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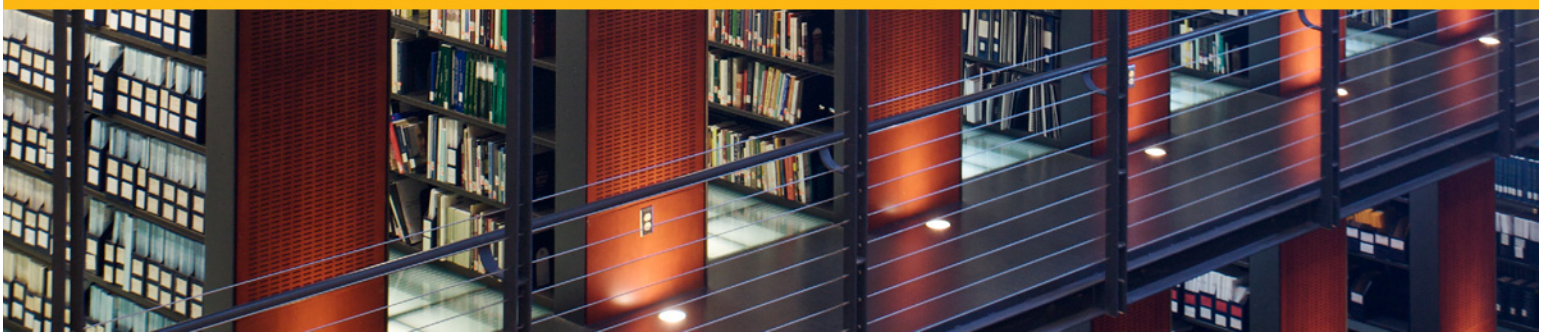

Rail Shipper Protection Under the *Canada Transportation Act*

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(Background Paper)

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RAIL SHIPPER PROTECTION UNDER THE *CANADA TRANSPORTATION ACT*

1 INTRODUCTION*

With important commodity sectors of the economy completely dependent on its enormous capacity to carry their products to market, rail transportation is vital in Canada. Trucking is simply not a competitive alternative to rail transportation for shippers of high-volume, long-haul freight.[1]

Moreover, many rail freight customers are "captive" shippers; that is, only one railway company offers direct service to their area.[2] For these shippers, the rail transportation environment is not naturally competitive and, in the absence of adequate legislative measures, there might be a tendency for the railway company to take advantage of its position as a monopolist in the region.

For more than 100 years, the Canadian government has used regulatory oversight and government intervention to deal with a monopolist railway offering lower levels of service at higher prices than it would under more competitive market conditions.[3] During the last decade, a number of important refinements have been made to the provisions that protect rail shippers in their dealings with federal railways in the *Canada Transportation Act* (the CTA),[4] which came into force in 1996 and contains the economic framework for the federal rail industry.[5] Recent amendments to the CTA have improved shippers' access to competitive remedies – notably through the elimination of the requirement to show substantial commercial harm to their business in order to apply for certain remedies – and have made the railways more accountable for the services they are legally obligated to provide.

This paper begins with an overview of the role of the Canadian Transportation Agency and then outlines the recent evolution of rail shipper protections under the CTA. The paper's conclusion identifies some of the issues currently affecting rail shippers that are likely to be examined during the 2014–2015 statutory review of the CTA, from which a final report is expected to be completed in December 2015.

2 THE CANADIAN TRANSPORTATION AGENCY

There has been some form of independent, economic regulator for the federal transportation system for over a century in Canada.[6] When it came into force in 1996, section 7 of the CTA continued the existing National Transportation Agency as the Canadian Transportation Agency (Agency), which is the current economic regulator for air, rail and marine transportation.[7]

With respect to the rail industry, the Agency is authorized to license rail carriers to operate within federal jurisdiction as well as receive – and make binding decisions concerning – complaints from rail stakeholders.[8] The railways' freight customers can file applications to the Agency respecting problems with transportation rates, levels of service, service charges, and interswitching rates. The Agency also has the mandate

to receive complaints from a variety of other stakeholders, such as individuals, governments, terminal operators and other railways. Stakeholders other than freight customers can raise concerns about the quality and quantity of rail service they receive, accessibility, noise and vibration, level crossings, construction work, line transfer and discontinuance, track sharing and line relocation with the Agency. Depending on the preference of the parties to the dispute, the Agency may facilitate, mediate, or adjudicate a resolution.[9] In certain prescribed circumstances, the Agency may arrange for the matter to be decided by internal or external arbitrators, whose decision the Agency enforces.[10]

3 RAILWAY SERVICE OBLIGATIONS

For more than a century, shippers have had a right to rail service in Canada.[11] Currently, section 113 (Level of Services) of the CTA requires railways to provide "adequate and suitable" accommodation for the receiving, loading, carriage, unloading and delivering of shippers' traffic and to carry it without delay. Sections 118 (Tariffs – Freight) and 121 (Joint Rates) of the CTA compel railways to issue a tariff (i.e., a schedule of rates and charges with terms of service) with respect to the movement of traffic on the railway at a shipper's request.

A shipper can complain to the Agency if the shipper believes that a railway has failed to respect the level of services provision, sometimes referred to as the railway's "common carrier obligation," or if a railway refuses to issue a tariff for a traffic movement upon request by the shipper. According to section 116(4) of the CTA, if the Agency finds that a railway has failed to respect the level of services provision, it may order a railway to carry out work and acquire property or rolling stock in order to fulfil the service obligation. The Agency may also specify the maximum rate the company may charge for doing so. If a shipper is dissatisfied with the rates and conditions for a traffic movement proposed by a railway company and cannot resolve the matter with the railway company, the shipper may request the Agency to arrange for final offer arbitration (FOA). FOA is discussed in section 6 of this paper.

After the CTA came into force in 1996, the Agency received few formal complaints about level of services despite the fact that shippers demand for rail cars was often not met during peak periods. Part of the reason for the absence of complaints was that the level of services required was not well defined, and shippers did not know what they could expect for a given rate.[12] In 2001, the Canada Transportation Act Review Panel (CTA Review Panel) recommended that the level of services provision be replaced by a requirement that a railway state the level of service it would provide in conjunction with its published rates.[13]

The requirement for a shipper to prove that it would suffer "substantial commercial harm" in order to be entitled to relief was likely a greater obstacle for shippers wishing to complain to the Agency about levels of service.[14] The substantial commercial harm test was first introduced into the economic framework for rail with the enactment of the CTA in 1996. Substantial commercial harm was expensive for shippers to prove, making it more difficult to seek remedy from the Agency. In 2001,

the CTA Review Panel recommended that the substantial commercial harm test be repealed.[15]

Legislative changes in 2008, 2013 and 2014 were intended to address the CTA Review Panel's recommendations and make remedies for complaints about services, railway rates and charges more accessible to shippers.

- In 2008, the CTA was amended to:[16]
  - eliminate the requirement (former sections 27(2), 27(3) and 27(5)) that shippers prove that they would suffer "substantial commercial harm" in order to apply to the Agency for relief;
  - add new section 120.1 that allows the Agency, upon written complaint from a shipper, to establish charges for services other than freight movements, such as cleaning and storing rail cars or weighing goods, or the terms and conditions of the movement, if the existing rates apply to more than one shipper and are found to be unreasonable; and
  - increase by 10 days the amount of notice a railway company must provide shippers before increasing a rate for a freight movement (section 119.1).
- In 2013, the CTA was amended to oblige railway companies to enter into a confidential service contract with a shipper at a shipper's request stating the level of service to be provided.[17] Pursuant to new sections 169.31 to 169.43 of the CTA, a shipper who has attempted to come to an agreement with the railway but is not satisfied with the railway's contract offer can request arbitration on the matter. New section 177(1.1) of the CTA authorizes the Agency to make regulations to enforce the arbitrator's decision and apply administrative monetary penalties for violations.
- In 2014, the addition of new section 116(4)(*c.1*) increased railway accountability for its service agreements by empowering the Agency to order a railway company to compensate a shipper when the railway does not meet its level of service obligations. As well, new section 169.31(1.1) was added to the CTA allowing the Agency to make regulations specifying what constitutes operational terms (e.g., the quantity of cars and the delivery route used) within confidential contracts between shippers and railway companies that may be subject to arbitration.[18]

4 INTERSWITCHING

Interswitching, whereby a rail carrier transfers freight traffic to another rail carrier at the request of a shipper, a municipality or another interested person, has been available to shippers for over 100 years. Interswitching is covered in sections 127 and 128 of the CTA and is generally available to shippers located within 30 km of an interchange with another railway regardless of the level and type of competition in their area. The Agency regularly sets rates to be applied on hauls to interswitching points or prescribes the manner in which the rate is to be calculated. Section 127(2) of the CTA states that the Agency "may order the railway companies to provide reasonable facilities for the convenient interswitching of traffic."

Interswitching for distances greater than 30 km may be permitted if it is the Agency's opinion that the point of origin or destination is "reasonably close" to the interchange

(section 127(4)). Following the amendments to the CTA in 2008, a successful application for "extended interswitching" no longer required the shipper to satisfy a substantial commercial harm test.

New section 128(1.1) of the CTA, which was added in 2014, allows the Agency to prescribe different interswitching distances for specific regions or goods in regulations. Pursuant to these new regulatory authorities, the Agency increased the interswitching limits in Manitoba, Saskatchewan and Alberta to 160 km.[19]

5 COMPETITIVE LINE RATES

Legislative provisions for competitive line rates (CLRs), which apply to freight moved by one railway to the nearest interchange with a connecting railway, have been available to rail shippers since 1987. CLR provisions are currently contained in sections 129–136 of the CTA and allow a shipper to request a CLR from a railway if the shipper:

- is located outside the interswitching limits; and
- has access to only one railway company at the origin or destination of the haul, and a continuous route is operated by two or more carriers.

Before requesting a CLR, a shipper must have an agreement in place with the connecting railway for the balance of the movement. A CLR is not available to shippers for:

- movements of containers, trailers on flat cars or less than carload traffic (i.e., multiple shippers per rail car), unless they are being shipped to or from a marine port in Canada; and
- movements where the CLR distance is greater than 50% of the total haul, or exceeds 1,200 km, unless the Agency approves the application specifically.

If the railway company and the shipper do not agree on a CLR, the shipper may apply to the Agency to set one.

The Agency has not received an application for a CLR since the CTA came into force in 1996.[20] The CTA Review Panel recommended in 2001 that the CLR provision be replaced with a more accessible "competitive connection rate (CCR)" provision, notably one without the substantial commercial harm test and for which the shipper does not require an agreement with a connecting carrier to be eligible.[21] Amendments to the CTA in 2008 retained the CLR provisions but eliminated the requirement for the shipper to satisfy a substantial commercial harm test. A shipper still requires an agreement with a connecting railway to be eligible for a CLR, which continues to be a barrier to applying for one.[22]

6 FINAL OFFER ARBITRATION

FOA provisions have been available to shippers with complaints about rail services or rates in Canada since 1987.[23] From 1996 to 2000, sections 159 to 169 of the CTA allowed shippers without alternative, effective, adequate and competitive means of transporting goods to submit a matter involving freight charges to FOA if negotiations with a railway company were unsuccessful. Since 2000, section 164.1 of the CTA has enabled a simplified process under which all disputes over matters involving charges worth $750,000 or less can be submitted to FOA, even if there are alternative, effective, adequate and competitive means of transporting goods. Under both processes, the railway and the shipper provide their respective final offers to the arbitrator (or panel of arbitrators) for a decision on which offer the railway and the shipper must accept.

Pursuing FOA comes at considerable expense (in the order of $1 million between the two parties) as well as the risk that the other party's offer will be chosen by the arbitrator.[24] The CTA Review Panel found in 2001 that the FOA provisions under the CTA provide enough incentives to parties to reach a commercial settlement where possible. The CTA Review Panel recommended, however, that the simplified FOA process for disputes involving charges of $750,000 or less be available only to shippers without alternative, effective, adequate and competitive means of transporting goods.[25] Although this recommendation was not implemented, the high cost of FOA would prevent all but captive shippers from seeking recourse in this manner.

In 2008, amendments to the CTA provided a more economical option for some railway shippers dissatisfied with the rate for, or conditions of, the movement of goods after trying unsuccessfully to reach an agreement with the railway. Sections 169.2 and 169.3 were added to permit groups of shippers to apply for FOA on matters relating to rates or conditions for the movement of goods that are common to all. Allowing groups of shippers to apply for FOA both reduces the costs to individual shippers and increases their leverage in negotiating with the railways.[26]

7 MEDIATION

Compared with adjudication and arbitration, mediation can be a faster and cheaper way for parties to settle a matter and can help them foster a better relationship going forward. In 2001, the CTA Review Panel noted that the *National Transportation Act* that was in force before 1996 provided a framework for mediation to resolve disputes and, at the time of the review, the Agency offered mediation as a pilot program.[27] In its final report, the CTA Review Panel recommended that the Agency be given the statutory authority to offer mediation services to resolve disputes.[28]

In 2007, new sections 36.1 and 36.2 were added to the CTA to create a mediation process for federal transportation matters.[29] The new sections permit the Agency to lead mediation on railway or other transportation issues at the request of the parties to a dispute. Section 36.1 allows the Agency to mediate matters within its jurisdiction, and 36.2 extends the Agency's mediation authority to many other railway matters covered by the CTA, such as arbitration, rates and charges, if requested to do so by

all parties. An agreement resulting from the mediation process is enforceable as if it were an order of the Agency.

In 2008, the CTA was amended to provide mediation as an option to parties involved in FOA. New section 169.2 allows for the suspension of the FOA process in order to refer the matter to an Agency mediator with the consent of all parties.

8 GRAIN SHIPPER PROTECTIONS

Rail freight rates for grain were highly regulated in Canada between 1897 and 2000. From 1897 to 1983, the *Crow's Nest Pass Agreement* and then the *Crow's Nest Pass Act* were the basis for subsidies to railway companies and fixed freight rates for many household and agricultural products, notably grain.[30] In 1983, the *Western Grain Transportation Act* replaced the *Crow's Nest Pass Act*, establishing a subsidy scheme for rail shipments of grain and allowing the government to set freight rates that were meant to be compensatory for the railway companies.[31] The *Western Grain Transportation Act* was repealed in 1995, and in 1996 the CTA provided maximum rate scales for the movement of grain, excluding charges for related services.[32]

8.1 MAXIMUM GRAIN REVENUE ENTITLEMENT

After a statutory review of the grain transportation legislation in 1999, the maximum rate scales for grain in the CTA were repealed in 2000, and section 151 was amended to limit only the aggregate amount of revenue that railways can earn from the transportation of grain. The railways are free to set rates for moving western grain as long as their annual grain revenues do not exceed a maximum entitlement, which is set by the Agency each year. The Agency monitors compliance with the cap and, when grain revenue exceeds the maximum entitlement, specifies the amount of revenue that must be paid back to shippers and any penalty that may be levied.

Some grain shippers allege that the grain revenue cap has not protected them from railways exercising market power. Shippers told the CTA Review Panel in 2000 that the railways had created an array of ancillary service charges outside the cap to increase their revenues from the carriage of grain.[33] In 2001, the CTA Review Panel recommended that the grain handling and transportation system become more commercial in nature and that the revenue cap be repealed.[34]

Although the grain revenue cap still exists, the addition of new section 120.1 to the CTA in 2008 allows all shippers to complain to the Agency about charges (but not rates), and the associated terms and conditions, for the movement of traffic or for the provision of incidental services in a tariff that applies to more than one shipper. If the Agency finds that the charges, or the associated terms and conditions, are unreasonable, it may order the railway to establish new charges, terms or conditions for the service that would be applied to all shippers.[35]

8.2 TRAFFIC OF GRAIN

In 2014, the CTA was amended to help overcome capacity challenges in the rail system and support the faster transportation of grain shipments to market.[36] New section 116.2 of the CTA establishes a minimum tonnage of grain per week to be moved by the Canadian National Railway Company and the Canadian Pacific Railway Company during the crop year ending August 2014. This new section also allows the Agency to provide advice to the Minister of Transport regarding the minimum monthly volume for subsequent crop years. Furthermore, new section 177(3) was added to the CTA, stating that the maximum fine for violating the requirements with respect to minimum weekly grain movements was $100,000 per violation.

8.3 INTERSWITCHING

The interswitching limits were extended to 160 km for rail shippers in Manitoba, Saskatchewan and Alberta, pursuant to new regulatory authorities provided under section 128(1) of the CTA in 2014.[37] The new interswitching limits in these provinces made the market for rail services more competitive by providing many farmers, as well as other shippers, with regulated access to more than one railway company.[38]

8.4 OTHER

In 2008, the CTA was amended to give grain producers more control over rail sidings used to load rail cars. Since then, section 150.1 of the CTA has required railway companies to maintain and publish a list of available sidings on their websites and to not remove a siding without providing 60 days' notice of the intention to do so.

9 RUNNING RIGHTS

There has been a legislative basis for running rights in Canada since the *Railway Act* of 1888.[39] Running rights, if awarded, permit one railway company to make use of another railway company's assets (e.g., land, terminals, track, etc.).

Initially, running rights provisions were intended to prevent multiple competing railways from building parallel track in populated areas. After the railway industry evolved into one dominated by two large players, running rights provisions have facilitated a railway company gaining competitive access to the track of another railway company. Although the CTA permits the Agency to grant running rights under certain circumstances, which are described below, railway companies generally seek running rights through a commercial agreement with another railway.

The current running rights are set out in sections 138 and 139 of the CTA and permit any railway company to apply to the Agency for the right to:

- take possession of, use or occupy any land belonging to another railway company;
- use the whole or any portion of the right-of-way, tracks, terminals, stations or station grounds of any other railway company; and

- run and operate its trains over and on any portion of the railway of any other railway company.

The request may originate from the railway company, a municipal council or any other interested party.

To rule in favour of running rights, the Agency must find them to be in the public interest.[40] If the Agency grants running rights to a guest railway, the railways have an opportunity to negotiate a rate. If they cannot agree on a rate, the Agency may set one.

In 2000, the CTA Review Panel heard that the running rights provisions do little to promote competition in the railway industry. The CTA Review Panel observed that applications to the Agency for running rights have been few and not successful. The public interest criteria and the requirement to be a federal railway (i.e., not under provincial jurisdiction) were viewed as the chief obstacles in the few cases brought to the Agency. Furthermore, stakeholders considered that the right of a guest railway to compete for traffic (traffic solicitation rights) on the host railway's line would be essential if the intent of the provision is to introduce competition in the rail freight market. However, when faced with its first application for running rights with traffic solicitation rights for the guest railway in 2000, the Agency ruled against it. In its decision, the Agency stated that its interpretation of the running rights provision in the CTA was that it was intended to be limited to operating trains, rather than broadly interpreted to include traffic solicitation rights.[41]

In spite of the CTA Review Panel's 2001 recommendations to amend the CTA to clarify that traffic rights may be awarded under the running rights provisions and that provincially regulated railways could apply, Transport Canada has proposed no amendments to the running rights provisions.[42] In 2003, Transport Canada published a policy paper in which it explained that introducing running rights with traffic solicitation was not justifiable, given the evidence that the Canadian rail industry was substantially competitive overall and the expectation that the regulatory costs and adverse impact on system efficiency would be substantial.[43]

10 CONCLUSION

In recognition that quantity and price of rail services available to Canadian shippers can affect the overall economy, federal legislators have always regulated and overseen the rail industry to help ensure that the market is as competitive as possible.

The CTA contains the economic framework for the rail industry and has been amended several times since 2000 to make it easier for shippers to receive better service from the railways and to ensure that rates and charges are fair and reasonable. Recent amendments to the CTA have created more opportunities for shippers and railways to settle matters through commercial negotiation as well as through Agency-led dispute resolution processes.

The last statutory review of the CTA in 2001 provided context for many of the amendments to rail shipper protections in the past decade. The 2014–2015 statutory

review is set to be completed by the end of 2015 and may guide legislative changes affecting rail shippers in 2016 and beyond.

The Review Secretariat noted in its 2014 Discussion Paper that reliability and adaptability are crucial to the competitiveness of the Canadian transportation system and of Canadian exporters.[44] The current CTA Review is expected to result in recommendations for making the rail system more responsive to traffic surges and disruptions, thereby enhancing the reputations of Canada's transportation system and export shippers in overseas markets.

NOTES

* This publication supersedes a paper with the same title prepared by the author in 2007.

1. House of Commons, Standing Committee on Transport, Infrastructure and Communities, *Evidence*, 2nd Session, 41st Parliament, 30 October 2014, 1215 (David Bradley, President and Chief Executive Officer, Canadian Trucking Alliance).

2. The Canadian Transportation Agency defines a captive shipper as one with a single choice of railway. See "Interswitching rates," *Accounting, rates and cost determinations*.

   Although there are nearly 30 federally regulated freight railways in Canada, two railways (Canadian National Railway and Canadian Pacific Railway) serve the vast majority of the market. The smaller federal railways are dependent on business from the two large freight railways. Most small railways with intra-provincial operations are under provincial jurisdiction. (Canadian Transportation Agency, "Federal railway companies," *Rail*.)

3. According to *An Act respecting Railways*, R.S.C. 1906, c. 37, the provision imposing an obligation to provide adequate and suitable services on railways (section 284) and the provision establishing the Board of Railway Commissioners to control rates and services (section 10) were introduced in 1903 (3 E. VII, c. 58, s. 8).

4. *Canada Transportation Act* [CTA], S.C. 1996, c. 10.

5. Hereafter, unless otherwise indicated, the term "railway" in this paper means a railway operating within federal jurisdiction.

6. The Board of Railway Commissioners for Canada (1904) was succeeded by the Board of Transport Commissioners (1938), the Canadian Transport Commission (1967), and the National Transportation Agency (1987). (Canadian Transportation Agency, "100 Years at the Heart of Transportation – An Historical Perspective," *Publications*.)

7. Canadian Transportation Agency, "Our organization and role," *About us*.

8. Canadian Transportation Agency, "Rail complaints," *Complaints and disputes*.

9. Canadian Transportation Agency, "Overview: How disputes are decided," *Dispute services*.

10. Canadian Transportation Agency, "Arbitration," *Dispute services*.

11. Section 284 of *An Act respecting Railways* imposed on railways an obligation to provide adequate and suitable services.

12. Canada Transportation Act Review Panel [CTA Review Panel], *Vision and Balance*, 2001, p. 62.

13. Ibid., Recommendation 5.1, p. 63.

14. Ibid., p. 36.

15. Ibid., Recommendation 5.6, p. 70.
16. *An Act to amend the Canada Transportation Act (railway transportation)*, S.C. 2008, c. 5.
17. *Fair Rail Freight Service Act*, S.C. 2013, c.31.
18. *Fair Rail for Grain Farmers Act*, S.C. 2014, c. 8; *Regulations on Operational Terms for Rail Level of Services Arbitration*, SOR/2014-192.
19. *Railway Interswitching Regulations*, SOR/88-41.
20. According to the Agency's searchable "Decisions" database, the last application for a competitive line rate [CLR] was in 1991. The CLR provisions that existed in the *National Transportation Act* (1987) differ from those in the CTA since 1996.
21. CTA Review Panel, Recommendation 5.5, p. 69.
22. Ibid., p. 34.
23. *National Transportation Act, 1987*, S.C. 1987, c. 34, ss. 48–57.
24. CTA Review Panel, p. 72.
25. Ibid., Recommendation 5.8, p. 72.
26. David Johansen, *Legislative Summary of Bill C-8: An Act to amend the Canada Transportation Act (railway transportation)*, Publication no. LS-569E, Parliamentary Information and Research Service, Library of Parliament, Ottawa, 27 June 2008.
27. *National Transportation Act, 1987*, S.C. 1987, c. 34, s. 46.
28. CTA Review Panel, Recommendation 19.3, p. 300.
29. David Johansen and Allison Padova, *Legislative Summary of Bill C-11: Transportation Amendment Act*, Publication no. LS-527E, Parliamentary Information and Research Service, Library of Parliament, Ottawa, 27 September 2007.
30. *An Act to authorize a Subsidy for a Railway through the Crow's Nest Pass*, S.C. 1897, c. 5.
31. *Western Grain Transportation Act*, S.C. 1983, c. 168.
32. *Canada Transportation Act* [CTA], S.C. 1996, c. 10, s. 150.
33. CTA Review Panel, p. 73.
34. Ibid., Recommendation 5.9, p. 73.
35. Section 120.1(7) of the CTA clarifies that this provision does not apply to "rates" for the movement of traffic.
36. Frédéric Forge and Alexandre Lavoie, *Legislative Summary of Bill C-30: An Act to amend the Canada Grain Act and the Canada Transportation Act and to provide for other measures*, Publication no. 41-2-C30-E, Parliamentary Information and Research Service, Library of Parliament, Ottawa, 1 April 2014.
37. Railway Interswitching Regulations, SOR/88-41.
38. House of Commons, *Debates*, 2nd Session, 41st Parliament, 28 March 2014, 1215 (Pierre Lemieux, Parliamentary Secretary to the Minister of Agriculture).
39. CTA Review Panel, p. 73.
40. Although the term "public interest" is not defined in the federal transportation legislation, it is expected to be consistent with the National Transportation Policy, which appears in section 5 of the CTA.
41. Canadian Transportation Agency, Decision No. 213-R-2001, May 2001.

42. CTA Review Panel, Recommendations 5.10 and 5.11, p. 76.

43. Transport Canada, *Straight Ahead – A Vision for Transportation in Canada*, Ottawa, 2003, pp. 31–32.

44. Government of Canada, "Discussion Paper," *Canada Transportation Act Review*, 2014.