



CP SUBMISSION TO THE CANADA
TRANSPORTATION ACT REVIEW PANEL



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EXECUTIVE SUMMARY & INTRODUCTION

EXECUTIVE SUMMARY

Canadian Pacific (CP) is pleased to provide this submission as part of the *Canada Transportation Act* (CTA) review that was launched by the Minister of Transport on June 25, 2014. The Review provides an important opportunity to undertake an in-depth fact based analysis of federal transportation policies in Canada.

Since the last Review in 2000, the Canadian and global economies have undergone significant change. The most fundamental advancements have been the fast paced growth of developing economies, increases in commodity prices and diversification of Canada's trading partners.

CP plays an important role in supporting Canada's trade-based economy as 66% of our freight crosses a border or moves through a port. Moving forward, trade will remain a key driver of Canada's prosperity where ambitious resource development and trade agendas are being pursued. In order for Canada to remain globally competitive and capture future opportunities we need policies that encourage further supply chain integration and robust levels of private sector investment.

Since 2000 CP's traffic has grown significantly and CP has invested over \$13 billion of private sector funds into our infrastructure. This investment in capital and technology has enabled a 60% increase in CP's labour productivity growth which has allowed CP to maintain rates in line with inflation and improve its financial sustainability. Given significant increases in many commodity prices this rate performance has resulted in rail transportation costs now being a lower percentage of the overall cost of the production and manufacture of commodities and goods exported to world markets and consumed in domestic markets. This is in contrast to the previous era where there was chronic underinvestment in the rail system, requiring the government to subsidize investment through such measures as rehabilitation of CN and CP grain branch lines and the purchase of grain hopper cars.

There was much discussion during the winter of 2014 regarding the performance of the rail-based grain transportation supply chain in response to a grain crop which was a major record in terms of size. CP responded to the challenge, as we moved 21% more grain during the 2013/14 crop year than our 3 year average and 16% more grain than ever. These quantities are unlikely to be matched for quite some time. This year's crop is back to historic levels and is 24 percent or 18 MMT smaller than last year's crop.

In this submission, CP presents some ideas for consideration on how to promote investment, increase capacity, support safety, advance supply chain cooperation and integration as well as improve the supply chain. These include:

- Sun setting the legislative provisions contained in Bill C-30;
- Having the shipper provisions in the CTA recognize the network nature of the rail sector;
- Maintaining the timelines for decisions on service matters in the CTA;
- Strengthening safety has a consideration in the CTA;
- Rationalizing the shipper provisions in the CTA;
- Commercializing the movement of Western export grain so that it is treated like all other commodities and goods;
- Improving Canada/US regulatory harmonization;
- Giving the Federal Minister of Transport the sole authority to approve rail crossings;
- Undertaking the necessary legislative changes to allow railways to use Locomotive and Video Recorders to proactively improve safety; and
- Having the Canadian Transportation Agency assess the impacts on operations and safety in decisions related to noise and vibration.

Over the medium to long term CP is confident that in the right rail policy environment the railway has considerable room to grow within its existing foot print.

Elements to support growth include financial sustainability, continued operational innovation and origin/destination supply chain capacity especially in key gateways such as Vancouver as well as acceptance of the policy matters noted above.

This review is very timely. Over the last years, since the previous review, we have seen a considerable layering-on of regulation, including in matters related to service. This has caused a departure away from the basic tenets of transportation policy in Canada namely that “competition and market forces... are the prime agents in providing viable and effective transportation services” and that regulatory recourse should only be an option when

competition and market forces are not prevalent. This divergence, if continued, can be detrimental because with excessive regulation we will return to an era of capacity reducing under investment. Careful, transparent and informed consideration of the regulatory regime is needed and welcomed.

INTRODUCTION

CP is a Class I railway that operates 13,700 miles of track in Canada and the US. We employ a workforce of 15,000 serving over 10,000 customers and handle more than 7,700 tendered shipments per day.

FIGURE 1: CP NETWORK



FIGURE 2: CP'S TRAFFIC BASE (2013)

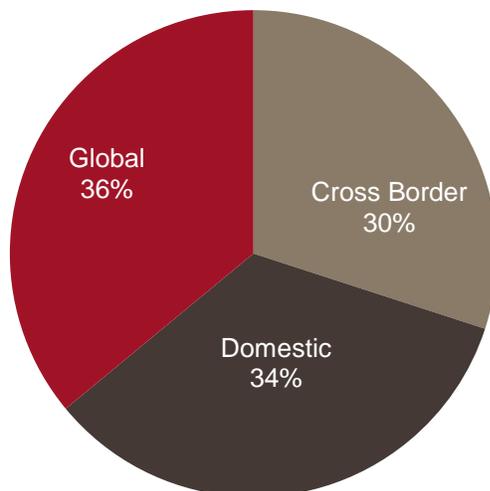


FIGURE 3: CP BOOK OF BUSINESS (2013)

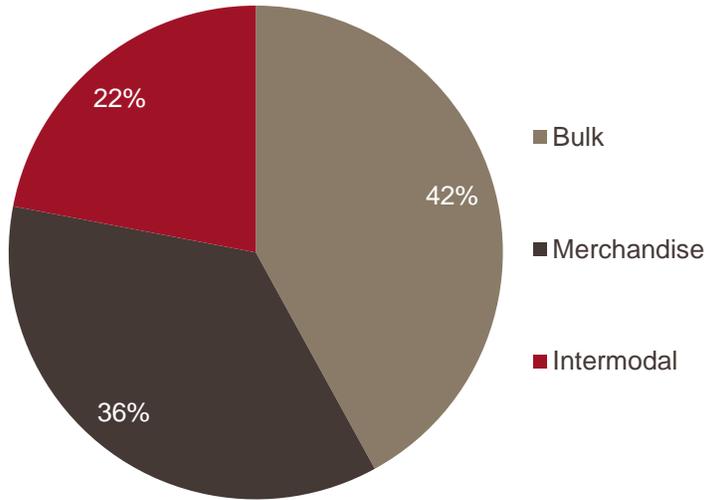
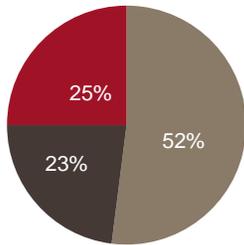


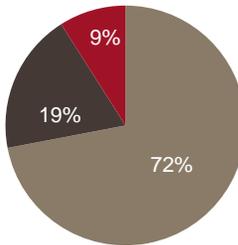
FIGURE 4: CP BUSINESS BY SEGMENT (2013)

Bulk
(% of 2013 Freight Revenues)



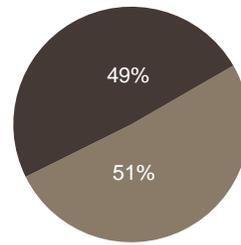
- Grain
- Coal
- Sulphur and Fertilizers

Merchandise
(% of 2013 Freight Revenues)



- Industrial & Consumer Products
- Automotive
- Forest Products

Intermodal
(% of 2013 Freight Revenues)



- Domestic
- Import/Export

KEY FACTS (2013)

TRACK MILES	13,700
WORK FORCE	15,000
2013 CARLOADS	2.7 MILLION
SHIPMENTS TENDERED DAILY	7,700
REVENUE/REVENUE TON MILE (RTMS)	4.3 (CENTS)
AVERAGE LENGTH OF HAUL	844 MILES (1,350 KM)
2013 REVENUE	\$6.1 BILLION
2013 GROSS TON MILES (GTMS)	268 BILLION

CHAPTER I

ECONOMIC CONTEXT

CP PERFORMANCE SINCE THE LAST REVIEW

Since the last review of the *Canada Transportation Act* (CTA) in year 2000, there has been significant change in the national, North American, and international economies, which has directly impacted railways and their customers. One of the major changes has been the significant demand for and

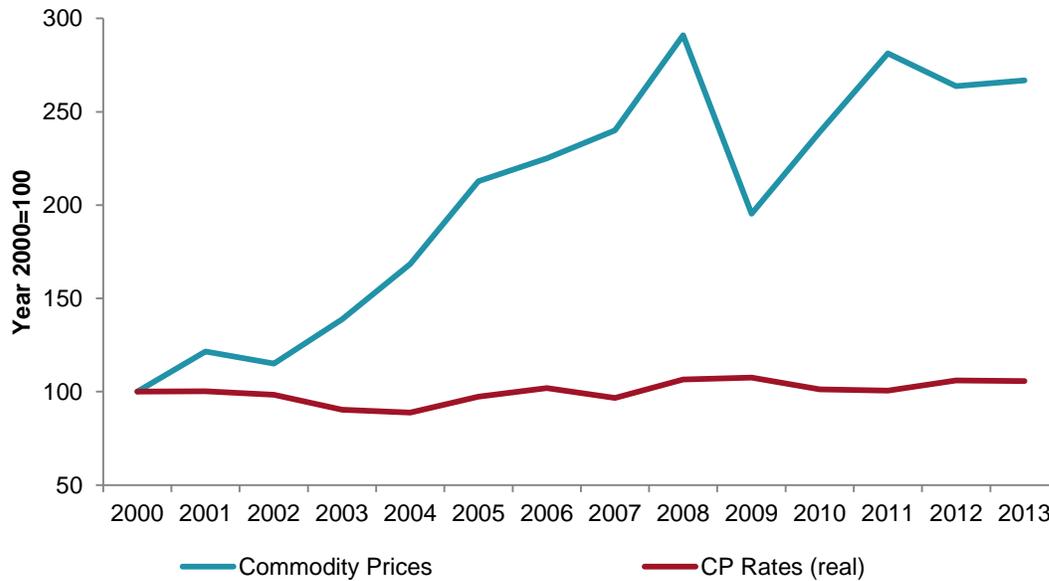
subsequent increase in commodity prices since the last review. As illustrated in Figure 5, commodity prices have increased 166%¹ or 4% annually, in inflation adjusted terms, between 2000 and 2013. In contrast CP's freight rates (revenue/revenue-ton-mile) have increased by 5.7% or 0.4% annually, inflation adjusted, over

the same time period. The growth in commodity prices has been primarily driven by the sustained long term demand associated with the growth of developing economies.

As illustrated in Figure 5, commodity prices have increased 166%¹ or 4% annually, in inflation adjusted terms, between 2000 and 2013. In contrast CP's freight rates (revenue/revenue-ton-mile) have increased by 5.7% or 0.4% annually, inflation adjusted, over the same time period.

¹ Bank of Canada Commodity Price Index

FIGURE 5: CP REVENUE/RTM VS COMMODITY PRICES, 2000-2013



Sources: CP Annual Reports and the Bank of Canada Commodity Price Index

Today's commodity prices are in direct contrast to the situation in year 2000 in which the prices of Canada's natural resource-based exports had been in decline since the 1970s due to lack of global demand and excess capacity. Further, at that time transportation costs represented a large component of the delivery price of bulk commodities. Given the growth in commodity prices and the flat growth in rail rates, rail freight represents a much smaller percentage of the delivery price of goods and commodities. For example and as shown in Figure 6, canola seed sold on average for \$545/tonne during the 2013/14 crop year, canola seed sold for \$288/tonne during the 1999/2000 crop year. During the 2013/14 crop year rail transportation cost is only about \$33/tonne or 6% of the delivery price for this commodity versus \$26/tonne or 9% of the delivery price during the 2000/01 crop year. This same fact holds true for many other commodities.

The average rate per ton for grain on CP is \$33. When distance is added the average rate per revenue ton-mile for grain is 3.4 cents. Canadian railways represent an incredibly efficient way

of getting Canada goods over long distances to tidewater and domestic markets. Canadian rail rates are the lowest in the world².

FIGURE 6: CANOLA SUPPLY CHAIN COSTS & CASH PAID TO FARMER, ONE TONNE OF CANOLA

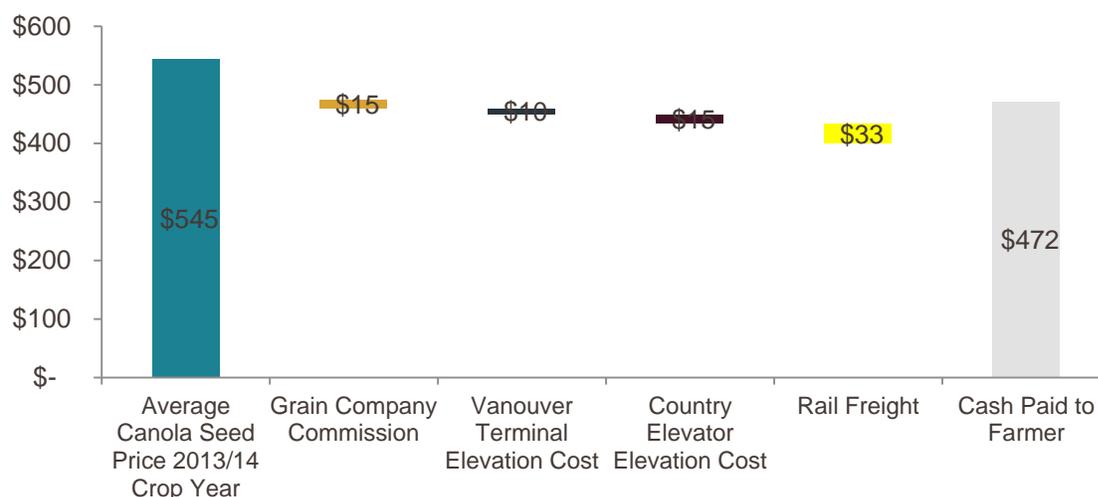


Figure 7 shows an index of CP rates (Revenue/RTM), volume growth (RTM), and labour productivity (RTMs/Employee), 2000–2013. Over that period CP’s rates are essentially flat. The primary drivers of this rate

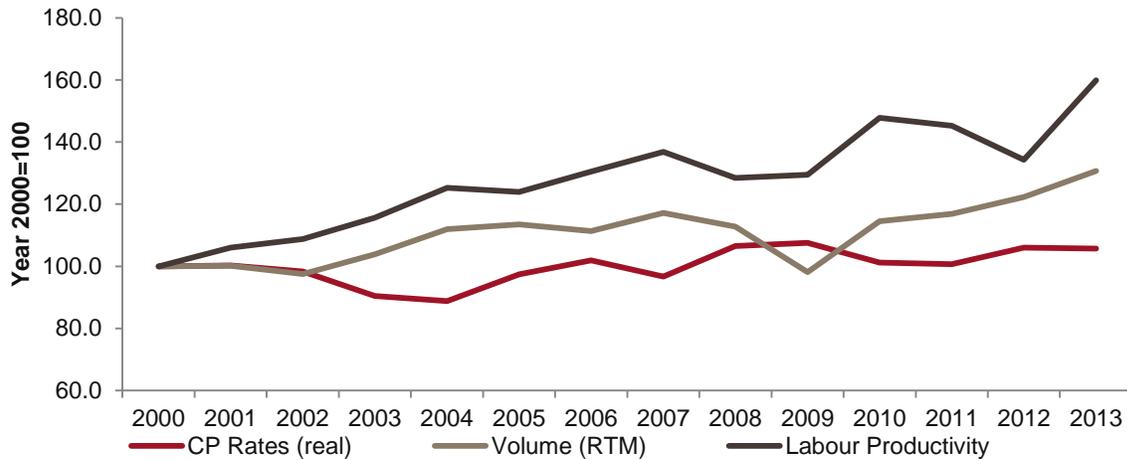
CP’s labour productivity has increased by 60% since year 2000 whereas overall business labour productivity increased by only 13%.

performance have been the considerable growth in productivity over the time period. CP’s labour productivity has increased by 60% since year 2000 whereas overall business labour productivity increased by only 13%³. The growth in productivity has allowed CP to absorb significant increases in other input costs such as fuel, steel, machinery and equipment to name a few. This has directly benefitted customers as they are able to get rail service at rates that are among the lowest rail freight rates in the world. This rate performance is also clear evidence that market forces are real and prevalent in the rail sector.

² Oliver Wyman "International Rail Regulation in Development Markets: Where Does Canada Stand?", November 26, 2014, page 28.

³ Canadian Business Labour Productivity: Statistics Canada CANSIM Table 383–0008

FIGURE 7: CP INDEX OF VOLUME (RTMS), REVENUE/RTM, AND LABOUR PRODUCTIVITY (RTM/EMPLOYEE), 2000-2013



Source: CP Annual Reports

Since 2012, with management change, CP's growth in labour productivity has accelerated by 19%. Going forward, however, productivity growth could slow given practical limitation on railway innovations. Some of the technical and operational innovations of the last years include:

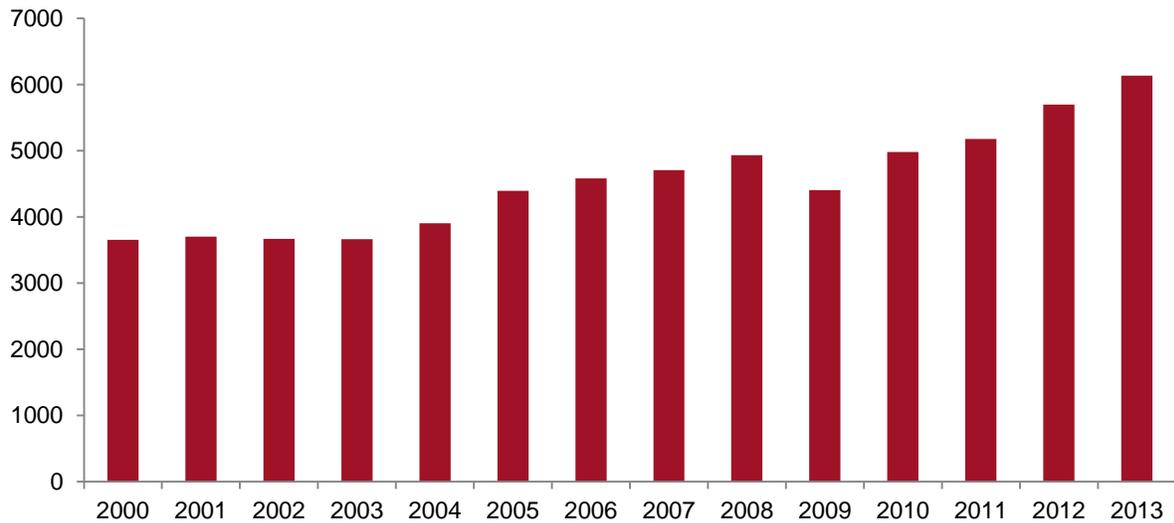
- Directional running;
- Co-production agreements;
- Distributed locomotive power;
- Longer trains;
- Heavier trains;
- Locomotive design (Tier III & IV);
- Railcar design;
- Fuel trip optimizer;
- Wayside detection systems including wheel impact load detection, acoustic wheel bearing detections;
- Dragging equipment detectors;
- Automatic Equipment Identification (AEI) tags;

- Greater use of centralized train control (CTC);
- Remote locomotive control (belt pack) in yard operations; and
- Narrow band communication technology.

CP continually assesses new technologies to improve safety and operational performance. However, in some cases, current legislation and regulation prevent the implementation of operational-enhancing technologies.

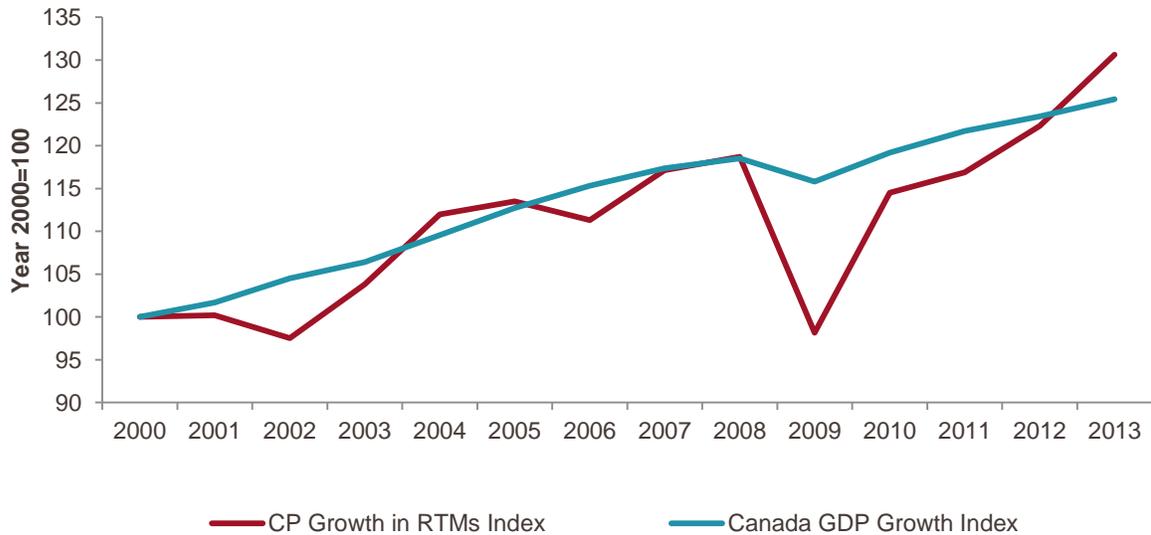
CP's annual growth in revenues and RTM's has been in-line with the growth in Canada's GDP, as seen in Figures 8 and 9.

FIGURE 8: CP REVENUE 2000-2013 (\$MILLIONS)



Source: CP Annual Reports

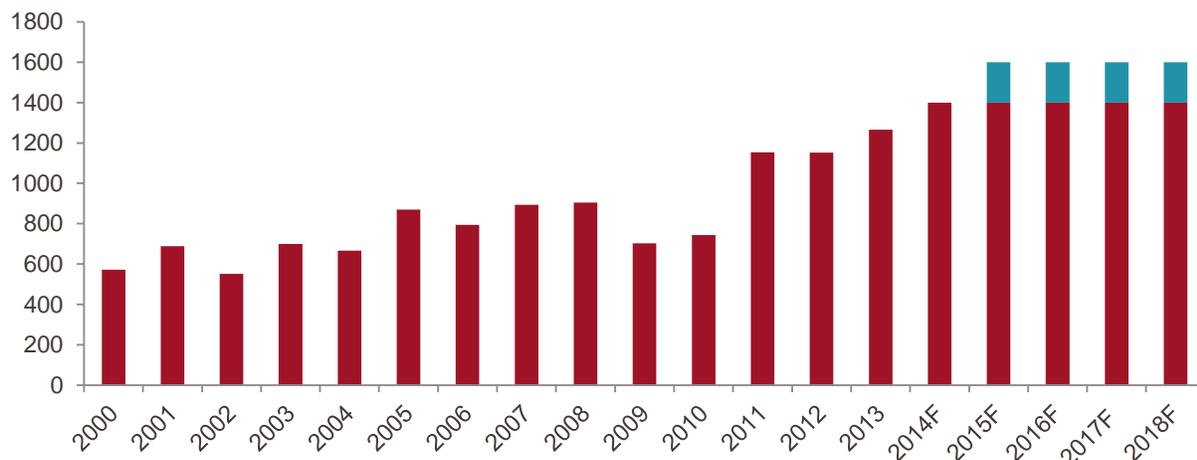
FIGURE 9: INDEX GROWTH IN CP RTMS VS. CANADA GDP GROWTH, 2000-2013



Sources: CP Annual Reports and the World Bank

Between 2000 and 2013 CP's revenue ton-miles (RTMs) has increased by 31% or an annual growth rate of 2%. This is in line with the growth of Canada GDP. However, this growth has been uneven. There was a downturn in 2002 following the economic slowdown at the beginning of the last decade. CP also experienced a historic drop in RTMs in the last quarter of 2008 and through 2009 due to the global economic recession. RTMs in 2009 were down 17% as compared to 2008. However, CP experienced a strong rebound in traffic in 2010, where RTMs increased by 16%. These sizable fluctuations in volumes provide significant challenges in terms of operational planning and deploying expensive capital.

FIGURE 10: CP ANNUAL CAPITAL INVESTMENT (\$MILLIONS)



Source: CP Annual Reports

Unlike many other modes, CP owns, operates and pays taxes on its infrastructure and must generate sufficient returns to fund capital projects that are required for maintenance and capacity

Railways are a very capital intensive industry and element of the supply chain. In the case of CP in 2013 it took \$3 worth of assets to generate \$1 in revenue.

improvements. Railways are among

the most capital intensive industries and the capital deployed is largely immobile. As shown in Figure 10, CP's annual investment increased by 120% between 2000 and 2013. Over the past 13 years, CP has invested between 15–22% of annual revenue back into its operations, as seen in Figure 11. More recently since 2011, capital investment has exceeded 20% of revenue.

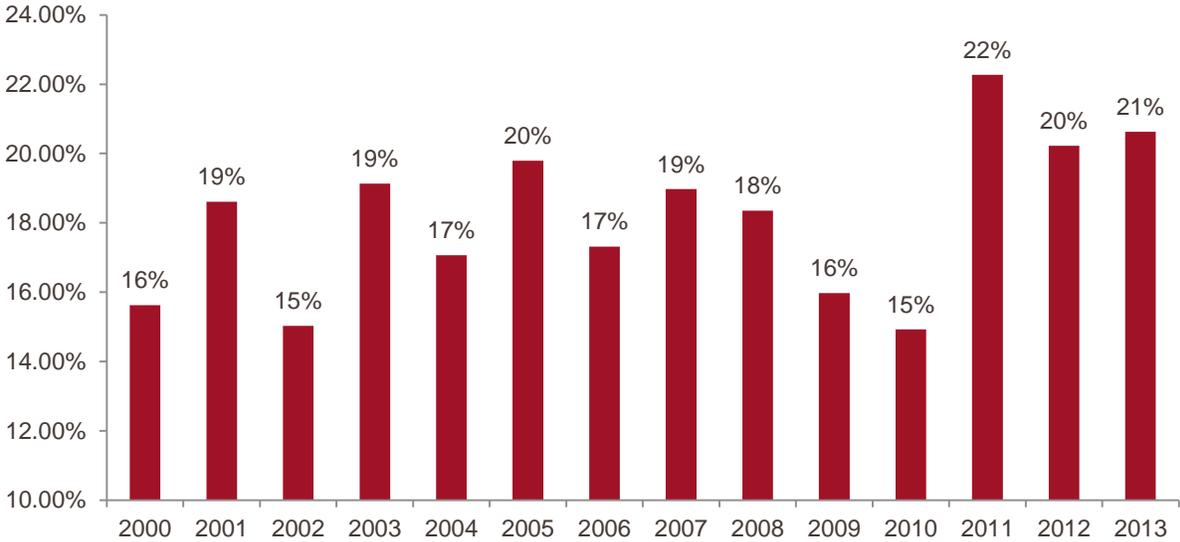
Between 2000 and 2014 CP has invested \$13 billion of private sector capital. Railways are a very capital intensive industry⁴. In the case of CP in 2013, \$3 worth of private sector assets were required to generate \$1 in revenue. These high levels of capital investment should not be taken for granted. Capital investment decisions are very much dependent upon the economic and regulatory environment in which railways operate. Rail investments are long term in nature, with assets amortized over very long periods (40 years). A stable and predictable regulatory environment, based upon market forces and competition first, is required so that the

⁴ Report on Business Top 1000 data.

railway can earn a sustainable return on investment. Failing that, future investments and funding sources will be difficult and costly to undertake.

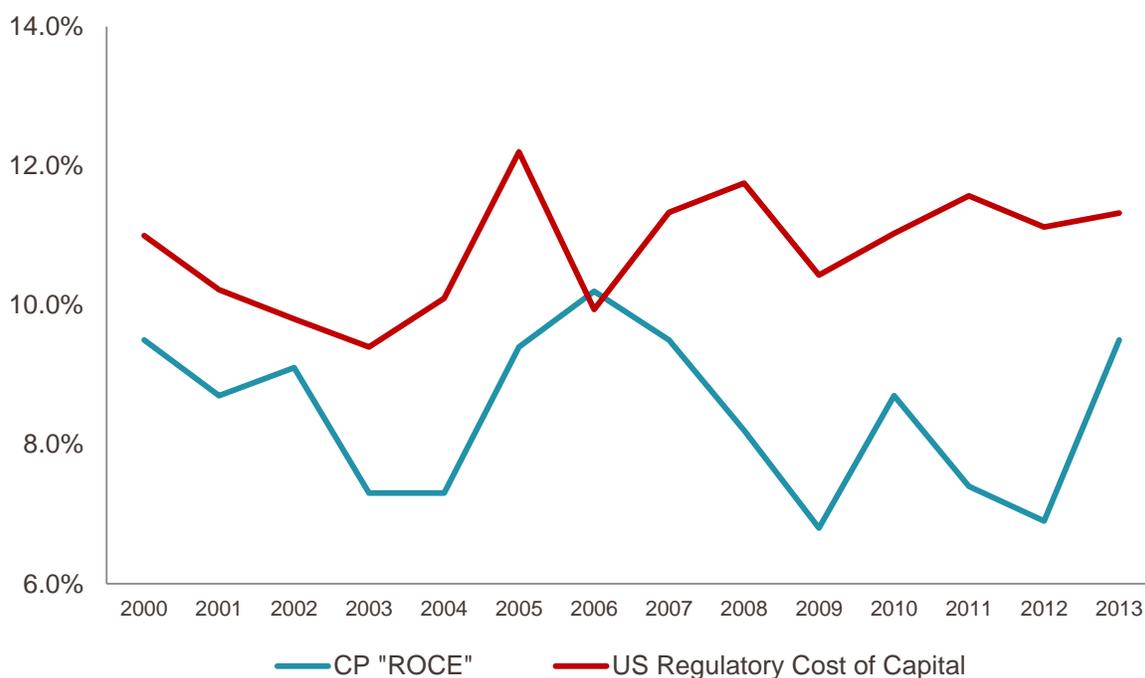
Recently the federal government has introduced a series of regulatory interventions that directly affect how railways operate and conduct their business. The most recent example is the enactment of Bill C-30 “*An Act to amend the Canada Grain Act and the Canada Transportation Act and to provide for other measures*”. The evidence is clear and it is undisputed – the invasive regulatory environment of the past resulted in negative net capital investment. Between 1985 and 1995, being a period of broad economic regulations of railways, the rail systems’ capital depreciation exceeded investment in each year. During that time period the annual underinvestment ranged from \$100 to \$700 million per year.

FIGURE 11: CP CAPITAL INVESTMENT AS A PERCENTAGE OF REVENUE, 2000-2013



Source: CP Annual Reports

FIGURE 12: CP RETURN ON CAPITAL EMPLOYED VS US REGULATORY COST OF CAPITAL, 2000-2013



Sources: CP Annual Reports and the Association of American Railroads

CP must utilize capital markets to raise private sector funds to support long term capital investments. As illustrated in Figure 12, CP has not earned the US Surface

Transportation Board (STB)

regulatory cost of capital over the 2000–2012 time period with the exception of 2006. Simply put, over this time period CP borrowed funds at a higher rate than the rate of return of capital that was being deployed. This situation is not sustainable over the long term, unless, as has been required in the past, the government is prepared to invest (e.g. the grain branch line rehabilitation program).

US regulatory policy, reflected in the 1980 *Staggers Act*, is grounded on the principle that US railroads must earn their cost of capital. This principle was developed due to the experiences that occurred during the 1970's where US regulation prevented railroads from earning an adequate return leading to a series of railroad bankruptcies that had an impact on the supply

CP has not earned the US Surface Transportation Board (STB) regulatory cost of capital over the 2000-2012 time period with the exception of 2006.

chain, customers, and ultimately the economy. Financially sustainable railroads greatly lower the risk of systemic supply chain disruption and enables significant private sector funding of supply chain infrastructure. In Canada, no revenue adequacy policy exists.

The National Transportation Policy, as outlined in Section 5 (a) of the *Canada Transportation Act*, states that “competition and market forces, both within and among the various modes of transportation, are the prime agents in providing viable and effective transportation services”. We agree with this statement and it should be strengthened. Given significant capital requirements of the rail industry, earning an adequate return should, at a minimum, be listed as a consideration in the National Transportation Policy.

Much has been publically reported on the improvement in CP’s operational and financial performance that has been achieved to date under its new management. The metric that is most cited to reflect railway performance is the Operating Ratio (OR). The OR is a ratio of operating expenditures to operating revenue, the lower the OR the better. Prior to CP’s new management being in place, CP was the North American Class I laggard, with an OR in the 80 percent range. This negatively impacted CP’s ability to invest as well as its borrowing costs.

A low OR lowers future borrowing costs, and increases funds available for capital investment. This, in turn, allows CP to improve the capacity, fluidity and the safety of its operations to the benefit of all customers and supply chain partners. It is a virtuous cycle. It is

An OR in the mid to low 60’s is required over a full business cycle to achieve a level of financial performance that will allow CP to earn a return of capital employed (ROCE) that is in line with its true cost of capital.

CP’s view that an OR in the mid to low 60s is required over a full business cycle to achieve a level of financial performance that will allow CP to earn a return of capital employed (ROCE) that is in line with its true cost of capital. Regulatory laws that increase operating costs or prevent CP from earning a fair return for its services will negatively impact CP’s OR. This in–turn negatively impacts CP’s financial performance, increases borrowing costs, and reduces needed capital investment and that has a direct negative effect on capacity, velocity and supply chain performance.

Capacity cannot be defined simply by the number of cars available or the number of cars on the system. Capacity comprises of track, bridges, tunnels, crews, locomotives, cars, snowplows, signaling system, etc. For example, the use of centralized train control (CTC) allows for a

greater number of trains to travel over a territory as compared to the use of occupancy control system (OCS) as the switches can be controlled remotely and trains can be spaced closer together. The effective use of all assets creates capacity for the rail system. Simply putting on additional railcars, in and of itself, will not create additional capacity. In fact,

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it can lead to network congestion which negatively impacts network fluidity and overall capacity. Recent regulatory rulings, especially those related to reduced speed, demonstrate a basic failure to understand this. Speed is not a contributor to railway accidents and does not appear in the top categories related to cause. Regulatory changes, as we have seen recently in both Canada and the US, have focused on train speeds. Those changes are not supported by evidence and have significant unintended consequences related to system velocity, capacity and growth. It is illogical, on the one hand, to ask the rail industry to move more while forcing it to slow down.

The federal government has an ambitious trade and resource development agenda. According to the Honourable Joe Oliver, then Minister of Natural Resources, “In the next 10 years, more than 500 projects representing over \$500 billion in new investments are proposed across Canada”. In addition, Canada is directly engaged in the following trade negotiations: Canada/European Union; Trans Pacific Partnership (TPP); and Canada–Korea Free Trade Agreement. In order to capture the full benefits of future trade agreements and natural resource development initiatives the Canadian economy needs rail to facilitate this trade. To meet future demand for rail services, railways must work with their supply chain partners, using commercial mechanisms and not regulatory ones, in order to expand capacity in the rail supply chain.

CHAPTER 2

CP BUSINESS AND INVESTMENT PLANS

CP BUSINESS AND INVESTMENT PLANS

In 2012 under new executive leadership CP took numerous steps towards creating a strong foundation for growth by improving the cost structure of the company; improving the service offering by working with our customers; and undertaking significant investment in our key corridors. Recently, we announced Phase 2 of our strategy “Moving More”. Central to this initiative is CP’s ambitious growth and investment plans for over the 2014–2018 period.

Overall, CP plans on increasing annual revenue growth to 10% until 2018. To support this growth, CP has a robust multiyear investment plan of record levels of investment of \$1.4–\$1.6B

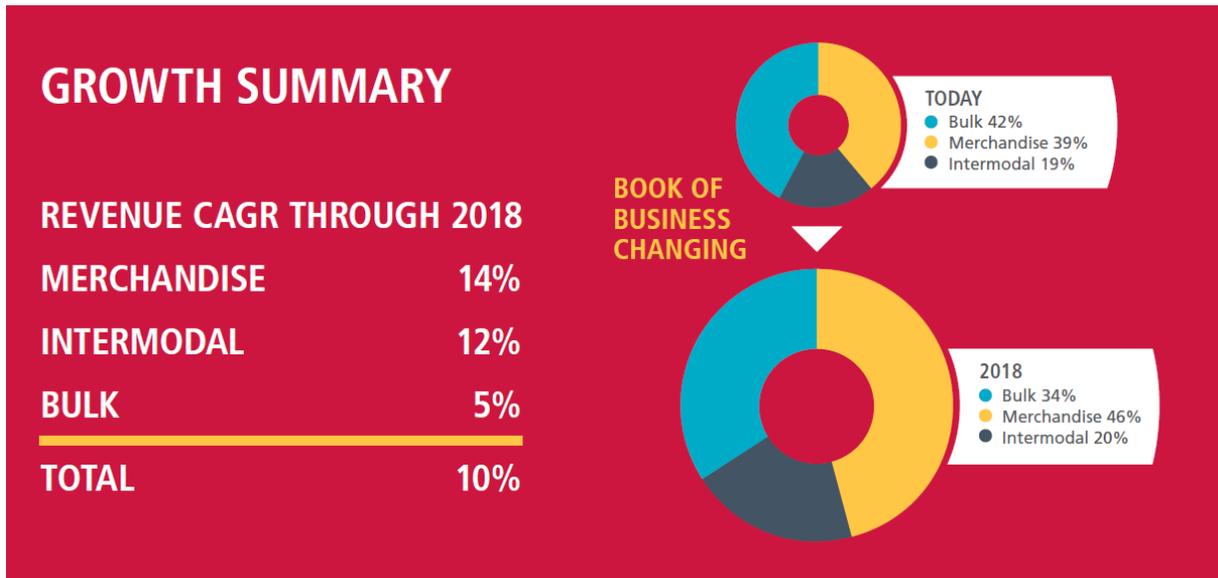
To support this growth, CP has a robust multiyear investment plan of record levels of investment of \$1.4–\$1.6B annually.

annually. CP’s growth and investment plan is aligned with the federal government’s priority of ensuring that Canada has the ability to move products to market in a timely, efficient, and competitive manner.

CP BUSINESS OUTLOOK

Over the next four years CP will undertake a transition in our book of business with expected annual growth in merchandise revenue of 14%, 12% annual growth in intermodal revenue, and 5% annual growth in revenue for bulk traffic. Today bulk traffic, which includes grain, coal, sulphur & fertilizer, represents the largest share of CP’s operating revenue at 42% and is anticipated to be 34% of our revenue in 2018. Our merchandise traffic, including consumer and industrial products, automotive, and forest products, is currently 39% of CP’s operating revenue and will grow to 46% of operating revenue in 2018. The remaining 19% of operating revenue comes from intermodal traffic which will increase to 20% of operating revenue in 2018.

FIGURE 13: CP GROWTH SUMMARY 2014-2018



CP CAPACITY INVESTMENTS

In order to meet growing demand, and to improve service and safety performance, CP is rebuilding its network from the ground up. Approximately half of annual capital expenditures (~\$720 million) will be dedicated toward basic infrastructure, which includes new rail, ties, ballast, bridges, track flaw detection technology, and signals and communication, including additional installations of centralized train control (CTC). These investments will enable CP to improve system velocity and capacity while continuing to improve upon our industry leading safety record.

FIGURE 14: CP NETWORK CAPACITY PROJECTS



Summary of projects:

1. North Line, between Edmonton and Winnipeg: 22 new and extended sidings to handle growth and improve efficiency;
2. Western Canada: Additional sidings and siding extensions to improve efficiency with improved siding spacing and support for long train operations;
3. Eastern Canada: Additional sidings and siding extensions to improve efficiency;
4. US Network: 9 new sidings and siding extensions to handle demand;
5. US Network: Additional sidings, siding extensions, and appropriate siding spacing to improve efficiency and support long train operations;
6. Terminals: Infrastructure upgrades at 8 terminals to drive improved efficiency.

CP is hardening its infrastructure on the North Main Line and between Moose Jaw and Chicago to allow for the effective use of longer and heavier trains to accommodate growing demand in an efficient manner. CP is also undertaking investments in urban centers, including installing new ties and ballast in order to operate more safely.

CP is hardening its infrastructure on the North Main Line and between Moose Jaw and Chicago to allow the effective utilization of longer and heavier trains to accommodate the planned demand. CP is also undertaking investments in urban centers, including installing new ties and ballast and surfacing to further enhance safety in these areas. In addition, the investments will mitigate the impact of winter weather during winter operations, including reducing instances of broken rails and CTC outages, thereby improving fluidity and capacity of the corridor⁵. CP will continue to invest in lock-step with our customers. To achieve adequate rates of return, investment must be “just in time” as the new demand materializes. It would be unsustainable to invest under the model of “invest and the business will come.”

FIGURE 15: CP CENTRALIZED TRAIN CONTROL (CTC) PROJECTS



Summary of CTC projects:

1. US corridor Glenwood to Portal to support increased demand, regulatory Positive Train Control (PTC) required to improve train service;

The use of CTC increases capacity of the network and improves safety.

⁵ Appended to the report is industry data of the impact of winter on rail operations.

2. North mainline CTC in stages concentrating around terminals with intention to extend through the subdivisions in later years;
3. Coal route CTC to reduce delay impact due to meets, improving service and reducing costs.

The use of CTC increases capacity of the network and improves safety. CTC allows for the optimum spacing of trains on the network and significantly reduces meet time between trains. In terms of safety, CTC immediately notifies the rail traffic control (RTC) in the event of a rail break and other hazards on the right-of-way. In such instances, the RTC informs the train crews; trains are protected and Engineering crews are deployed to rectify the problem.

CP is further implementing CTC in high growth areas of the network, including the North Main Line, the coal route in BC, and between Moose Jaw and Chicago.

THE FUTURE - CAPACITY

Over the coming years, CP is well positioned to continue to grow with our customers. In fact, we are in a much better position to expand capacity than most of our supply chain partners. With the right policy environment, as outlined in Chapter 5 of this submission, CP has ample room to expand capacity, including extending sidings and double track, within our footprint.

Over the medium to long term we are concerned about the ability of ports, especially the Vancouver inner harbour, to increase needed capacity to facilitate growing trade volumes. In the case of Vancouver, there is limited access to industrial lands for future development and there is strong community resistance to the expansion of industrial activity. Consideration must be given on how Government policy can support future growth at Canada's major port gateways.

CHAPTER 3

**SUPPLY CHAINS/
COMMERCIAL
UNDERTAKINGS**

THE SUPPLY CHAIN

The rail supply chain consists of several components:

- Origination terminals, reloads, mines, manufacturing facilities, elevators, etc.
- The rail network (carload, intermodal, bulk)
- Interchange with other rail carriers
- Connections with other modes, trucks, barges, vessels
- Port terminals, destination terminals, customer facilities.

Running a network that spans 13,700 miles, which serves 10,000 customers, originates 7,700 shipments per day and interfaces with 5 other Class 1 railroads and numerous short line railroads is incredibly complex.

CP develops operating plans for all movements. As with any multi-user shared network, traffic variability, vessel delays, weather, interchange with other railways, outages and other numerous factors affect the railway and its supply chain connections. Issues in any one area affect the network.

Service design and execution is a crucial aspect of operating a railway and providing customer service across the entire multi-user shared network. When things are going smoothly, it is in large part because of the advance work that is occurring in service design. Running a network that spans 13,700 miles, which serves 10,000 customers, originates 7,700 shipments per day and interfaces with 5 other Class 1 railroads and numerous short line railroads is incredibly complex.

At CP, we use the same set of limited resources, including track space, yards, locomotives, and crews to serve all these customers. In a complex multi-user shared network like the railway, any service issue is exacerbated because of the intensive resource utilization. In order to maintain service at the current average low rate per tonne-kilometer, the intricately-timed moving parts must not be impeded.

At CP we use the same set of limited resources, including track space, yards, locomotives, and crews to serve all these customers.

CP is subjected to level of service obligations under the *Canada Transportation Act*. We cannot refuse traffic that is tendered to us. This additional traffic must be accommodated while considering the service needs for all other customers. CP must also comply with a host of legislative shipper legislative provisions such as final offer arbitration (FOA), service arbitration, interswitching, maximum revenue entitlement, running rights, competitive line rates, etc.

Unfortunately, a recent Canadian Transportation Agency (Agency) ruling has directed a railway to provide service to one customer which is detrimental to others across the network.

CP operates in a transportation marketplace where there are numerous competitive factors⁶, including:

Direct Intramodal Competition: Direct intramodal competition is where there is choice to move traffic between two or more railways. As a result, parallel rail systems in Canada (CP and CN) are often in direct competition for traffic. There are many shippers in Canada that are served by two railways. Furthermore, the CTA Review Panel's 2001 final report defined direct competition as including "traffic that originates and terminates within 30 kms of the points of interchange with a competitive railway"⁷. The Panel estimated that within the 30 km interswitching limit 40% of all rail freight is subject to direct competition. The enactment of Bill C-30 extended interswitching limits to 160 km for all traffic in western Canada. As a result practically all rail freight in western Canada has direct rail competition.

Indirect Intramodal Competition: Rail is subjected to indirect intramodal competition which occurs when a shipper can move a product by truck to another competing railway. In the case of grain, all grain originates on a truck which gives grain farmers the choice of which grain terminal and associated rail service to ship their grain through.

Intermodal Competition: Intermodal competition is traffic that can be shipped by another mode of transportation. CP is subjected to competition from trucks, marine and pipelines. The increase in commodity prices has resulted in greater use of trucks due to decreased transportation costs relative to the price of the commodities. In addition, the use of long combination vehicles (LCV's) has lowered truck operating cost on a tonne-km basis which has contributed to greater competition for the movement of intermodal containers. CP is subject to competition from the marine sector, in particular in the movement of bulk commodities, in the

⁶ To quote "Vision and Balance", from the last Canada Transportation Act Review, "the considerable pass through of productivity gains suggests the presence of substantial competition, overall, in rail markets.", page 41.

⁷ Canada Transportation Act Review Panel, "Vision and Balance", page 30.

Great Lakes region as well as barges. CP also competes with pipelines, namely in the movement of energy products.

Routing Competition: Shippers have the right to control routing of their traffic and regularly use that right as a competitive lever. Even if one railway can carry a shipper's freight from origin to destination (or close to destination), shippers may, and do, insist that the originating railway deliver all or some traffic to one or more other railways. Shippers thereby create their own competitive options.

The rail network in North America includes many options for exchange and transfer of traffic between railways and various alternatives to complete a routing from origin to final destination. Routing of a shipment is chosen by the shipper. The shipper, based upon market factors, can decide to direct transfer of its traffic to a connecting railway at numerous points along a route for a portion of the overall movement. Shippers can and have also included such routing options in regulatory proceedings, including final offer arbitration to leverage legislative provisions as well as routing competition as a tool to attain lower rates.

Gateway Competition: CP is subjected to gateway competition which is when a buyer is able to purchase a product from the same source by transporting the product through an alternative gateway or seaport. For example, a retailer in Toronto purchases containerized goods from a supplier in Shanghai, China. The retailer can choose to ship the product from Shanghai to Toronto through the Port of Metro Vancouver and use CP to transport the goods to Toronto. However, the retailer can also choose to ship from Shanghai through the Port of Prince Rupert, and use CN to ship the product to Toronto

Market Competition: CP is subjected to market competition, namely in the movement of commodities. Market competition occurs in cases where the railway is constrained by competition faced by the product that is being shipped. For example, in the case of metallurgical coal that is shipped by CP from the interior BC to Robert's Bank, the buyer of that coal can purchase coal from other suppliers, including Australian suppliers. CP would be faced with a loss of coal traffic if the rail freight rates render the coal producer uncompetitive.

Product Competition: Buyers of products moved by CP may be able to substitute one product for another. For example, CP moves crude oil from the Bakken region to refineries on the east coast of North America. If the cost to transport crude becomes uncompetitive the refiners can choose to source different forms of crude from other North American or off-shore sources.

Geographic Competition: Geographic competition occurs when a shipper is able to sell their product to alternative buyers in different geographic locations or when a producer with production facilities in different countries can choose to vary production at one facility relative to another, based on the price of transporting products to their customers. When the existence of multiple facilities, which is common in the forest products industry, is used as leverage in rail rate and service negotiations, this is referred to as a form of “shipper leverage”.

Long Run Competition: Long run competition occurs prior to the construction of a particular plant or transportation facility. For example, an automotive manufacturer that is in the process of choosing a new location for an assembly plant may want to have direct access to a railway. Prior to deciding upon a location the manufacturer can negotiate with multiple railways on a long term contract to ensure competitive rates prior to the construction of the assembly plant. On the flip side, shippers can use long-term contracts when making decisions on production relocations.

Given the prevalence of competition in the rail freight market place, one or more forms of competition exist for virtually all customers that we serve. Yet all customers have access to a long list of regulatory options. This is inconsistent with the policy statement in the CTA related to market forces and competition being the primary driver.

COMMERCIAL AGREEMENTS AND SERVICE PARAMETERS

In today’s highly competitive global economy, customers have more diversified service expectations. We recognize this. In examining network operations, service design, and investment plans, CP balances the competing needs of all its customers to provide the best service we can to our customers.

The key to improving service is that as many movements as possible be forecasted and committed. CP spends a lot of time and effort to get assets – cars, locomotives, and crews– in the right place at the right time to handle traffic flows. Getting those assets in the right place takes lead time, whether that involves moving locomotives or training crews to operate over particular territory. This intricate service design is essential to integrate our various services with one another and with appropriate assets in order to avoid negative outcomes like underutilized capacity or causing bottlenecks that ripple through the network. It is important

to recognize that forecasts are estimates. It is an imprecise tool. Nevertheless, lead time forecasts and accuracy in forecasting are also critical elements for planning.

At times a customer's desire for specific service parameters can conflict with efficient railroad operations. This customer's motivation would have nothing to do with the efficiency of CP or the rail's supply chain or with the service received by other customers.

In these instances agreed-to undertakings between a customer and CP can accommodate the needs specific to that customer, while

At times a customer's desire for specific service parameters can conflict with efficient railroad operations.

respecting the other important interests. Examples of these undertakings are prevalent across our customer base given differences in customer needs. That said, allowing parameters of service to be imposed by a regulator on the railway, based on a consideration of only one customer's needs and does not reflect the network aspect of the supply chain can have serious negative consequences for the efficiency of the bus route network. Worse still, is the threat of a diverse set of imposed service parameters for different customers.

Often, for rail as well as in the supply chain generally, service can be more predictable with better visibility and consistency in the traffic offering. Some customers are unwilling or unable to predict, forecast, or commit

shipments to the railways. Because of the inability to forecast or commit to ship their volume, railways similarly cannot forecast or commit to the defined level of service that will be provided when the

Some customers are unwilling or unable to predict, forecast, or commit shipments to the railways. Because of the inability to forecast or commit to ship their volume, railways similarly cannot forecast or commit to the defined level of service that will be provided when the "unforecasted" shipments are tendered.

"unforecasted" shipments are tendered. This is because of the

constant variability in traffic across our entire network and the need to supply crews, locomotives, rail cars, yard and mainline capacity, all of which are not available on a moment's notice. Furthermore, our capacity and ability to move traffic which is presented to us with advance notice is still dependent on the state of the overall supply chain, including ports and terminals, both in Canada and in the US, as well as the availability of specialized equipment,

availability of train crews, as well as rail yards/lines, and, importantly, the needs of other customers.

Foremost from a policy perspective, regulatory options available to a customer should be directly linked to competitive alternatives. If a shipper is considered not to have competitive options it is imperative, for system efficiency reasons, that any service imposed by a regulation is not driven from the viewpoint of any single customer in isolation. Imposed service must be viewed by looking at the entire network because the resulting effects can span the entire network and all traffic flows at the same time. Imposed service would not simply affect the customers who seek these proposals, it would affect all customers. This is also why service cannot be codified up front. It's situational and as such, must be based upon a large set of facts relevant at the time.

An appropriate analogy for the rail system is the city bus route. Bus routes are planned to provide the best possible service to the most people, rather than being tailored to each rider's specific desire. We are witnessing a recent trend where more shippers use regulation in an effort to force the "bus" to deliver taxi service—regardless of the detriment to other shippers.

This trend not only relates to new service arbitration provisions but also in level of service applications and in final offer arbitration. We have also witnessed increased regulatory action during episodic occurrences such as severe weather. Outcomes from these regulatory decisions that look at one customer in isolation can have

Outcomes from these regulatory decisions that look at one customer in isolation can have cascading consequences across the bus-route system. Regulatory decisions are also to be undertaken within very short timelines. This does not provide sufficient time to undertake a proper fact driven analysis of systemic issues or the impact of decision on all the other customers on the bus-route.

cascading consequences across the bus-route system. Regulatory decisions are also to be undertaken within very short timelines. This does not provide sufficient time to undertake a proper fact driven analysis of systemic issues or the impact of a decision on all the other customers on the bus-route. The goal is to run as efficient multi-user shared network as possible, which means maximizing long-hauls, minimizing car handlings, minimizing switching, minimizing the number of times a car must be handled in a yard, maximizing train lengths, consolidating traffic flows, and other efficiency-generating activities.

Service arbitrations also result in what is known as private, confidential “one-off” type decisions. This can also erode service consistency on a network basis and create an accumulation of shipper specific decisions that undermine system efficiency.

COMMERCIAL AGREEMENTS/DINNING FACILITATION PROCESS

CP was a participant in a facilitation process, led by Mr. Jim Dinning, which involved CP, CN, rail shippers, and other supply chain participants as well as government officials, in developing a commercial agreement template⁸ and commercial dispute resolution process.

The meeting participants were tasked with developing a template that would be used by parties to negotiate a service agreement. Mr. Dinning recognized that each and every service agreement is unique and worked with the Committee to establish 16 fundamental elements to guide bi-lateral negotiations. Based on the 16 fundamental elements a three-tiered service agreement matrix was developed. The tiered approach recognizes that as the traffic offering by shippers becomes more predictable and reliable the rail service provided can be more precisely defined in a service agreement (i.e. more elements can be utilized). It also recognizes that defined service levels and consequences, including financial penalties, can be negotiated when shippers commit traffic volumes.

A Tier 1 shipper does not provide a railway with any forecasted traffic volumes or specific volume commitment that will be shipped. In such cases, Tier 1 shippers would not be in a position to negotiate performance standards or financial and non-financial consequences for railway non-performance. A Tier 2 shipper is one that can provide volume forecasts and thereby expand their service agreement to include service standards and non-financial consequences for non-performance. A Tier 3 shipper can provide volume forecasts and volume commitments. These shippers can negotiate financial penalties as they provide more predictable traffic through a volume commitment as well as negotiate a premium service (non-bus route) for a premium price.

⁸ Much confusion exists regarding service agreements, service level agreement and confidential contracts and commercial agreements. CP sees these all as being commercial agreements. The preferred mechanisms being a confidential contract which ties price and reciprocal service offering together in one explicit agreement.

What is fundamental to the tier approach is that without reciprocal commitments shippers will be unable to negotiate service standards or financial penalties because the traffic offering is not predictable. CP supports the Dinning's Report perspective on service undertakings and, therefore, supports the principle of reciprocity in establishing commercial agreements with customers. If a customer wishes to commit to volume forecasts and volume commitments then CP is willing to establish service performance measures within a commercial agreement. Once this basis is determined, then CP is equally willing to include in the commercial agreement performance penalties if service provisions are not met – provided the customer is willing to reciprocate and pay a penalty if it does not tender the traffic that it committed to in the agreement. Underlying this is that the railway, in order to commit to service, invests in a variety of resources and commits to reserve capacity that might otherwise be utilized elsewhere. This affects the interests of others (e.g. terminals, truckers, suppliers, other customers). Accordingly, rail capacity cannot be committed without some certainty on the traffic offering.

CP supports the Dinning's Report perspective on service undertakings and, therefore, supports the principle of reciprocity in establishing commercial agreements with customers.

For example, for most of our major grain customers, we have in place a dedicated train program that was developed over many months in collaboration with our customers. It is based on reciprocal undertakings in the form of reciprocal railway/customer obligations and penalties. If capacity is not delivered by CP then CP pays a penalty to the customer and if capacity is not used by the customer then the customer pays a penalty to CP. Prior to these commercial undertakings grain customers could enter as many requests for rail cars as they wanted without consideration of supply chain capacity or consequences. This system was problematic in that it generated considerable misalignment between expectations and service levels that could be reasonably supplied.

Some shippers and associations have put forward a claim that demurrage is a non-reciprocal financial penalty, one that is arbitrarily imposed on a shipper by a railway. This perspective is misplaced and totally at odds with logic and the law.

Demurrage is simply an asset use charge. Efficient asset use is a key

The purpose of demurrage is to induce the efficient use of rail assets which is essential to effectively servicing the needs of all other customers.

component of providing low-cost transportation and fluid railway operation. Railcar dwell, either in rail yards or at loading facilities, is inefficient, and consumes capacity. Reduced dwell translates into faster, more reliable cycle times and better service.

Very few of CP's customers incur demurrage charges. Ideally demurrage should be kept to a minimum, allowing assets to be efficiently utilized and returned for the next service requirement. This is a very important element given that in some lines of business, like grain, access to rail capacity starts with the furnishing of equipment. Extended railcar dwell at one facility impacts order fulfillment for all other customers.

CHAPTER 4

CP GRAIN PERFORMANCE

CP GRAIN PERFORMANCE

The 2013/14 grain crop was unanticipated and the largest in history by a large margin with crop yields of approximately 80 million metric tonnes (MMT). To put the magnitude of the 2013/14 grain crop into perspective, the previous 5 year crop yield average was 58 MMT.

The 2013/14 grain crop was 37% larger than the previous 5 year average and 27% greater than the previous crop year record in 2008/09.

The 2013/14 grain crop was 37% larger than the previous 5 year average and 27% greater than the previous crop year record in 2008/09. No one, including the federal government, grain farmers, ports and terminals, had expected or predicted a larger than average crop.

Canada historically exports grain shipments of 33–34 MMT. Given that domestic grain consumption is relatively stable, there was a 22MMT exportable grain surplus, as a result of the 2013/14 bumper crop, representing a 67% increase over historical averages. This exportable surplus is 1.5 times greater than annual potash exports and is in line with annual Canadian coal exports.

CP moved a record volume of grain and grain products during the 2013/14 crop year. Volumes were up 21% over the three year average and up 16% over the previous record in crop year 2008/09. Figure 16 shows CP grain and grain products carload performance for the 2013/14 crop year and the first 13 weeks of the 2014/15 crop year. As shown, there was little demand during the first three weeks of the 2013/14 crop year and customer service requests were 16% below historical levels in August. As a result, during that period there was significant unused railway capacity. Between Weeks 4 and 18 of the 2013/14 crop year CP had a very strong performance, significantly exceeding the three year average each week. Extreme winter conditions then set in at the end of November and continued through the end of February.

During this 12 week period CP grain carloads were below the three year average for 7 weeks. Once the extreme winter conditions subsided,

CP moved a record volume of grain and grain products during the 2013/14 crop year.

CP resumed moving record volumes of grain. CP moved in excess of 26,000 cars a month over the summer months of 2014. It is clear that the winter of 2013/14 was a difficult one⁹. That said, the key characteristic of the 2013/14 crop year was the record size of its harvest¹⁰.

⁹ There were 49 days where temperatures were below -25 degrees. The 2013-14 North American cold wave was an extreme weather event extending from December 2013 to April 2014, and was also part of an unusually cold winter affecting parts of Canada and the Eastern United States.[6] The event consisted of 2 episodes, the first one in December 2013 and the second in early 2014, both caused by southward shifts of the North Polar Vortex (Polar Vortex). Record cold temperatures also extended well into March. The result impacted the broader North American economy, for example, the US experienced the highest number of flight cancellations in 25 years; Service at the Port of Thunder Bay started a month later due to widespread ice coverage on the Great Lakes; and over 7,000 homes in Winnipeg had frozen water and sewer pipes. The persistence of the temperatures below -25 degrees forced CP to shorten train lengths by approximately 20%, caused increased occurrences of broken rail, wheel breaks, CTC outages, motive power failures, and decreased train speed, which negatively impacted overall capacity

¹⁰ CP is of the view that additional capacity could be found with more 24-7, continued improvement in loading in inclement weather and additional port terminal investment.

FIGURE 16: 2013/14 CROP YEAR, CP WEEKLY GRAIN CARLOADS AS COMPARED TO THE THREE YEAR AVERAGE

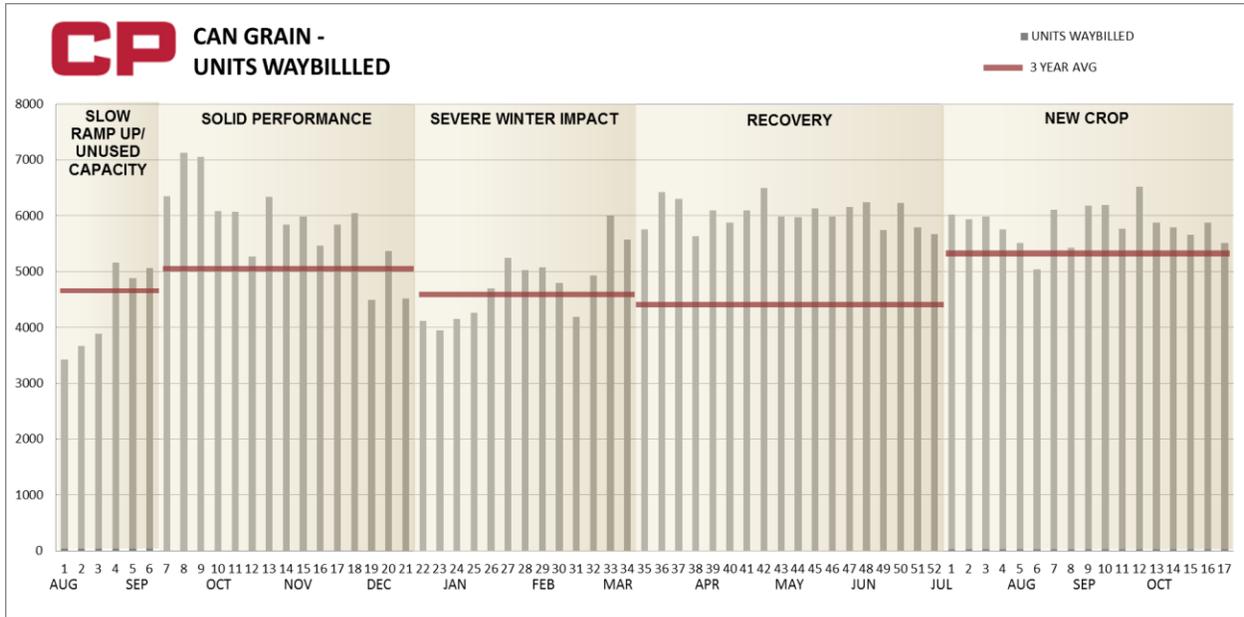
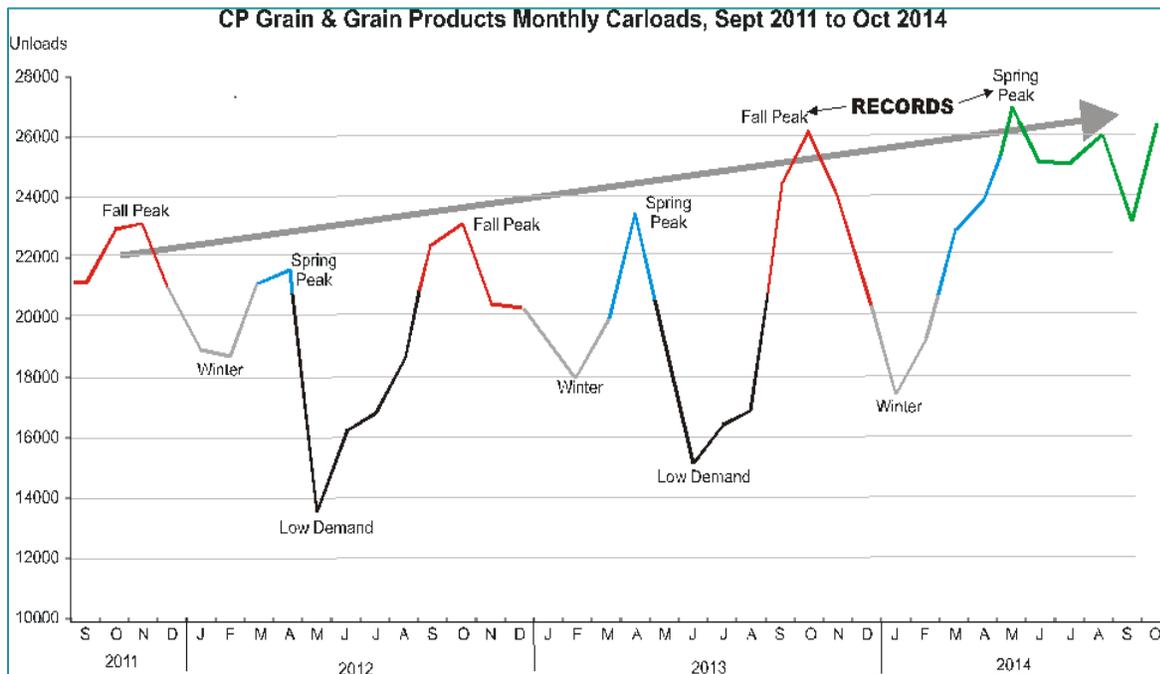


Figure 17 illustrates CP’s monthly western Canada grain and grain products carloads for the last three crop years. The chart demonstrates the cyclical nature of grain movements throughout the crop year and the ability of CP to respond with surge capacity to meet demand.

FIGURE 17: CP WESTERN GRAIN & GRAIN PRODUCTS MONTHLY CARLOADS, AUGUST 2011- SEPTEMBER 2014



Unlike manufacturing or mining facilities most of CP’s traffic offering for grain is very seasonal. Figure 14 depicts the annual peaks and valleys of monthly rail carloads in grain. There is a sharp fall peak where supply chain capacity is fully utilized. Winter grain volumes are lower due to the closing of the Port of Thunder Bay which is a major outlet for Canadian grain. Following the reopening of Thunder Bay there is spring peak followed by a decrease in demand when there is excess supply chain capacity at which point CP stores a large portion of the grain hopper car fleet, typically May to August each year.

The 2013/14 crop year was unique in the fact that we had a record grain crop and one of the coldest winters in recorded history, which resulted in exceptional demand for grain service through the spring and summer months of 2014. Given the strong grain supply chain performance and the fact that this year's crop is anticipated to be -24% lower than last year CP expects that we will move the remaining backlog from the 2013/14 crop year and the majority of the 2014/15 crop by the spring of 2015. This will result in CP parking grain hopper cars, as is usual, in May 2015 and the grain supply chain returning to excess seasonal capacity until the Sept 2015 fall peak commences.

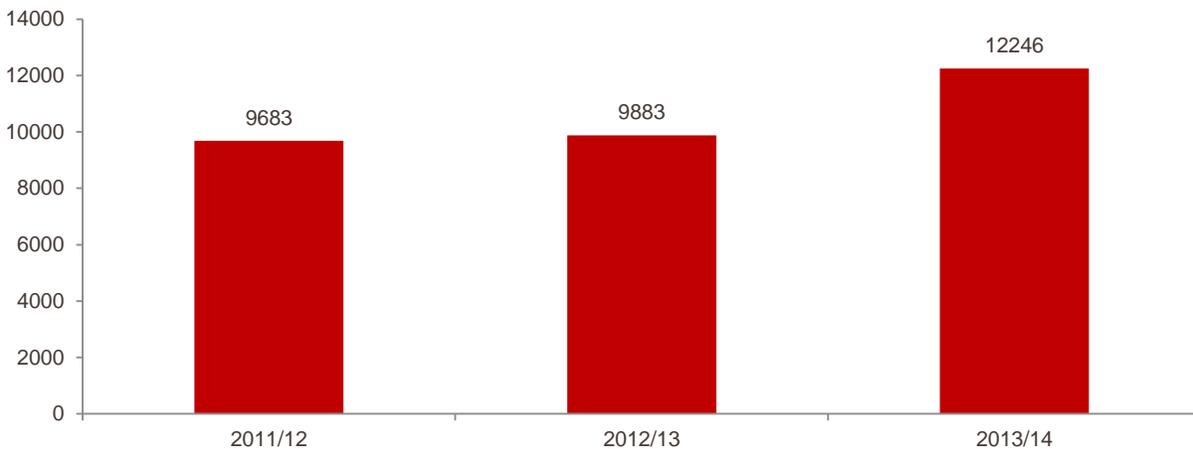
CP will be parking grain hopper cars, as is usual, in May 2015 and the grain supply chain returning to excess seasonal capacity until the Sept 2015 fall peak commences.

SERVICE TO GRAIN DEPENDENT SHORT LINES AND PRODUCER CAR SITES

CP serves 10 grain dependent short line railways in the provinces of Manitoba and Saskatchewan and over 60 producer car sites in Manitoba, Saskatchewan and Alberta. Producer cars are grain cars that are typically loaded by grain farmers.

CP provided high levels of service to grain dependent short line railways and producer car sites during the 2013/14 crop year. Over the last three crop years CP has moved increased grain volumes from short lines and producer car sites as volumes have increased by 24%, a record level. As shown in Figure 18, during the 2013/14 crop year we moved 12,246 carloads from short line and producers car locations. Producer cars represent about 4% of CP's total grain carloads originated in western Canada. Simply stated, service to our short line customers and local deliveries to producer car sites are not a problem.

FIGURE 18: CP GRAIN CARLOADS FROM GRAIN DEPENDENT SHORT LINES AND PRODUCER CAR SITES, CROP YEARS 2011/12-2013/14



CAPACITY OPPORTUNITY: 24-7 SUPPLY CHAIN

In order to increase the capacity of the grain supply chain we need the full supply chain, which includes in-land terminals and export terminals, to operate on a full 24-7 basis as railways do. Some terminals operate three shifts per day, five days a week while others operate two shifts per day, seven days a week. Only one terminal in Vancouver consistently operates on a true 24-7 basis.

In order to increase the capacity of the grain supply chain we need the full supply chain, which includes in-land terminals and export terminals, to operate on a full 24-7 basis as railways do.

Because of the absence of a true 24-7 supply chain for grain, a much higher percentage of cars get unloaded on weekdays versus weekend. Such unload patterns waste capacity as cars sit, cause congestion in important rail yards and create imbalances in flows. Recently, at times there has been a further deterioration in weekend loading. If we are going to compete within the global economy and grow Canada's grain supply chain capacity, we need a true 24-7

system in grain like we have in other innovative supply chains and at CP. Our analysis shows that by going to a full 365 24-7 grain supply chain in Canada's largest export gateway, Vancouver, an additional 25% or 5.2 MMT of grain could have been moved during the 2013/14 crop year. Given the record size of the crop, in the 2013/2014 crop year, with the exception of the first 6 weeks, the grain supply

chain was fully utilized over the entire year. Even in a normal crop year, a 365 24-7 grain supply chain would allow for greater throughput during the fall/winter peak. This operational

By going to a full 365 24-7 grain supply chain in Canada's largest export gateway, Vancouver, an additional 25% or 5.2 MMT could have been moved during the 2013/14 crop year.

change would increase productivity and provide additional capacity at low incremental cost.

Capacity can also be found by increasing innovation at existing and prospective terminals. As shown in Exhibit 1, in the United States Pacific North West (PNW), facilities that compete with Canada's west coast supply chain have loop track operations which greatly enhance the speed by which unit trains can be unloaded. One of these grain terminals processes as many as 600 rail cars daily. Currently, in Canada, grain cars are only unloaded individually or at best two at a time. This performance is inadequate when compared to the more efficient loop track unloading operation. Consequently, the largest grain terminal in Canada only processes about 180 rail cars daily. Unfortunately, given physical constraints in the Inner Harbour of Vancouver it is very difficult to build loop tracks. Over the medium to long term consideration must be given to new terminal capacity at locations that can accommodate innovations like loop tracks. Another area of innovation, as shown in Exhibit 2, is terminals that have permanent roof structures in order to permit loading in inclement weather. Some progress has been made on this issue in Vancouver with the implementation of through hole versus open hatch loading as well as with tarping systems but more can be done.

Exhibit 1: Dual Loop Track Operation



Exhibit 2: Permanent Roof Structure at Export Terminal



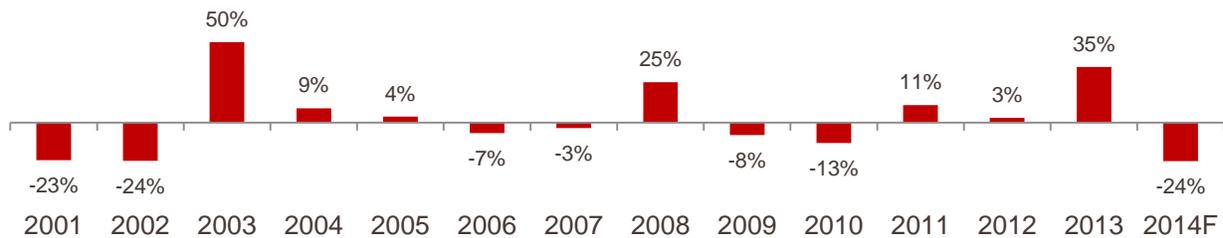
As for the future, CP anticipates continued year-over-year variability in Western Canada grain production. Figure 19 illustrates the significant variation in annual crop production between

2000–2014. Since year 2000, year-over-year variability in Western Canada grain production has been as high as +50% and as low as -24%. This year we are expecting the grain crop to be -24%

Since year 2000, year-over-year variability in Western Canada grain production has been as high as +50% and as low as -24%.

below last year’s crop. The nature and cost of railway resources makes it difficult to respond to extreme variations in demand for railway services.

FIGURE 19: YEAR-OVER-YEAR VARIABILITY OF WESTERN CANADA GRAIN PRODUCTION, 2001-2014



Sources: Statistics Canada, CANSIM Table 001–0010 and Agriculture Canada

In all of the circumstances any legislative or regulatory intervention that forces CP to move more grain at any particular time is totally unfounded either on the evidence or on sound policy. What is worse, any policy that supports this sort of intervention totally distorts adequate and sustainable rail freight networks because it runs the risk of sponsoring the special treatment of one type of customer to the detriment of all others.

CHAPTER 5

PRIORITIES FOR THE REVIEW

BILL C-30

In reaction to the demands by some, on May 29, 2014, the federal government enacted Bill C-30. The provisions contained in Bill C-30 sunset on August 1, 2016. The legislation gives the Governor in Council, on the advice of the Minister of Agriculture and Agri-Food, the ability to specify minimum weekly grain volumes to be moved by CP and CN; increases the interswitching limits in the prairie provinces from 30 km to 160 km for all commodities; gives the Agency the authority to order a railway to compensate customers for expenses incurred; and provides specific operational terms to be applied for a level of service determination. These provisions are actions of the federal government to further regulate the rail industry. They will not promote the investment and supply chain coordination that is needed to improve supply chain efficiency and capacity. As stated earlier, they introduce alarming distortions to CP's overall freight network while supposedly benefitting a vocal few.

The imposition of volume minimums for grain is an unprecedented action by the federal government in terms of dictating the operational and commercial practices of CP. Fortunately, CP was able to consistently exceed the grain volume minimums that were mandated through the government's Order in Council that was issued on March 26, 2014. Giving preference to a specific commodity is not only inconsistent with railway operating practices it is also inconsistent with national transportation policy which states "competition and market forces, both within and among the various modes of transportation, are the prime agents in providing viable and effective transportation services."

In terms of the interswitching extensions, this change is very problematic given as it grants US railroads a non-reciprocal access into our market without the corresponding right for Canadian railways to enter theirs. Furthermore, many of the regulated rates, as determined by the Agency, are non-compensatory and will not generate revenue that can support investment. The previous CTA Review looked at interswitching and determined, "expanding the interswitching limits would worsen the market-distorting aspects of the interswitching rate regime and would be a step backwards"¹¹.

Recommendation 1: CP recommends the Government respect the overarching transportation policy enacted by Parliament and not renew the anti-commercial provisions of Bill C-30 in 2016. Simply stated, they lack any sort of sound evidentiary or policy foundation.

¹¹ "Vision and Balance, page 63.

THE IMPACT OF CTA LEGISLATIVE PROVISIONS ON SUPPLY CHAIN CAPACITY AND SAFETY

Agency decisions, including Final Offer Arbitration (FOA) determinations and level of service (LOS) decisions are always taken in isolation. They fail to take into account the impact on anyone else along the rail freight bus route and, in many cases, cause public safety concerns. Nor do they consider the competitive alternatives a shipper may have.

The Agency has departed from any informed reasonability test in its assessment of LOS complaints. Going back to 1921¹² and until 2008¹³ it was an accepted approach that the railway's service obligation was not absolute; it always had to be tempered by reasonableness, always with particular reference to the facts of each case including the impact on a railway to provide service during peak cycles in demand. This approach, grounded in reasonableness and case specific facts, permitted and encouraged appropriate capacity decision-making in the short as well as for the long term. More recently this has changed with the Agency opining¹⁴ that the railways obligation was not to be tempered by weather or peak load demand. To the contrary, and departing from years of precedent by predecessors, the Agency found that the railway company is always obligated to purchase more assets\capacity in order to provide requisite service to all. In coming to this decision in a recent proceeding the Agency surmised that it was the railway's pursuit of a low operating ratio and its low investment levels under the MRE that was the reason for its rail freight service to the complainant.

The impact of this decision is significant. It will force a misallocation of resources and harm the overall network. It compels the railway company to invest in sufficient capacity to serve all shippers, wherever located and at any time without consideration of the facts or other reasonability factors such as peak load short term demand spikes. Most fundamentally it allows the Agency to force the railway to serve one customer in a way that is beneficial to that one customer and detrimental to others.

[Recommendation 2: CP recommends shipper remedy provisions in the CTA recognize:](#)

- [The network nature of the rail sector](#)

¹² Harris v. Quebec Central Railway Company (1921) 27 C.R.C. 447

¹³ CWB, North East Terminal Ltd et al v CN (Agency Decision No. 488-R-2008)

¹⁴ Agency decision Louis Dreyfuss Company v CN (unreported)

- The impact of a decision on other shippers
- The level of service for the purposes of S. 113 to S. 116 should be an average reasonable level of service taking into consideration the facts and circumstances in a given case
- Competitive alternatives available to a customer
- The timeframes for Agency decisions not be shortened

In another case, following the Lac Mégantic tragedy, CP suspended service to Montreal, Maine & Atlantic (MMA) traffic until the Transportation Safety Board (TSB) completed their investigation. This was done to protect public safety. CP wanted assurance that dangerous goods railcars on the MMA could be moved in a safe manner. However, MMA applied to the Agency to have the suspension lifted whereupon the Agency ruled¹⁵, expeditiously on August 21, 2013, during the early days of the TSB investigation, that CP must resume service to MMA, including moving railcars that contained dangerous goods. This decision represents a serious disconnect in the current regulatory framework. The Agency has no mandate whatsoever regarding the safety of rail operations and yet was unabashed in ordering a resumption of rail service on the MMA.

Recommendation 3: CP recommends that the Agency, in making a service order, should not ignore safety concerns

The Agency's involvement in service matters has increased significantly over the last few years. This has happened at a time when timelines for Agency adjudication has been shortened by its own initiative. Service matters are generally complex, network related and sometimes systematic. Having to reach decisions in a rapid manner without adequate and proper evidence and consideration is dangerous given the network/bus route nature of rail service, not to mention safety concerns.

Recommendation 4: CP recommends that the timelines for decisions on service matters under the CTA be maintained or lengthened

¹⁵ Agency Decision No. LET-R-99-2013

RATIONALIZATION OF LEGISLATIVE PROVISIONS

The *Canada Transportation Act* (CTA) has a long list of economic regulations that pertain to federally regulated railways. They include the following:

- Level of Service obligations
- Maximum revenue entitlement for western grain
- Final Offer Arbitration
- Regulated interswitching
- Competitive line rates
- Running rights and joint track usage
- Right of a shipper to challenge charges or terms that apply to more than one shipper
- Alternative Dispute Resolution–Voluntary and Regulated
- Mandated Service Agreement Arbitration
- Rail line discontinuance restrictions
- Railway liability regulations

The CTA recognizes that competition and market forces are the prime agents in providing viable and effective transportation services. We agree with this fundamental principle and recommend that those principles be validated and specifically reaffirmed as part of the 2015 review. The CTA also recognizes that regulation is a last resort when economic, safety, security, environmental or social outcomes cannot be achieved satisfactorily by competition and market forces. It can be reasonably implied that such regulation should only be resorted to the extent necessary to mimic competition and market forces which are the prime agents in the policy. Regulation is a last resort. The goal of regulation is not to shift economic power back and forth between railways and shippers, but rather to do the best it can to duplicate a competitive environment so that the efficiency of the entire transportation system is realized for the benefit of all Canadians – not individual shippers or railways. Both railways and shippers are incented by competition and market forces in order to survive and prosper and this should create viable and effective transportation services.

Regrettably there is a disconnect between the policy wording and actual regulatory action which can only be described as incremental, disjointed and uncoordinated. It is a classic case of regulatory creep. For example, Bill C-30 granted extended interswitching for all commodities in three western provinces. There are significantly more shippers who have access to two or

more railways – yet those same shippers have access to every single shipper remedy in the CTA. Rather than to simply “consider” or “have regard” to whether a shipper has effective competitive alternatives, the law would make it clear that additional remedies are not available to shippers who have reasonable competitive alternatives. The analysis of whether a shipper has competitive alternatives should be evidence based having regard to the specific facts of the case, not based on generalized and outdated historic assumptions – as is the case today.

Where shippers are truly captive, and captivity is not automatically determined by physical track connection to one railway, then the vast suite of shipper remedies (or some rationalized/coordinated version) ought to be available to those who have a demonstrated, evidence based need for protection.

This layering-on of legislative provisions is a result of various legislative reviews and one-offs. Many of the provisions are over lapping and are not efficient in addressing issues related to the commercial relationship between railways and their customers. For example, FOA has been used by shippers when they have clear competitive alternatives to move their traffic and even in cases where CP has only been the interchange carrier. Consideration should be given to a process to rationalize and simplify the legislative provisions available to customers prescribed by the CTA.

[Recommendation 5: CP recommends a rationalization of the legislative provisions available to customers prescribed by the CTA.](#)

MAXIMUM REVENUE ENTITLEMENT

In 2000, the Maximum Revenue Entitlement (MRE), which is administered by the Canadian Transportation Agency, was brought in to replace the Maximum Rate Regime. The MRE was initially deemed to be a transitional measure to the full commercialization of grain transportation. Under the MRE, railways have flexibility to set different rates (e.g. destination, car block size, etc.) as long as the total revenue earned in any particular year does not exceed the MRE. If a railway exceeds the MRE, in any year, a penalty is assessed and is paid to the Western Grains Research Foundation to promote research in agriculture. Shippers also have the right to challenge rates for transportation of grain by rail, using such shipper tools as Final Offer Arbitration. Grain shippers are also predominant complainants in level of service disputes before the Canadian Transportation Agency.

The MRE encompasses grain, including oils, meals, and consumer products, carried from points west of Thunder Bay or Armstrong, Ontario, to export positions at Vancouver and Thunder Bay. Any fees charged to grain customers, including fees for premium service, related to grain shipment are included under the MRE. Excluded under the MRE are soybeans and beet pulp, traffic originating in Canada to the US or to domestic locations, and grain to a port in BC for export to the US for domestic consumption. Also excluded are revenues from performance penalties, interswitching rates, switching fees, drayage, demurrage and industrial development funding.

The intent of the MRE is to put an effective cap on rail freight rates for grain and, therefore, to depress revenue earned by railways for the movement of grain. This is evident by the fact that CP's revenue/RTM for regulated grain is 3.7

cents/ton mile versus a system wide average for CP of 4.3 cents/ton mile. Since the introduction of the MRE the Volume Related Composite Price Index (VRCPI), that is used to calculate the annual change in the MRE, has increased slightly less than inflation. The

MRE combined with Final Offer Arbitration, level of service regulatory proceeding, and most recently the Bill C-30 provisions all layer on to give hyper regulatory attention to grain shippers.

Since the introduction of the MRE the Volume Related Composite Price Index (VRCPI), that is used to calculate the annual change in the MRE, has increased slightly less than inflation.

There have been two one-time adjustments to the MRE. When it was introduced the federal government reduced it by 20% in order to “remove productivity gains” from railways. The other adjustment occurred in 2007 (-5.4%) to reflect maintenance costs for the Government of Canada hopper car fleet. This was a concession to farmers after the federal government signed long term leases with CP and CN for the fleet versus giving the hopper cars to farmers.

In 2012, the federal government passed Bill C-18 “*An Act to reorganize the Canadian Wheat Board and to make consequential and related amendments to certain Acts*”, which removed the Canadian Wheat Board (CWB) as a sole marketer of western wheat and barley destined for export or for human consumption in Canada. The CWB played a predominant role in the grain supply chain dictating, for example, when and where the grain cars moved. CP now deals with the grain companies directly on matters related to the movement of all grains. The consequence is an overall improvement in supply chain performance.

Under a commercialized framework, the transportation market can be made more adaptive and responsive, as exists in the US grain business and all other Canadian commodities. A commercial market sends the right price signals with respect to investment in the system and how capacity is managed. Pricing mechanisms can respond to market conditions and price signals can also be used to manage how capacity is allocated.

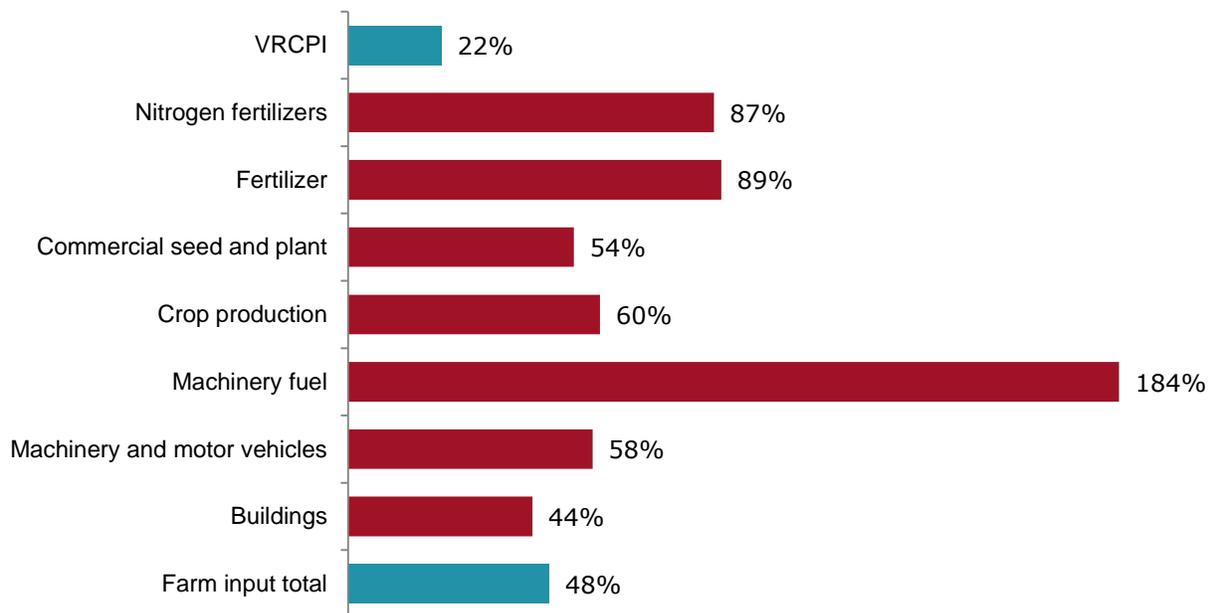
In US grain service the railway uses market mechanisms to align transportation decisions with the grain market. Car auctions are used to manage demand for grain capacity. The market determines demands and is responsive to needs of the shippers. Under such a system grain shippers can capture market

opportunities which improve their overall financial performance.

Unfortunately the regulated system in Canada does not allow for the use of such market mechanisms.

Unfortunately the regulated system in Canada does not allow for the use of such market mechanisms.

FIGURE 20: CHANGE IN FARM INPUT COSTS (2002 CONSTANT DOLLARS) VS CHANGE IN THE VOLUME RELATED COMPOSITE PRICE INDEX (VRCPI), 2002-2013



Sources: Statistics Canada, CANSIM Table 328-0015 & Canadian Transportation Agency
 Note: All items, excluding the VRCPI, are adjusted for inflation

Figure 20 compares the change of the cost of major farm inputs to increases in the MRE (as tracked in the VRCPI).

The base year of 2002 was chosen as it is the first year in the revised Statistics Canada Farm Input Price Index. The Index is based on constant 2002 dollars and 2002=100 for the Index.

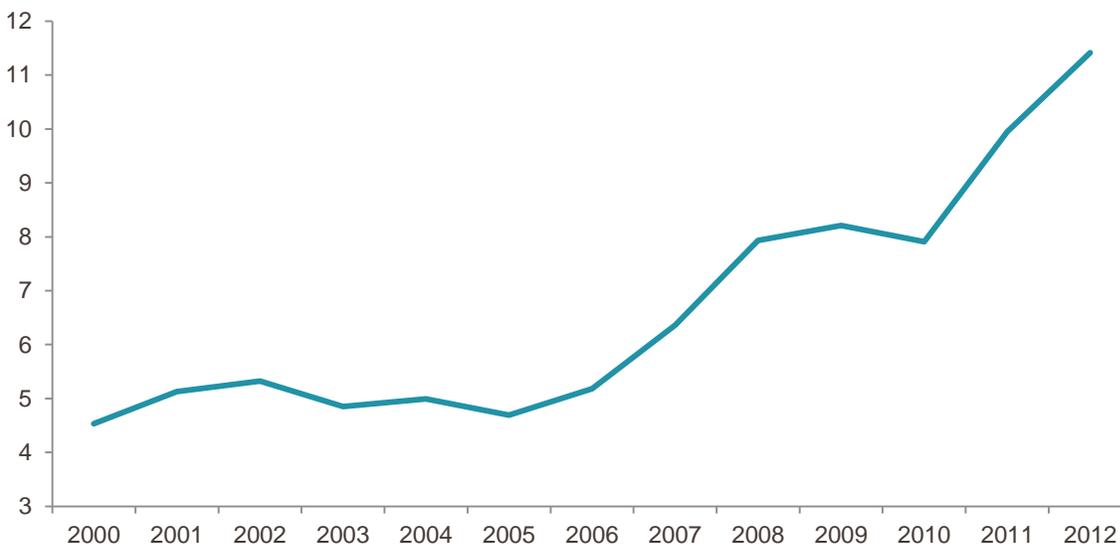
The growth in the VRCPI is for the crop years between 2002/03 to 2012/13. The VRCPI was 1.0 for the 2000/01 crop year and is adjusted annually by the Canadian Transportation Agency to reflect changes in railway costs and is used to determine the revenue cap for the movement of western grain.

Overall, farm inputs have increased 48% over the 2002-2013 time period, twice the rate of the VRCPI. The rail portion of the movement of grain is increasingly becoming a lower cost component, and is not a significant cost driver in the production and

Overall, farm inputs have increased 48% over the 2002-2013 time period, twice the rate of the VRCPI.

movement of grain.

FIGURE 21: OILSEED AND GRAIN FARM TOTAL INCOME (\$BILLIONS), 2000-2012



Grain and oilseed farm incomes have experienced tremendous growth between 2000–2012. Total farm income for the oilseed and grain sector increased 153% from \$4.5 billion to \$11.4 billion¹⁶. Growth in total farm income has been primarily driven by the significant increases in grain prices, growth in yield per acre, the size of the harvested area, and productivity growth. Grain and oil seed prices have

increased by 85%¹⁷, the average yield per acre increased 13%¹⁸, the size of the harvested area increased by 16%¹⁹, and productivity experienced 24%²⁰ growth. Given the size of grain and

oilseed farm income, the claim made by various farm industry groups, which was widely reported²¹, that they lost \$7–\$8 billion in lost sales during the 2013/14 crop year is not supported by facts.

Grain and oilseed farm incomes have experienced tremendous growth between 2000-2012. Total farm income for the oilseed and grain sector increased 153% from \$4.5 billion to \$11.4 billion.

¹⁶ Statistics Canada, CANSIM Table 002–0035

¹⁷ Statistics Canada, Farm Product Price Index, CANSIM Table 002–0068

¹⁸ Statistics Canada, CANSIM Table 001–0010

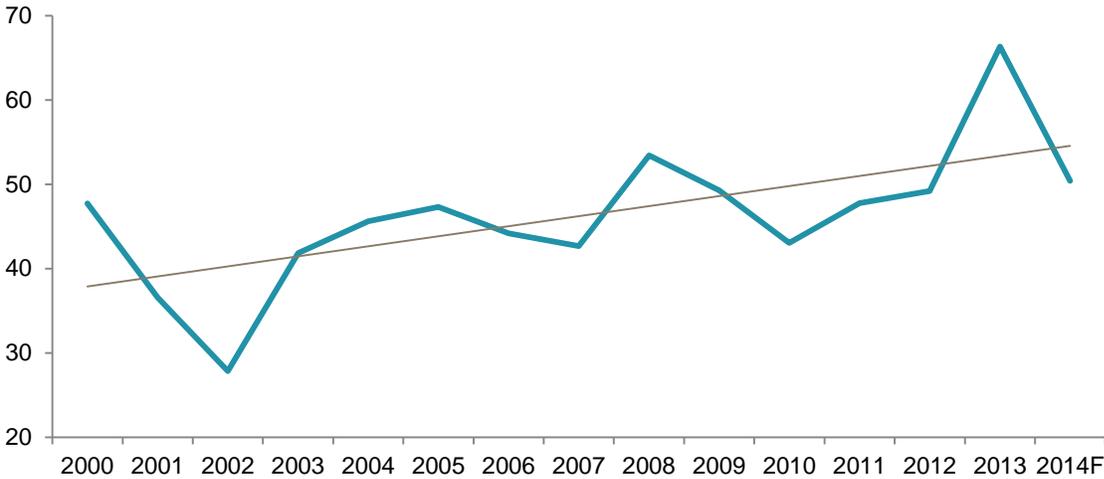
¹⁹ Ibid.

²⁰ Statistics Canada, CANSIM Table 383–0021

²¹ Regina Leader–Post, “Farm groups, industry differ on CTA review of grain transportation backlog”, October 27, 2014.

CP expects that the production of grain will continue to increase into the future, with long term annual production growth of 2–3% annually. The trend line in Figure 22 depicts the production growth over the 2000–2013 time period. Given that domestic consumption of grain and grain products is relatively stable, growing in line with population growth, increased production will have to be moved to export position.

FIGURE 22: WESTERN CANADA PRODUCTION OF PRINCIPAL FIELD CROPS (MILLION METRIC TONNES) 2000-2014F



Source: Statistics Canada, CANSIM Table 001–0010 and Agriculture and Agri–Food Canada Crop Forecast

The removal of the MRE would allow for increased investment, capacity, and overall competitiveness in the grain supply chain. One of the most significant opportunities for investment, to increase capacity and efficiency in the grain supply chain, but one which the MRE inhibits, is the replacement of the

Government of Canada (GoC) hopper cars. Figure 23, outlines the age profile of CP’s GoC hopper cars. Overall, CP has 5,567 GoC hoppers and the average age of the fleet is 35

New hopper cars are shorter than the GoC hoppers which allows for additional cars to be hauled on either a grain unit train or a manifest train and they also have a higher load capacity.

years. They are nearing the end of their useful life, which is approximately 40 years.

New hopper cars are shorter than the GoC hoppers which allows for additional cars to be hauled on either a grain unit train or a manifest train and they also have a higher load capacity. The

maximum length of trains is primarily constrained by the length of rail sidings. It should be noted that CP has and continues to undertake considerable investments in building longer sidings and extending the length of current sidings. Table 1 outlines the capacity opportunity per unit train by using new hoppers versus GoC hoppers. Overall, new hoppers allow for 23.4% more capacity, by tonnes of grain, per unit train as compared to GoC hoppers. Also, new hoppers allow for quicker unloading at export grain terminals which allows for further capacity improvement in the grain supply chain. Table 2 demonstrates the annual capacity opportunity, by tonnes, from replacement of GoC hopper cars. Overall, new hoppers can carry an additional 3.859 million metric tonnes per year versus the GoC hopper cars.

The MRE effectively prevents CP from replacing the GoC hopper car fleet. A commercialized system would allow CP and other grain supply chain partners to purchase new hopper cars which would significantly increase the capacity of the grain supply chain.

Recommendation 6: CP recommends removal of the MRE and the full commercialization of grain transportation

FIGURE 23: AGE PROFILE OF THE CP GOVERNMENT OF CANADA HOPPER CAR FLEET BY YEAR BUILT

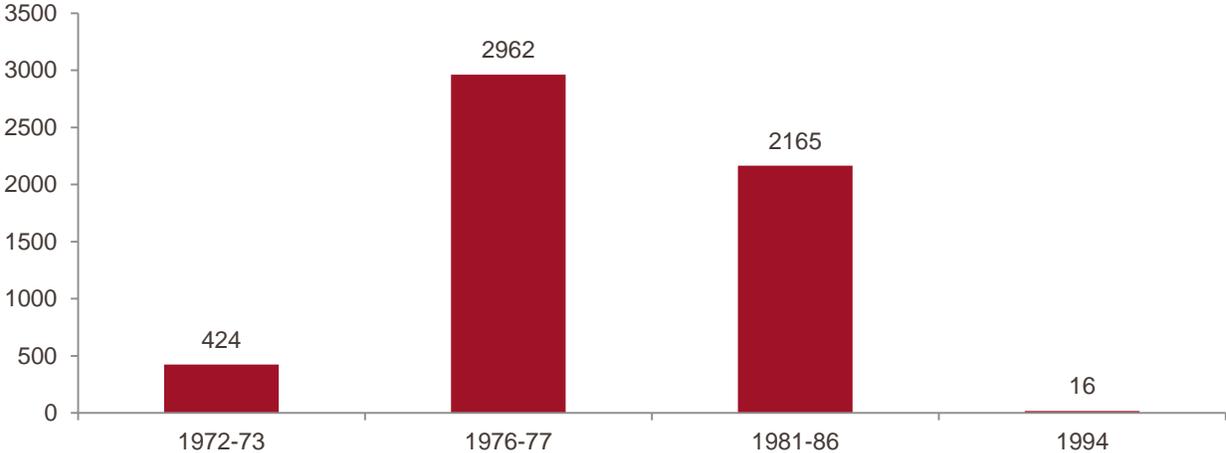


TABLE 1: GRAIN UNIT TRAIN CAPACITY OPPORTUNITY, GOVERNMENT OF CANADA HOPPER CARS VS NEW HOPPER CARS

	GoC Hopper	New Hopper
Length of train (cars only) in feet	6608	6608
Load limit (tonnes)	93	101.2
Length (feet)	59	53
Maximum cars/unit train	112	127
Maximum total load (tonnes)	10,416	12,852
Capacity opportunity (tonnes/train)		2,436
Capacity opportunity (carloads/train)		15
Capacity opportunity (%)		23.4%

TABLE 2: ANNUAL CAPACITY OPPORTUNITY OF REPLACING THE GOVERNMENT OF CANADA HOPPER CARS WITH NEW HOPPER CARS

	GoC Hopper	New Hopper
Number of cars	5567	5567
Potential Number of Unit Trains	50 (112 cars/unit trains)	44 (127 cars/unit train)
Potential Annual Turns (3/month)	36	36
Additional Tonnage per Turn		2,436
Additional Annual Tonnes (million)		3.859 MMT

CANADA/U.S. REGULATORY HARMONIZATION

As is the case with the North American economy, the railway system in North America is highly integrated. Over 33% of CP's traffic crosses the Canada/US border. CP is supportive of efforts being taken by the US federal government and the Government of Canada, through the Beyond the Border Initiative and the Regulatory Cooperation Council, to further improve border processes and harmonize regulations, to improve the competitiveness of the North American economy.

CP has extensive operations in Canada and the US and interchanges traffic with all other North American Class I railways as well as numerous short line railways on a daily basis. Given the highly integrated nature of the railway industry, regulations related to equipment and operating practices should be harmonized while ensuring a high level of safety standards.

A current example of where both Canada and US governments should be working together in cooperation with industry is in the development of new tank car standards for the movement of dangerous goods. The rail industry fully supports new standards that will improve the overall integrity of the tank car and will mitigate the risk to public and the environment in the event of an accident. However, the standard, once developed, should be the same in Canada and in the US. Given that tank cars move between Canada and the US, having in place different tank car standards will not allow for optimal use of the tank cars thus increasing the cost to shippers that require tank cars to deliver their product to market.

[Recommendation 7: CP recommends transportation policy in Canada be harmonized with the United States](#)

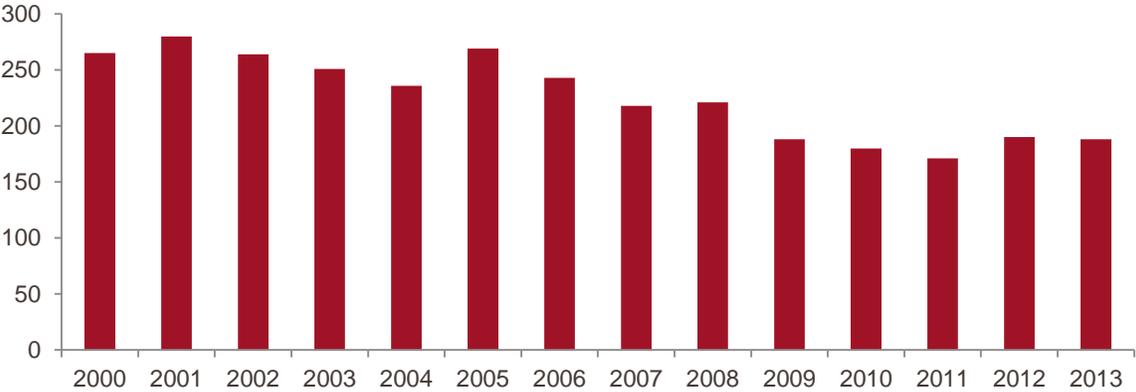
TRESPASSING, GRADE-CROSSING ACCIDENTS, AND ENCROACHMENT

There have been numerous reports and recommendations identifying a need to deal with municipal planning and encroachment, trespassing, and grade-crossing accidents, all of which, if addressed appropriately, will significantly improve rail and public safety.

We have and will continue to work with municipal leaders to improve public safety. However, all levels of governments and the public at large have to recognize that this is not an issue that the railway can solve alone.

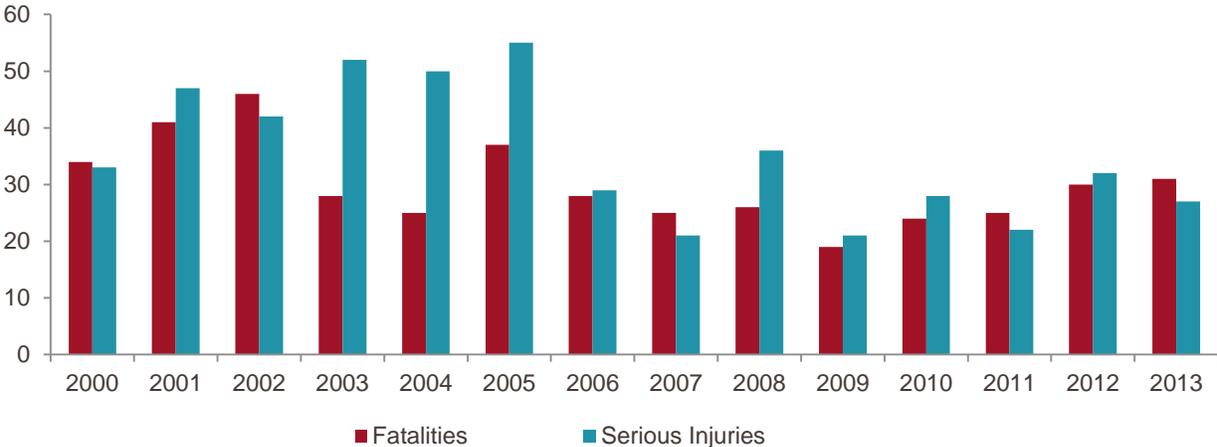
Railway crossing accidents are one of the top causes of accidents, and represent the greatest risk to human life and serious injury. Despite industry and government efforts to educate the public on the hazards associated with rail crossings, investments in rail crossings, and implementation of various safety enhancing regulations, the number of crossing accidents are on the rise in 2012 and 2013. This is shown in Figure 24. Further, as depicted in Figure 25, over 40 percent of crossing accidents result in a fatality or serious injury. The increase in crossing accidents is primarily due to the proliferation of level crossings combined with increases in road and rail traffic volumes.

FIGURE 24: NUMBER OF CROSSING ACCIDENTS, 2000-2013



Source: Transportation Safety Board

FIGURE 25: NUMBER OF CROSSING ACCIDENTS AND SERIOUS INJURIES, 2000-2013



Source: Transportation Safety Board

Transport Canada supports and funds the closing of crossings. While Transport Canada is on record of encouraging the closure of rail crossings and discouraging new ones, the Agency is in the business of doing just the opposite. The Agency's regulated approach is to grant all private crossing requests (s. 102 CTA – often referred to as 'farm crossings'), even though the resultant crossings are not private at all. Rather they are de facto public. These crossings are public ones due to ongoing transit by vehicles for various public uses e.g. cottages and cottage associations, shopping complexes and industrial parks. An example of this is the 2013 case in *Creekside Developments v. CP* where the Agency ruled that CP must construct and pay for a farm crossing but had to make it suitable for land development purposes. The Agency ignored CP's concerns about impact on train efficiencies and speeds coming out of the Toyota car plant and ruled that a 'private' crossing, irrespective of its broad public use, should be installed and maintained at CP's expense.

The federal government should act to correct the inconsistent regulatory regime that exists in Canada and to quell the Agency's predisposition to grant all crossing application.

As it stands, the Agency opens crossings based on private and municipal transit interests without due consideration to either the impact on railway capacity or public safety, while another, Transport Canada, regulates the overall safety of crossings. In one case the Agency ordered CP to open a crossing just after Transport Canada had ordered it permanently closed for safety reasons²². Canada needs a reinvigorated approach to consolidate and reduce the number of crossings, then apply appropriate protection to those that remain.

Recommendation 8: CP recommends that the Minister of Transport have the sole authority to approve new crossings and should only do so as an option of last resort upon evidence of clear need and adequate safety. In the event of a new crossing opening an existing crossing should be closed so that there is no net increase in the number of crossing. The overall goal should be to reduce the number of crossings which will benefit overall public safety.

LOCOMOTIVE VOICE AND VIDEO RECORDINGS

The most significant opportunity to greatly reduce risk, improve safety, and assist in post-incident investigations is the deployment of Locomotive Voice and Video Recorders (LVVRs). This technology is readily available and has proven to reduce accident rates, notably in public

²² Agency Decision No. 485-R-2004

transit. CP is prepared to invest in and install LVVR technology if it can be used to improve safety proactively. The use of this technology would have an immediate effect on enhancing a culture of safety and accountability in the rail sector, an action that will save lives. However, under the current legislative regime, on-board recordings are privileged and can only be used for post-occurrence investigations by the Transportation Safety Board (TSB).

Opponents of taking this important step forward in rail safety are concerned about how railways would use the information. They say employees have a right to privacy while at work and recordings would be used for disciplinary purposes. CP is firmly of the view that the need to prevent accidents outweighs these concerns. CP is also prepared to implement procedures that would ensure LVVR information must be tightly controlled and only used within strict guidelines.

Responsible, controlled, risk-and-incident-based review of LVVR data will add to existing compliance processes and promote a safety culture and accountability. Evidence shows that these systems increase industry operating rules compliance and reduce tendencies toward behaviours that erode safe operations.

Currently, on-board recordings are privileged and can only be used for post-occurrence investigations by the TSB. Therefore, legislative change is required in order for railways to be able to use this technology to prevent accidents and increase safety.

[Recommendation 9: CP recommends that the federal government undertake the necessary legislative changes to allow railways to use Locomotive Voice and Video Recorders \(LVVRs\) to proactively improve safety.](#)

NOISE & VIBRATION

Poor urban planning contributed to and also resulted in significant encroachment and interference with rail operations, as well as a rise in trespassing incidents and accidents. CP receives many public complaints associated with operations, namely noise and vibration. In response, we attempt to resolve or mitigate the concerns raised in a manner that does not compromise the safety of our operations or impact other citizens. In some cases complaints are filed with the Agency for a decision under the relevant provisions of the CTA. Both CP and CN have seen recent decisions where locomotive operations, including engine idling, have been curtailed during nighttime hours and expansion plans have been stalled due to noise and

environmental concerns voiced by a few local residents without consideration of operational and safety impacts. In many cases the ruling results in the relocation of rail activity that in-turn impacts others as well as having negative impacts on the safety and efficiency of rail operations. There needs to be a balanced fact-based approach to these determinations so that collaborative and cost-effective solutions can be found. Only this will allow railways to continue to operate in the national interest to support Canada's trade economy and quality standard of living. CP cannot stress enough the safety impacts must be a consideration in these determinations. In one case the Agency did not consider safety impacts before it ordered CP to relocate aspects of its yard operations.

95.3 (1) On receipt of a complaint made by any person that a railway company is not complying with section 95.1, the Agency may order the railway company to undertake any changes in its railway construction or operation that the Agency considers reasonable to ensure compliance with that section.

Section 95.1 is as follows:

95.1 When constructing or operating a railway, a railway company shall cause only such noise and vibration as is reasonable, taking into account

- (a) its obligations under sections 113 and 114, if applicable;
- (b) its operational requirements; and
- (c) the area where the construction or operation takes place.

A significant omission in Section 95.3 is that the Agency need not consider the impact on safety in their decision. The Agency is only compelled to consider if a railway is in compliance with Section 95.1.

[Recommendation 10: CP recommends that the Canadian Transportation Agency assess the impacts on operations and safety in decisions related to noise and vibration.](#)

SUMMARY

CP appreciates this opportunity to file a submission under the auspices of this important review. We look forward to additional follow-up and dialogue over the coming months as you work towards your December 2015 deadline. The broad thrust of this submission is that since 1996 there has been a creeping re-regulation of the freight rail industry in Canada. The result is a proliferation of overlapping and ad hoc, often sector specific regulatory provisions, which can benefit a few shippers to the detriment of most. The resulting regulatory interventions are random, unpredictable and in many cases arbitrary all of which run counter to rail freight system safety and efficiency

ANNEX I

SUMMARY OF RECOMMENDATIONS

ANNEX I: LIST OF RECOMMENDATIONS

Recommendation 1: CP recommends the Government respect the overarching transportation policy enacted by Parliament and not renew the anti-commercial provisions of Bill C-30 in 2016. Simply stated, they lack any sort of sound evidentiary or policy foundation.

Recommendation 2: CP recommends shipper remedy provisions in the CTA recognize:

- The network nature of the rail sector
- Competitive alternative available to a customer
- The timeframe for Agency decisions not be shortened

Recommendation 3: CP recommends that the Agency, in making a service order, should not ignore safety concerns

Recommendation 4: CP recommends that the timelines for decisions on service matters under the CTA be maintained or lengthened

Recommendation 5: CP recommends a rationalization of the legislative provisions available to customers prescribed by the CTA

Recommendation 6: CP recommends removal of the MRE and the full commercialization of grain transportation

Recommendation 7: CP recommends transportation policy in Canada be harmonized with the United States

Recommendation 8: CP recommends that the Minister of Transport have the sole authority to approve new crossings and should only do so as an option of last resort upon evidence of clear need and adequate safety. In the event of a new crossing opening an existing crossing should be closed so that there is no net increase in the number of crossings. The overall goal should be to reduce the number of crossings which will benefit overall public safety.

Recommendation 9: CP recommends that the federal government undertake the necessary legislative changes to allow railways to use Locomotive Voice and Video Recorders (LVVRs) to proactively improve safety.

Recommendation 10: CP recommends that the Canadian Transportation Agency assess the impacts on operations and safety in decisions related to noise and vibration.