

# COALITION OF RAIL SHIPPERS

September 24, 2009

Dale McKeague  
Director, Industry Determinations and Analysis  
Canadian Transportation Agency  
Ottawa, ON  
K1A 0N9

Dear Mr. McKeague:

The Coalition of Rail Shippers (CRS) is an affiliation of shipping industry associations that has been together since 2005 and whose members account for over 80% of the revenues of our national rail freight carriers. The CRS provides input to government on matters affecting Canadian rail freight transportation. The CRS membership list is attached.

We appreciate the opportunity to comment on the Canadian Transportation Agency's plans to conduct a: *Review of the methodology used by the Canadian Transportation Agency in determining cost of capital for federally regulated railways.*

## TIMING

The first question that comes to mind is..."Why now?" In our view the proposed review is ill-timed. The market place for shippers has undergone catastrophic change and continues to be unstable as a result of the worst global recession since the thirties. Also, this is a time of severe instability in financial markets.

## OBJECTIVES

On page 4 of the draft RFP, an examination of "*a variety of existing cost of capital methodologies which could potentially be used by the Agency for determining cost of capital rates*" is set out as an objective. We question the relevance of "*existing cost of capital methodologies*". Canadian railways serve a much different marketplace than their American counterparts. Since a review of the cost of capital methodology has been requested by Canadian railways, the focus of the review should be limited to Canadian jurisdictions.

The draft proposal states that a reasonable methodology "*be consistent with the objective being pursued - namely to provide regulated railways with a fair and reasonable return, thereby*

*providing railways with continued incentives to invest and protecting shippers from abusive rates.”* The notion that a reasonable methodology should provide railways with “*continued incentives to invest*”, rather than simply enabling them to secure required capital, is difficult to endorse.

In addition, the *Canada Transportation Act* makes no mention of “abusive rates” nor is it an appropriate “Objective”. Shippers should not merely be protected from “abusive rates” but rather be provided with rates in accord with the National Transportation Policy as set out in Section 5 of the *Act*, (rates that would be expected to be found in environment of effective competition). Similar to the concept of “*providing an incentive to invest*”, the provision of a “*reasonable rate of return*” may have nothing to do with whether or not railways impose “abusive rates” on shippers. Such abuse is most likely to occur in situations where a railway is in a position of monopoly power irrespective of the rate of return.

#### SCOPE

On page 5 of the RFP, Phase 1 (B) requires: “*An examination of the approaches adopted by up to five regulatory bodies for establishing cost of capital rates. Amongst the five there should be at least two regulatory bodies responsible for regulating rail transportation on a national level...*”

In the face of this requirement, it is natural to assume that the United States Surface Transportation Board (STB) is likely to be one of these regulatory bodies and there are a number of reasons why shippers see this as inappropriate.

U.S. railroad transportation policy differs significantly from Canadian policy. Canadian transportation policy requires that rates be consistent with those that would be achieved in an environment characterized by effective competition. In addition, the capital funds used to support U.S. railroad investments are derived from very different borrowing and tax sources than are the Canadian capital funds.

Additionally:

In Canada, the Canadian Transportation Agency (CTA) makes annual determinations of the cost of capital rates to be used in:

- ❑ The determination of the western grain revenue cap
- ❑ The setting of regulated interswitching rates

- ❑ The setting of extended interswitching rates
- ❑ The setting of competitive line rates
- ❑ The setting of joint rates
- ❑ Agency Orders pertaining to capital works in levels of services complaints
- ❑ Parties to final offer arbitration proceedings also routinely estimate railway costs, using the cost of capital rates established by the Agency.

Areas where the STB must make costing determinations, and more specifically – cost of capital determinations - differ greatly, however, from those carried out by the Canadian Transportation Agency in Canada, and we would suggest are inappropriate in any comparisons to the Canadian rate-setting regime.

We strongly recommend this Review be suspended until a more thorough consideration of the potential consequences is undertaken. Serious reconsideration should also be given to the fast-track approach being proposed. At a minimum, a matter of this consequence should provide full opportunity for affected parties to present their positions and comment on others in a public forum before the terms of reference are finalized.

This review clearly raises the potential of a windfall for railways which again begs the question why? Over the past decade, using the current methodology, our national carriers have enjoyed consistent record profits, unlike the shipper community who do not have the same marketplace advantage. CRS is of the view that the railways' desire for changes that would enhance their bottom lines is not reason enough to undertake a review?

For example, the potential for a grain risk adjustment is assessed annually by the Agency and routinely it is determined that none should apply. There are sound reasons for this: grain is a growth export and one of our most consistent and reliable commodities, and poses little or no risk for carriers, therefore no increase is warranted. Why is this item under consideration?

It is the view of CRS that any changes to the matters set out on pages 8 and 9 under the heading: *2. Current and Recurring Issues raised with regard to the Agency's Cost of Capital Methodology* will result in significantly increased costs for shippers. At a time when the industries which are key drivers of the Canadian economy are struggling to maintain sales and

employment levels, it is unreasonable to introduce a process that will result in these industries being saddled with higher shipping costs.

It is apparent this proposed review is being considered because Canadian railways are in favour of it. Shippers are not. In the face of such diametrically opposed viewpoints from the rail freight network's key stakeholders, the CRS recommends that the Agency consider carefully whether such a review is required at this time. The Agency's current cost of capital methodologies are largely based on the 1985 Cost of Capital Decision of the Canadian Transportation Commission, which followed a 4-year review of railway cost of capital methodology. That Decision was very specific respecting the rationale underlying its findings. The need for a further review now should be dependent on whether changes have occurred which undermine that rationale. The segment of the TOR that discusses the need for the current review does not refer to any such changes. Prior to undertaking such a contentious process, the CRS would recommend that the Agency first conduct an evaluation to determine whether or not the present rationale and, by extension methodology, are still valid.

In summary, we question the need for the Cost of Capital Methodology Review in the absence of more in-depth consultations between the Agency and stakeholders on such an important matter and, in addition, we are concerned about the commencement and timing of the review on such short notice to stakeholders.

We would appreciate receiving your responses to the points addressed in this submission and look forward to hearing from you in the near future. The CRS group would be pleased to meet with Agency officials to further discuss these issues.

Sincerely,



R.H. Ballantyne  
Chairman  
Coalition of Rail Shippers  
& President  
Canadian Industrial Transportation association

cc: Coalition Members

## Coalition of Rail Shippers

### Members

- Animal Nutrition Association of Canada
- Association of International Automobile Manufacturers of Canada
- Canadian Canola Growers Association
- Canadian Dehydrators Association
- Forest Products Association of Canada
- Grain Growers of Canada
- Inland Terminal Association of Canada
- Pulse Canada
- Shippers Council of Canada, a coalition of:
  - o Canadian Chemical Producers' Association
  - o Canadian Fertilizer Institute
  - o Canadian Industrial Transportation Association
  - o Mining Association of Canada
  - o Propane Gas Association of Canada
- Western Canadian Shippers' Coalition
  - o Alberta Forest Products Shippers Association
  - o Canadian Oilseed Processors Association
- Western Canadian Wheat Growers Association
- Western Grain Elevator Association

Canadian Industrial Transportation Association  
Ottawa, ON  
November 12, 2008