant to Bill C-30, a detailed definition of what elements constitute “operational terms” was passed into law. This is important, because the scope of an arbitrated SLA is limited to this definition of operational terms. Strictly from an operating perspective, we find the definition of operational terms to be acceptable. However, the practical use of a Service Level Agreements is severely limited if obtaining a remedy for a breach of the SLA requires the shipper to commence proceedings before the Agency, and/or in court, or to rely on the proposed Administrative Monetary Penalties (AMPs) scheme. It is not possible for shippers to undertake costly and lengthy Agency and/or court proceedings for damages resulting from railway service failures each and every time they occur.

The WGEA strongly believes that, in order for the SLA legislation to be truly effective, it must include provisions for reciprocal performance penalties and these must be eligible for arbitration. There are items other than those that are strictly operational in nature that can be in dispute in the process leading to the arrival of an agreement and “financial consequences for poor-performance” is a critical item. The intent behind SLAs is to support the creation of what would otherwise be found in a competitive environment, through legislation and regulation. Therefore the legislation must be amended to include all measures that work in normal commercial contracts between customers and service providers, as eligible for arbitration. In a normally functioning marketplace, performance penalties in contracts between business partners are commonplace and should therefore be included in SLAs and determined by arbitration if they cannot be agreed upon.

Option #2 – Performance Standards as Contractual Obligations

The WGEA is of the view that the above option would require the least invasive set of amendments to the CTA, while allowing the most flexibility for grain shippers to arrive at balanced service contracts, or SLA’s that work for them. However, a more formulaic second solution could be as follows.

The legislation could be amended to require the railways establish a rolling service plan sent out each day to shippers indicating the plan for delivery of empty railcars are country elevators and the associated scheduled load date for each elevator spot for a given period of time. The loading dates indicated on the service plan will form the basis of the performance measurement.

- Measure: Empty cars spotted at the elevator to meet the scheduled load date, with daily penalty for cars spotted late and tiered penalty for advance-booked origin-destination cars:
- Penalty: For cars that are spotted for loading after the scheduled load date specified on the advance plan, the penalties would apply at the same magnitude as the daily loading demurrage charges.

Each railways would then be required to establish and communicate expected times of arrival (ETA) at destination when a load is released by a shipper. These ETAs will form the basis of the performance measurement:

- Measure: Cars arriving at destination within 24 hours of the ETA communicated upon release at origin.
- Penalty: For cars that arrive at destination beyond the required performance measurement, the penalties would apply at the same magnitude as the daily unloading demurrage rate for the first 48 hours, and would escalate in regular time intervals from that point forward.

While our preference would be to have ETA's established on the basis of the original planned spot date, this would be administratively burdensome to track. An increasing rate of demurrage recognizes both the shippers' liability with extended delays in arrival (e.g., potentially stiff vessel demurrage rates), as well as the flexibility that railways would have under our proposed spotting performance regime above, but is easier to implement administratively speaking.

The regulations could then be established to indicate that these performance standards would be a deemed contractual obligation within the railway tariff and would carry the above noted minimum standards of service with the associated penalties for failure to perform, unless otherwise agreed upon by the relevant parties. The ability for the parties to agree upon other arrangements (i.e. to not make the penalties so rigid that shippers do not have the right to waive them) is a critical element to allow for railways and shippers to operate within normal commercial parameters that in many instances could result in reasonable leeway being provided to a business partner. As shippers, we would similarly expect the railways to provide leeway on load or unload penalties where we believe it may be warranted.

Either option above would provide the balanced accountability that grain shippers have sought for decades. It is only with such penalties that the railways, which operate as effective monopolies, will be forced to be accountable to their customers for the service they are obligated to provide.

The WGEA further proposes that the penalties for failure to meet performance standards, as well as any direct or punitive damages assessed by the CTA, would be applied in a manner that they do not offset the reporting of revenues earned under the effective grain revenue entitlement for the respective railway in the fiscal year in which they were applied (i.e. they could not be applied as "costs").

It will be necessary to ensure shipper orders are placed with certainty so that the railways may operate under the correct assumption that orders demanded are "real". To this end, shippers will have to be subject to penalties for car orders placed and then canceled, ensuring integrity in the car order system.

3. Dispute Resolution

Level of Service Complaints are very costly, time consuming and extremely combative. They do not work well for smaller disputes, or disputes that the shipper would describe as non-systemic in nature. There are always individual circumstances that arise where shippers and railways will

disagree on the “rules of the game.” Once again, there are two options for arriving at a fair dispute resolution process, which coincide with the two options identified in the above section.

Option #1 - Amendments to Arbitration Provisions for Service Level Agreements to include Dispute Resolution Process

The current Service Level Agreement legislation does not permit a shipper to ask the arbitrator to include provisions in an SLA to govern the resolution of disputes under an SLA. The inability to secure access to an expeditious and cost effective process to recover from breaches of an arbitrated SLA limits the practical use of an SLA to shippers. Without this option, a shipper may well have to bring a complaint to the Agency for a determination of whether the SLA has been breached. The expense associated with complex proceedings is prohibitive for many shippers.

Accordingly, we propose a modification of 169.31 (1) (b) to include the right to such mechanism.

169.31 (1) If a shipper and a railway company are unable to agree and enter into, a contract under subsection 126(1) respecting the manner in which the railway company must fulfil its service obligations under section 113, the shipper may submit any of the following matters, in writing, to the Agency for arbitration:

(b) the terms that the railway company must comply with if it fails to comply with a term described in paragraph (a); which may include terms governing the determination of whether or not a service failure has occurred and the consequences resulting from such failure, such consequences including but not limited to those that are financial or punitive in nature;

In the simplest of terms, the amendment would allow the arbitrator to establish a fair and reasonable dispute resolution process that would be included within the Service Level Agreement.

Both CN and CP advocate the use of alternative dispute resolution to address disputes with customers, including disputes over whether they have met their service obligations. Both CN and CP offer dispute resolution processes on their websites. However, these CDR processes are weighted in favour of the railways. They provide the illusion of a fair and reasonable dispute resolution process, however, when one seeks to understand their details, they do not provide shippers with any substantial benefits that are not available to them under the current Canada Transportation Act. For example, their proposal would do nothing to address the fundamental lack of accountability or the level of service shortfalls.

There is no reason why a shipper who is also interested in this approach should not be able to ask the appointed arbitrator to set in the terms of an SLA fair and reasonable parameters for dispute resolution between the parties. There is also no reason why that dispute resolution mechanism could not deal with alleged breaches of the SLA and the compensation to be paid in case of breach.

While the courts are perhaps the typical forum in which one seeks damages, there are many instances where legislation provides for arbitration or other non-court process to resolve disputes and where the statutory decision-maker has the power to make monetary awards in the form of damages or compensation. At the federal level, this would include the following:

- Under the *Canadian Human Rights Act*, a member or panel of the Human Rights Tribunal conducting an investigation may order the payment of compensation for expenses and additional costs incurred by a person as a result of a discriminatory practice by another.
- Under the *Canada Labour Code*, an arbitrator appointed to resolve a dispute has the ability to order compensation or damages.
- Arbitration Committees appointed under the *National Energy Board Act* to determine compensation for acquisition of lands for a pipeline also have the power to set compensation for damages suffered as a result of the operations of the pipeline company.
- Under the *Canada Grain Act*, the Grain Commission has the ability to determine compensation payable to a person for loss or damage sustained by that person resulting from a contravention of or failure to comply with any provision of the legislation. This jurisdiction operates independently of the “public” enforcement provisions which make it an offense to contravene the provisions of the Act and provide for prosecution.
- The Board of Arbitration continued under the *Canada Agricultural Products Act* has the power to determine claims for compensation resulting from a failure to comply with the regulations relating to grades, standards or marketing of prescribed agricultural products in import, export or interprovincial trade. Again, this jurisdiction operates independently of summary conviction offences created by the same statute which may attract fines.

The example from the *Canada Labour Code* is particularly apt, since the *Code* also provides a process for the CIRL Board to settle the terms of a first collective agreement where an employer and a union cannot agree on those terms. The Board essentially makes the agreement for the parties. The *Code* requires provisions for the resolution of disputes to be included in the collective agreement, and the CIRL Board presumably complies with this requirement when exercising its jurisdiction to settle the terms of a first collective agreement.

Option #2 - Fast-Tracked Arbitration as Contractual Obligation

Should the concept of including a dispute resolution process as eligible for arbitration into an SLA not be a preferred option of the Panel members, the WGEA would propose that that legislation be amended to provide that every rail car shipment carry an implicit contractual obligation that would allow either the shipper or the railway to resolve a penalty-related dispute (whether a penalty happened to apply or not) by have a mandatory “fast-tracked” arbitration process. The parties would have 7 days to submit written arguments with a clear recommended solution. An arbitrator would be allowed 14 days in which to rule upon the dispute, but the arbitrator would be constrained by having to choose either the shipper’s or the railway’s

recommended solution, insofar as that solution complies with existing regulation or legislation. This would force parties to recommend reasonable outcomes, and ensure timely awards by the arbitrator for minor disputes.

In terms of how the penalties and the arbitration concepts raised in the “solutions” section of this document (both “option 2’s” above) might be brought about, the WGEA believes there is a rather simple means to accomplish this goal. Legislation could be amended to outline that cars must be committed in writing for delivery by a railway to a shipper and that this written confirmation would be *deemed* to include contractual obligations related to both tariffs and service performance standards which would be set out in regulation. Again, the regulations could then be established to indicate that the deemed contractual obligation per the legislation would carry the above noted minimum standards of service with the associated penalties for failure to perform, unless otherwise agreed upon by the relevant parties. The last provision is extremely important, in that it sets out the ability for a shipper and a railway to negotiate alternative arrangements acceptable to both parties. This allows for normal commercial partnerships to be formed and for these business partners to allow for flexibility in their relationship. In addition to the service standards and penalties, the regulations could also provide for the aforementioned fast-tracked arbitration option.

For clarity, the WGEA is still recommending that Level of Service and Final Offer Arbitration procedures be retained (and LOS provisions enhanced as described in point 1 above), and that either railways or shippers could pursue these options even if a commercial arbitrator has already heard a particular case either in part or in whole. Thus, the current barriers to the aforementioned procedures (costly, time-consuming, combative) would be effective deterrents for frivolous “appeals” of the proposed streamlined commercial arbitrations.

4. Improved Monitoring, Measurement and Communication

Rail system logistics performance must be subject to ongoing measurement so that regulators can monitor changes in performance. Unfortunately, the quality, integrity and availability of good data are diminishing, at the very time its importance is increasing. For example, CN has announced changes to their car ordering process, which came into effect in September 2014. In the new process, they have established a limitation on the number of railcar orders from an individual shipper which equates to approximately two weeks’ worth of typical CN supply to the shipper. In other words, a shipper will not be able to place new orders with CN beyond an amount calculated by CN that represents approximately two weeks of service at CN’s established service levels. New orders will not be accepted until old ones have been filled. This has resulted in the elimination of the measurement of CN shortfall. This was the measurement that highlighted the rail issues in 2013-14 that led to the establishment of the volume thresholds.

The WGEA recommends the Agency or another federal department should establish an oversight body that measures performance of the railways and publishes these observations. The existing Grain Monitor could possibly provide some guidance and insight into how a Rail Service Monitor might be organized and operated.

Improved communication between railways and their customers is critical to ensuring trust exists and solutions to problems are found for rail service issues. One way proposed by shippers to improve communication is by increasing transparency in the statistical reporting of rail service performance and equipment availability. The monitor would be responsible to:

- a) Establish measurements for car order fulfillment (compared to targets as to the level of performance the railways should reasonably be expected to provide). Standards for measurement must be simple and rapid.
- b) Collect data from the railways and others in the supply chain (this may require the introduction of adequate regulation to both (i) require this monitoring and (ii) obtain data from the railways to do this monitoring),
- c) Issue periodic public reports (perhaps annually), and
- d) Give advice to the Canada Transportation Agency to launch and undertake investigations on its own initiative, after which the Agency could initiate its own Level of Service Complaint based on its findings. The independent monitoring activity could be formally reviewed every five years.
- e) Do all of the above according to a timeline of days and weeks (versus months of waiting for data, analysis and advice – data well after the fact is not very helpful). Data should be provided on an ongoing basis.

The Monitor would also have the ability to make recommendations on an ongoing basis for improvements to items such as better railway contingency plans and better systems in place to communicate those plans with the railways' customers. In other words, a watchdog is necessary to ensure the railways pay the required attention to the service needs of shippers and receivers at their loading and unloading facilities in conjunction with their ongoing focus on scheduled line-haul operations.

5. Rail Service an Essential Service

From time to time, a work stoppage on either CN or CP threatens to halt or slow the shipping of Canadian commodities. Due to the railways' inability to recover in normal circumstances, we know that a work stoppage of any length of time means lost shipping opportunities that will never be recovered. Invariably, the major shipping industries such as grain, mining, forest products, manufacturing, etc. write the government asking for back to work legislation, lest we do irreparable harm to the Canadian economy and the Canadian reputation as a reliable supplier of product. During the last three railway work stoppages the government acted quickly and had workers back on the job within three days. Likewise, work stoppages occur in other parts of the logistics chain that affects the flow of grain, such as pilots, port authorities, the St. Lawrence Seaway, etc.

The WGEA urges the government to take steps to introduce legislation that prohibits work stoppages for the purposes of rail service for grain movements, by deeming the rail service to be "an essential service." In addition to declaring rail service for all industries as essential, we urge the government to make all segments of the supply chain that moves grain itself to be essential services. There is precedent for such a change. Clause 87.7 of the Canada Labour Code declares that the long-shoring industry shall continue to provide the services they normally provide to ensure the tie-up, let-go and loading of grain vessels at licensed terminal and transfer elevators,

and the movement of the grain vessels in and out of a port.

Debit/Credit Model for Railcar Allocation

The WGEA is reticent to enter a discussion on railcar allocation, since such a system becomes necessary only in times of short car supply, and the railways control the supply of railcars. Since it is the railways which control the supply of railcars in the grain elevator loading cycle, it becomes convenient for the rail companies to deflect the discussion to one that focusses on dividing rail service, rather than expanding the service pie. Our focus, and the focus of the CTA Review Panel, must be to ensure the transportation of grain from the prairies through our strategic transportation corridors can meet the transportation challenges of the next decade in a way that supports Canada's economic growth and prosperity. Entering into a discussion on a better way to "divide the same sized pie" is not the solution.

In its decision October 3, 2014 decision in the application by Louis Dreyfus Canada Ltd. against the Canadian National Railway Company, pursuant to section 116 of the *Canada Transportation Act* (Case No. 14-02100), the Agency agreed;

[23] The CTA is specific about the railway company's duty, which is to provide adequate and suitable accommodation for "all traffic offered for carriage..." That is to say the obligation of a railway company is owed to each individual shipper in respect of whatever traffic is tendered to the railway company by each shipper....

[24] In other words, the compliance of a railway company with its level of service obligations to a shipper must be assessed having regard to that specific shipper's individual requests for rail services, not simply according to the railway company's assessment of the combined requests of all shippers or groups of shippers, or its car allocation or rationing policies or programs.

That being said, we understand that at some point, even with the required amendments to provide Canadian shippers with the capacity, flexibility and resiliency to meet future demands, there will be times where the service pie will have to be apportioned by some mechanism among grain shippers. Today, the railway companies use a system of historic percentages of railcar usage to establish the percentage a company shall receive in the future. Since rail capacity and rail service are the key constraints blocking the Canadian grain industry from maximizing value for the commodities we export, a historical allocation model makes it impossible for a grain company to grow its business.

Instead, the WGEA proposes the following model, which both addresses the "historical allocation" problem, and recognizes the efficiency concerns expressed by the railway companies in the past:

1. An average cycle time for each corridor should be established by the Agency based on all grain shipping in all corridors in the peak shipping period.

2. Average cycle times would need to be made visible to grain shippers, and would have to be updated periodically.
3. Corridors are established on a province and destination basis. For example, average cycle times on shipping from Alberta elevators to Vancouver terminals would constitute one corridor and one average. Then Saskatchewan to Vancouver would be a second corridor, and Manitoba to Vancouver would be a third (BC could be combined with Alberta). Likewise from each province to each of Prince Rupert, the United States, Thunder Bay, Churchill, the St. Lawrence Seaway direct, and Eastern Canada domestic and other domestic. Once average cycle times are established in each of these corridors (30 corridors), then a straight average among corridors would be used to establish an overall average cycle time.
4. Railway capacity provided should be established based on average cycle times in a way that includes both longer and shorter hauls in the calculations.
5. The model being described requires a starting point in terms of a baseline allocation of capacity for each grain shipper. For the purposes of applying changes to an individual shipper's capacity beyond the first crop year, and in the absence of any other methodology, we default to the use of historical allocation percentages, as have been applied by the railway companies to grain company allocation in recent years.
6. A flexible allocation component could then be imposed, in which a grain shipper could choose the corridors in which to focus its sales programs and therefore shipping. If a grain shipper elects to ship into corridors with longer cycle times (i.e. Saskatchewan to the United States) then the shipper relieves the railway of a portion of its obligation on overall capacity. The shipper that chooses to ship in those longer cycle time corridors would be obliged to accommodate that relief. In other words, the reduction in the railway's promised capacity for that particular week, would come off that (or those) shippers who ship in the higher cycle time corridors. Likewise, if a shipper decides to focus shipping in corridors with shorter cycle times (i.e. Manitoba to Thunder Bay), it would increase the railway's capacity for that particular week. The credit for the added volume would go to the allocation of that (those) shipper(s) which selected the shorter cycle time corridors.
7. Changes in allocation percentages would then apply to grain shippers each crop year, based on their historical allocation from the previous year, which would have already been adjusted in accordance with each shipper's selection of corridors in which to require shipping.
8. The benefits of more efficient grain elevator operations of a particular shipper would accrue to that shipper. In other words, the shipper who loads and unloads railcars faster would receive their next train more quickly.
9. Grain shippers alone decide in which corridors they wish to utilize rail capacity.

10. Grain shippers alone decide which origins get priority in the spotting of trains in a particular week.

11. Quorum, the grain monitor, should be consulted on average cycle times.

It is recognized that the above would be a moving, complex formula for the establishment of the railway's obligations on overall volume thresholds, and each shipper's overall credit or debit from what they would have otherwise received, on an ongoing basis. However, the WGEA believes that such a model can be designed to be workable.

The volume thresholds established by the federal government were an emergency solution intended to deal with a crisis situation. However, since they did not include the necessary level of specificity, they resulted in unintended negative consequences. They gave the railways the signal that they had to meet the thresholds above all else, while giving the railway companies complete flexibility to determine how this was to be accomplished. As a result, the railways provided capacity in the corridors that allowed them to obtain quicker turnaround on their assets, which was not always in balance with the corridors that shippers would have established as shipping priorities. The west coast and Thunder Bay received the majority of the capacity while eastern Canada and the United States markets suffered. Soybeans were excluded from the thresholds while canola oil, meal, malt and processed oats were included and effectively reduced the amount of capacity available for bulk grain shipping. Shippers were not provided with the ability to select the locations to which they required the empty trains delivered and their destination corridors on a week to week basis, and the volume thresholds were set well low of the demand by grain shippers. One WGEA member company reported that they were forced to default on a sales contract to the US due to the railways unwillingness to supply railcars to that market, which resulted in the grain company paying over \$1 million in contract default penalties. In short, the volume thresholds did not work well because they were not designed to be market driven. If they were implemented in combination with something similar to the debit/credit model identified above, it may have resulted in less damage to the grain industry.

Conclusion

Lack of adequate rail capacity and service to grain shippers in the 2013-14 crop year has brought forth a high level of attention to the matter of rail service and the imbalance in accountability between a railway company and a shipper. However, the fundamental underlying issues have been present for decades, and the large crop size only amplified the ongoing problems.

In summary we are recommending the following changes be enacted in legislation or regulation whichever is appropriate:

1. Enhancements to Level of Service Provisions to properly define "adequate and suitable accommodation" in the legislation, give the Agency investigative powers, and the ability to launch a Level of Service action of its own volition.

2. Giving shippers through legislation the right to apply financial penalties against the railways in instances where the railways have failed to perform against pre-established criteria, just as the railways currently do against shippers that fail to meet load or unload performance criteria.
3. Having a “fast-tracked” arbitration process for every rail car shipment that would allow either the shipper or the railway to resolve a penalty-related dispute (whether a penalty applied or not). This could be applied through a Service Level Agreement or another explicit contractual obligation.
4. The CTA or other federal department should establish an oversight body that measures performance levels for the railways and publishes the results against actual performance in different regions of the country.
5. Declaring rail service to be “an essential service” in the context of potential labour disruptions.

Canada requires a commercial and market driven rail freight system. Market driven means “demand driven.” A demand driven system is the only way to grow the Canadian economy. The above recommendations all fall under the theme of establishing balanced accountability. The railways should be held accountable to the same level of performance to which they hold shippers. The longer we wait for a re-balancing to address rail service issues, the more significant becomes the erosion of our competitive position in international markets.

Without the regulatory/legislative change that the WGEA is recommending, the Canadian grain industry will continue to suffer from:

- lost grain sales domestically and internationally;
- lost revenue because grain will be sold outside of peak price periods;
- large potential for significant vessel demurrage bills;
- lost confidence in Canada as a reliable supplier; and
- higher costs to farmers.

All of these costs make Canadian grain, oilseed and special crop production less viable. Without material changes to the legislation and increase in railway accountability, there is little that can be done to address service disruptions and almost no way for shippers to hold the railways accountable.

The reality of global exports is that the railways are only one piece in a very long chain. The chain begins with a customer, somewhere else in the world, that has in front of them a wide variety of options in the origins of the goods and services they wish to consume. The chain works back from them to a long array of manufacturers, importers, import terminals, vessels, export facilities, exporters, domestic manufacturers, producers and suppliers. If Canada is able to compete in this global marketplace, then Canada as a whole must be cost competitive and able to deliver at all levels, or another country will. All components in this chain either need competitive options that ensure cost and service effectiveness or regulation that provides it when the marketplace does not. The railways are no exception.

Farmers and grain companies have invested billions into upgrading the system and increasing capacity both in the country and at port terminals, to meet global demand. The grain industry needs its logistics partners, the railways, to undertake similar investments to expand capacity and ensure service is available to meet increasing demand, so the Canadian grain industry may properly capitalize on the economic growth opportunities of the next decade and beyond.