

Submission to Canada Transportation Act Review Panel

Competitive Rail Access
A System Approach
Transport Canada Annual Report

Brotherhood of Maintenance Way Employees

October 23, 2000

Executive Summary

The Brotherhood of Maintenance Way Employees represents over 7600 Canadian men and women who maintain and repair railway tracks and bridges. We have done our share to improve the productivity of the Canadian railway system which has the lowest rail freight revenue per tonne-kilometre in the world. Freight workload per rail employee has doubled in the past decade.

Some groups and provinces pushing for open rail access implicitly assume that open access can be introduced within a closed Canadian border. But Canada is part of a continental market. Such a domestic policy would discourage investment in the Canadian rail infrastructure. It would also allow U.S. based railways to siphon off traffic from Canadian lines while Canadian based railways would lack reciprocal access to traffic on U.S. railroads.

Promoters of open rail access believe that any short-term reduction in rail rates will flow through grain companies to farmers under the implicit assumption that grain companies operate in pure competition. While grain freight rates declined five per cent between 1987 and 1999, elevator charges increased 52 per cent. What happened to the savings from elevator closures?

Omnitrax is proposing to use open access to operate a regional railway service on the prairies. The Federal Government partly implemented this proposal in legislation affecting branch lines last June. Now there are proposals to provide short lines with greater access to main line rail tracks.

A regional rail system focused on railways alone will fail. There is no future for branch lines without a companion grain handling and marketing system to bring grain to the branch lines.

Our union has been working with farmers and communities to develop an integrated regional grain collection system in order to lower total costs by making better use of existing elevator, road and rail infrastructure in an intermodal system. By dealing with branch lines, grain collection and grain marketing in a *system approach*, it can secure a supply of grain for the branch lines.

The annual reporting requirements under the Act should be expanded to include life cycle road costs and subsidies, allocation of highway costs to heavy trucks, and a full-cost accounting for different modes of transport.

Introduction

The Brotherhood of Maintenance Way Employees represents over 7600 Canadian men and women who maintain and repair railway tracks and bridges. We have done our share to improve the productivity of the Canadian railway system which has the lowest rail freight revenue per tonne-kilometre in the world.

In 1999 compared to 1990, the Canadian railways hauled 29 per cent more freight with 35 per cent fewer employees. Freight workload per employee has doubled. This has cost 23,000 railway jobs.¹

Our union has commissioned a number of research studies into transportation restructuring. It has been working with farmers and communities on solutions that increase benefits for people.

Role of Labour

According to Transport Canada, between 1986 and 1997, productivity on Canadian railways improved four per cent per year, double that of trucking at 1.9 per cent per year. A recent report by the Conference Board of Canada concludes that future improvements in railway productivity will not be found in further cutbacks or downsizing. They will come from investments in new equipment and information technology.

The proposed open access system instead will discourage the needed investment and will lead to more lay-offs and a shrinking traffic base to support the overhead costs of the east west Canadian rail lines and ports. Investment and maintenance will be deferred on the Canadian east west system. Jobs and investment will instead flow into the U.S. system.

Lack of investment was the very reason why the Federal Government purchased hopper cars and began paying subsidies to the railways for grain movement in 1983. The Government terminated the subsidy in 1995. Are we going in a policy circle? Is the intention of the Government to resubsidize the railways when the infrastructure starts to deteriorate under open access?

¹ Railway Association of Canada, Railway Trends 2000, September, 2000, p.6

Any resulting loss of traffic to the U.S. system would affect rail labour in Canada. Railways have already been restructured as a result of rail deregulation in 1987, but open access could introduce competition from non-union operators and affect the relationship between the infrastructure and operating components of the railway.

Short lines have lower wage or salary costs than CNR or CPR because they use non-union labour. This would be offset by the new expense they would incur in hostelling, supporting and pooling operating crews along the main line railway. A large short line operator might be able to provide service under contract to a grain or potash company that could offer large volumes at a few origin-destination pairs.

Current and Emerging Trends in the Grain Industry

The commodity groups and provinces pushing for open rail access implicitly assume that:

- *Canadian legislators can drive changes in efficiency and pricing of the Canadian grain handling and transportation system by domestic legislation for open access within a closed border*
- *Canadian railways can extract monopoly prices, but grain companies are purely competitive. Therefore, measures to reduce railway prices via open access will flow through grain companies to farmers.*

There is reason to examine these assumptions in light of current and emerging trends in grain and transportation markets under NAFTA and globalization:

Assumption parameters of solution are domestic

- Open access in Canada would allow the U.S. based grain companies and railroads to haul Canadian grain through the U.S. without contributing to the overhead costs of the Canadian system. Transnational grain companies are expanding their activities in Canada by building inland terminals, setting up joint ventures with Canadian grain companies such as Saskatchewan Wheat Pool and by taking over Canadian cooperatives such as United Grain Growers. These companies have the financial clout to take over the remaining Canadian companies such as Sask Pool and Agricore. They have available capacity in grain terminals at U.S. ports and will rationalize grain handling across borders.

- The railways and grain companies operate transborder. Ownership is substantially foreign. Open access in Canada would discourage investment in the Canadian system. Investment will instead shift to rail infrastructure serving the U.S. Pacific NorthWest ports. Capital is mobile.

Assumption grain companies will pass savings on to farmers

- Farmers have less market power than grain companies to capture the benefit of any short-term reduction in rail rates as a result of open access. After the transition of the Wheat Board to buying at port, oligopoly grain companies will have even more room to skim off the savings of rail discounts and reductions in rail rates. How will railway revenue reductions take effect in cases where farmers are not shippers and for transactions outside the grain pool accounts?
- In the emerging agriculture economy, farmers will be under contract with chemical companies for inputs and with grain companies for the sale and transportation of product. The structure of the grain companies is oligopoly rather than pure competition. While the rail system is under the microscope, there is no similar investigation of grain company tariffs, revenues or margins. While the Agency did an analysis to determine how railway productivity savings were shared, there is no analysis of how the grain companies shared the savings of consolidating country elevators.
- The grain companies have been able to close elevators and raise tariffs without government interference or control. Elevator closures have progressed far faster and more extensively than rail closures. While grain rail rates paid to the railways (including the Crow Benefit until 1995) declined five per cent between 1987 and 1999, elevator charges increased 52 per cent. What happened to the savings from elevator closures?

Open Rail Access

An earlier version of the proposed 1995 Canada Transportation Act would have allowed running rights for a provincial railway on a federal railway to the nearest interchange with a competing federal railway. This would have given a short line railway access to both CNR and CPR instead of just one of them. The Federal Government removed this provision from the Bill because it was concerned about CNR and CPR losing traffic to other railways and being less cooperative in setting up short lines. It was probably also concerned this would have reduced the share value of privatizing CNR.

Some commodity groups in the Estey/Kroeger process proposed an even more extreme form of open access. They recommend that “any person” (including a provincial short line) may apply to the Canadian Transportation Agency for running rights over the lines of another railway with the onus being on the latter to show why the application should not be granted.

It should be noted that Canadian legislation already allows a (federal) railway company to apply for running rights over another railway where this cannot be agreed to voluntarily. According to the Estey report, since 1988 the Agency (NTA or CTA) has received only four applications for imposed running rights, and has not ruled in favour of any of them. The current process to impose running rights has not been used extensively because of uncertain results.

Currently, it appears that the applicant has to prove that imposed running rights are in the public interest. Under the proposed system, the host railway would instead have to prove that running rights would be detrimental to the public interest. This is the so-called “reverse onus” test. A stakeholder proposal to Kroeger also talks about legislative direction to the Agency to give primary emphasis to the interest of shippers (over the railways).

Although the impetus for open rail access comes from the grain reports of Estey, once implemented it cannot be contained to just grain, just the Western lines, or just the Canadian based railway companies. It would also be extended to other bulk products using West Coast ports such as coal and potash. U.S. based railroads would also gain access to the traffic on CN and CPR lines in the industrial heartland of Ontario and Quebec. Once implemented, even for a five year trial period, open access cannot easily be reversed.

The revenue cap and open access are not sustainable long-term policies unless similar measures are adopted in the U.S. Investment would shift from Canadian lines to U.S. lines where return on investment would not be affected by revenue caps and access.

Heavy Haul Truck Corridors

The proposal for open rail access must also be considered in the context of the plan by B.C. Alberta and Saskatchewan to establish and designate a regional network of heavy haul trucking corridors, acknowledging that some routes may require upgrading. The plan as currently envisioned would target indivisible loads and specialized heavy haul equipment. There is every reason to suspect that, once corridors are designated and upgraded, the trucking industry and shippers will want to make widespread use of them for divisible loads.

A possible working model of a heavy haul corridor was the movement, for about 30 years, of Saskatchewan potash 100 kilometres by truck to a Burlington Northern railhead at Northgate N.D. (Note, these loads were divisible) Early on in the program, highway 9 was severely damaged and then rebuilt. By the 1990's, trucks under permit were operating at about 190,000 pounds gross weight, compared to 138,000 under the national standard.

Manitoba is not designating heavy haul corridors because it does not agree to the proposed axle weight limits which would increase road damage.

The heavy haul trucking plan points to the continuing fragmentation of truck size, weigh and safety standards across provinces. The Government has not implemented the recommendations of the 1993 National Transportation Act Review Commission which would see the Federal Government implement consistent national standards for interprovincial and international trucking. The Review Panel should revisit these recommendations.

Impacts of Open Access and Heavy Haul Corridors

The availability of open rail access and heavy haul trucking corridors would increase political pressure to further deregulate the Wheat Board export controls and deregulate the Grain Commission standards in order to allow Canadian exports to flow through U.S. ports. The Board has already examined the cost and feasibility of exporting via U.S. routes.

The U.S. based grain companies are transnational in nature compared to the local Canadian grain companies. With the declining role of the Wheat Board, the transnationals will be able to use their international networks to gain market share from the Canadian grain companies. Open access would allow the transnationals to arrange for their own equipment and have greater control of their logistics system. Transnational grain companies account for four of the top 10 barge firms on the Mississippi system. Government financial support in the U.S. enhanced export elevator capacity and provided an extensive inland waterway system to the Gulf of Mexico and Pacific Northwest.

Open access could lower short-term costs of exporting Canadian grain via U.S. ports, which could result in a shrinkage of capacity at Canadian east and west coast ports. It could also result in a short-term increase in U.S. grain moving in transit via Canada (e.g. SOO/CPR/UP to the Northwest or via Windsor or Niagara Falls to New England). Canada would, however, be at risk of domestic U.S. political actions to stop the flow of Canadian grain when the U.S. system is congested. Contamination of Canadian grain in the U.S. system or by U.S. grain in the Canadian system is another market risk.

In the past ten years, there has been a dramatic increase in grain exports from Canada to the U.S. market, from 60,000 tonnes per year to 3,400,000 tonnes per year. The U.S. share of Canadian grain exports grew from 0.5 per cent to 16 per cent. Open access could increase this amount at the expense of overseas exports via ports.

Disputes over rail access fees would likely result in government regulatory and political intervention. If the fees are too high, grain would be diverted to the U.S. system. If the fees are too low, this would likely invite trade disputes over Canadian government intervention and unfair subsidies. Low fees could also harm the financial viability of rail infrastructure, leading to government subsidies.

It is not clear that the short-term rate reductions under open access would flow through to farmers. The grain companies might keep some of it rather than pass it on. The Estey report² notes that the grain companies currently handle about 30 per cent of export sales contracts for the Board, for example malting barley. In this case, the companies deduct from the farmer price the full freight rate without railway discounts for multi-car loading. This indicates there is imperfect competition or oligopoly economic power in the grain companies. Estey also noted there was a conflict of interest, or perhaps a divided loyalty, on the part of grain companies owned by or affiliated with multinational operations.

It is difficult and time-consuming to acquire imposed running rights in the U.S., although this has sometimes been required in merger approvals. If more liberal access to running rights is implemented in Canada, this would put Canadian railways at a competitive disadvantage. U.S. railways could obtain running rights to pick up product in Canada and divert it to the U.S. system. Canadian railways would not have reciprocal access to running on U.S. rail tracks south of the border. Investment would flow from the Canadian to U.S. lines where returns are higher.

² Hon. Willard Z. Estey, Grain Handling and Transportation Review Final Report, 1998, p.16

Canada's Parliament cannot legislate open access on provincially incorporated railways. Thus, while short lines would be able to operate on CNR/CPR tracks, CNR/CPR might not be able to operate on short lines. This would create a competitive advantage for short lines in addition to their non-union labour costs.

Taxpayers will pay for the extra road damage and to upgrade heavy haul corridors for higher axle weights and may have to subsidize railway infrastructure due to declining traffic. Overall economic efficiency declines as there are greater demands on public funded roads while less utilization is made of existing user-pay east west rail lines.

Private Sector Regional Railway Proposal

Omnitrax is proposing to use open access to operate a regional grain transportation system on the prairies. The Federal Government has already gone part way to facilitating this proposal by passing legislation in June that would give the Canadian Transportation Agency authority to require CN or CPR to sell branch lines. It could also grant running rights to a federally incorporated railway to operate on a branch line of another company or on a connecting track to the branch line.

Current proposals expand this concept of a regional railway farther. For example, there is a suggestion to allow provincially incorporated railways to operate over a connecting main line to the interchange of a competing main line. Even more extreme is the concept of allowing forced access beyond the interchange with a connecting carrier.

A regional system focused on railways alone will fail. There is no future for branch lines if the transnational grain companies acquire control of grain markets and can force-feed grain to inland terminals on main lines. How can you have community-based branch lines if there is no grain?

And once a private sector company has used the regional railway concept as a way to build political support for open access to get into the main line business, what interest will it have in operating marginal branch lines? In the meantime, forced open access at regulated fees in Canada would expose Canadian grain exports to trade challenges.

System Approach Alternative

Our union has been working together with farmers and communities to develop an integrated regional grain system in order to lower overall costs by making better and more rational use of existing elevator, rail and road infrastructure. By dealing with branch lines, grain collection and grain marketing in *a system approach*, it can secure a supply of grain for the branch lines. Moreover, this would be compatible with international trade rules. It would not discourage investment in the Canadian east west main lines.

CN has agreed in writing to explore these options with us. This opens the door to set up a process whereby farmers, labour, communities and the railway can together explore innovative solutions to the challenges facing the branch line system and road infrastructure in the prairies as well as the handling and marketing system. CN acceptance is enabling us to move the debate beyond the rigid traditional, and often adversarial, relationship among stakeholders to identify creative solutions in our common interest. We have informed federal and provincial governments of this proposal.

For the first time, it may be possible to analyze the assets of railways, roads and grain gathering systems to develop an intermodal system that minimizes the total cost and captures the maximum benefit for farmers, workers and for Canada in the restructuring of the grain sector.

The Federal Government has expressed interest in a community-based solution. We would like to see it participate in this initiative.

Following are the benefits of our system approach alternative compared to the private regional railway concept or open running rights:

- 1) CN has agreed to work with us on a region-wide branch line solution.
- 2) Provide service at cost to farmers, after covering the fixed cost of investment
- 3) Generate system synergies by coordinating branch lines with grain handling
- 4) Obtain regional economies of scale and attract grain to branch lines by working together with local communities and farmers for mutual economic benefit
- 5) Joint planning of road and rail infrastructure for a least-cost intermodal system

The Government needs to consider introducing more integrated policies on a continental basis. Such policies need to be conducive to an institutional re-arrangement in which Canadian farmers, workers and rural communities are able to develop and maintain a strong level of countervailing power to deal with the increased concentration of ownership in the grain handling and transportation system.

Farmers and labour cannot and will not stop the global restructuring affecting the Canadian grain handling and transportation system. Governments can help by supporting the development of an alternative in which the ultimate goal is to create a vertically integrated grain system under farmer, labour and community control that can effectively compete within the rules of the deregulated global economy. Unlike the private regional railway proposal and open access, it would not trigger challenges under trade agreements. It would not extract wealth from rural communities.

Reporting Requirements

Under the Canada Transportation Act, the federal Minister tables an annual report on transportation. Transport Canada should be commended for producing very comprehensive reports that are useful to everyone involved in the transportation debate.

However, there is a serious shortcoming in the scope of the material on road subsidies. The tables of cash expenditures do not illustrate the true economic cost on a life cycle basis including interest and depreciation. If these charges were included, the annual road subsidy would amount to about \$5.5 billion.³ The road should allocate costs of federal, provincial and municipal roads to big trucks.

The annual report should also determine the costs imposed on society by different modes of transportation for pollution, accidents, noise and congestion. Some will say these cost are difficult to quantify. The fact is that are being quantified. By leaving them out, they are being quantified as “0”. There is no science to support the conclusion of zero cost. A full cost accounting for transportation would be conducive to implementing a least-cost intermodal policy.

³ based on work done by Transport Canada in a special report in 1996 on road life cycle costs and road-related revenues

Recommendations Suggested to the Review Panel

Do a comparative analysis of the current Canadian framework and options for change with the surface transportation policy framework in the U.S., our major trading partner.

Analyze the implications and constraints on domestic transportation policies (including the grain revenue cap and open access) in the context of international agreements signed by the Government of Canada.

Amend the parameters of the Transport Canada annual report to include road subsidies based on life cycle costs, highway cost allocation to big trucks and a full-cost analysis of different modes of transport.