

## **THE DISCLOSURE OF RAIL CARRIER COSTING INFORMATION**

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### **Introduction**

The widespread adoption of confidential contracting following its introduction into Canadian railway law in the *National Transportation Act, 1987*, has resulted in a significant reduction in rail carrier freight rate information. Consequently, shippers have little basis on which to assess the reasonableness of freight rate levels, particularly in respect and to the extent of captive traffic. Unfortunately, published railway tariffs are unhelpful as they may, and often do, overstate the actual rates paid, sometimes on account of undisclosed rebates or, more often, because little or no traffic is shipped under those tariffs, either because of the excessive level of the rates or the inferiority of the levels of service associated with the rates, or both. A railway company, on the other hand, possesses all of the rate information in respect of traffic it carries, subject to some exceptions of little relevance here. This asymmetry of accurate rail freight rate information is harmful to shipper interests and to the economy overall, particularly where supra-competitive pricing or sub-competitive service conditions or levels prevail. In the absence of comparable rail rate information, one of the few means available to assess the reasonableness of rates is by reference to rail costs. Therefore, shipper access to reliable rail carrier costing information is all the more critical, particularly with respect to individual shipments between origin and destination pairs (“O/D Pairs”).

### **Examples of Rail Freight Tariff Rates**

There are two rate mechanisms in the *Canada Transportation Act* (the “Act”) pursuant to which a rail carrier may transport traffic: tariffs and confidential contracts.

Tariffs must be published.<sup>3</sup> They may contain freight rates in respect of multiple or single O/D Pairs. Although it most often will object, a rail carrier is obligated to issue a tariff in respect of traffic on its railway upon the request of a shipper.<sup>4</sup> Once a rail carrier issues and publishes a tariff of rates for the movement of traffic in accordance with the requirements of the Act, whether of its own volition or because it has been compelled to do so by order of the Canadian Transportation Agency (the “Agency”), those rates “are the lawful rates of the railway company”.<sup>5</sup> The level of the rate is not a subject of negotiation; on the contrary, it is a unilateral declaration. If a rail carrier proposes to increase a rate in a tariff for the movement of traffic, it must publish a notice of the increase at least thirty days before its effective date.<sup>6</sup> The only avenue to contest the rate is final offer arbitration (“FOA”), which is rarely used.

Confidential contracts contain freight rates that are, as the term expresses, confidential between the parties to the contract.<sup>7</sup> They may contain other terms and conditions such as shipper and rail carrier commitments in respect of service levels, traffic volume, ancillary charges, commercial dispute resolution, rate adjustment mechanisms, among others. Rates in confidential contracts are not subject to FOA.

At least one Canadian rail carrier has taken the view that the Act permits a rail carrier to issue hybrid documents, commonly referred to as limited distribution tariffs (“LDTs”), each of which is typically applicable to a single shipper.<sup>8</sup> The rail carrier also asserts that LDTs are confidential and need not be made publicly available.<sup>9</sup> The Agency has undertaken a consultation in respect of LDTs, and received several submissions, but has not yet made any pronouncements on the status of LDTs under Canadian law.<sup>10</sup>

### **Comparable Rates**

Comparable rail freight rate information is scarce. When assessing the reasonableness of rail freight rates in respect of an O/D Pair, the starting point tends to be a shipper's prior rate with the same rail carrier in respect of that O/D Pair, provided such rate exists. Secondly, if a shipper has rates in respect of the movement of traffic other than the subject movement with the same rail carrier, such rate information can be useful, whether or not added to other information.

Further, in the relatively rare case in which a shipper uses the services of another rail carrier to ship or receive goods, either at the subject origin or other locations, the other rail carrier's freight rates might form a basis for comparison. However, if the rail freight rates for the other movements are contained in one or more confidential contracts, such rates could not be disclosed to the rail carrier for the relevant O/D Pair, which could be very useful in a negotiation, but of limited utility in FOA proceedings.

Occasionally, rail freight rate information might be disclosed in reported accounts of other shippers' rates. For example, if a shipper's continuous disclosure obligations are discharged in such a way as to include isolated distribution costs, and if one could reasonably estimate certain other information embedded in those distribution costs, one might be able to reasonably estimate the shipper's rail freight rates. On occasion, this approach yields reasonably good rate information. Similarly, a rail carrier might disclose average or aggregated rates for a commodity group that could allow for the testing of rate estimates.

One other source of potentially useful rail freight rate information is comparative rate studies. However, such studies invariably aggregate the source data such that no information can be isolated in respect of particular movements, and accordingly such data tends to be of limited utility.

### **Comparing \$/RTM**

Rail carriers, who are possessed of many data points and all information regarding rates on their networks, enjoy the luxury of demonstrating the reasonableness of their rates when they feel compelled to do so, such as in some FOA settings, by comparing the monetary value of freight carried over distance. The most common measure is revenue per tonne mile or RTM, which is the amount of revenue generated by a rail carrier by moving one tonne of freight one mile and is generally expressed as cents per RTM (“CRTM”).

Shippers’ lack of access to reliable comparable rail freight rate data makes for one-sided negotiations. A carrier, with unlimited access to its rate information, enjoys a tremendous advantage over a shipper, whose data is limited to its own and possible estimates of others. That advantage carries over into the only means of contesting rates, namely, FOA. That problem is compounded by the use of misleading metrics, including in particular CRTM. Cents per RTM comparisons can be meaningful, but only when comparing similar movements.

For instance, Item 1010000-AA of CN Tariff 512737-AG sets out freight rates for transportation of various chemical products on CN.<sup>11</sup> Specifically, that tariff sets out a rate of \$3,675 per railcar for transportation from North Vancouver, British Columbia to Kamloops, British Columbia (a rail distance of approximately 460 miles) and a rate of \$10,500 per railcar for transportation from North Vancouver, British Columbia to Toronto, Ontario (a rail distance in excess of 2,600 miles). Assuming for ease of calculation that each railcar contains 100 tonnes of product, the North Vancouver to Kamloops rate produces a value of approximately \$0.08/RTM (8.0 CRTM), while the North Vancouver to Toronto rate produces a value of approximately \$0.04/RTM (4.0 CRTM).

As a general rule, because long haul movements are more efficient than shorter movements, they typically warrant a proportionally lower average freight rate on account of such efficiencies. Long haul movements are generally more efficient than corresponding short haul movements because the more costly first and last mile of each

movement is proportionally less costly on a per mile basis. Thus, in the foregoing example comparing O/D Pairs in CN Tariff 512737-AG, all that we learn is that movements over a greater distance enjoy a lower CRTM.

In addition to distance, factors relevant to an RTM analysis may, though not necessarily, include the degree of similarity of the movements in respect of characteristics such as terrain and weather conditions traversed, the type of commodity transported, unit train versus carload traffic, type of equipment used, whether any portion of the respective rail routings are shared, and other factors.

Rail carriers often quote units of cents per RTM in various public disclosure materials as justification for rate levels. For instance, in support of the proposition that Canadian railways offer “some of the lowest freight rates in the world” the Railway Association of Canada (“RAC”) published the figure reproduced below:



Source: *Rail Trends 2012*, as published by the RAC.<sup>12</sup>

The RAC characterized the figure as representing “Canada’s freight rates throughout the last five years compared to most of the world’s largest economies” and it is evident that the countries can be coarsely grouped into high cents per RTM countries and low cents per RTM countries, with Canada falling within the latter.<sup>13</sup> When interpreting CRTM figures, it is important to note that the average distance travelled for each country is exactly as important to the expressed cents per RTM value as the average revenue figure. However, in respect of the above figure, the RAC provides no information as to the average length of haul in each country, thus rendering any comparisons essentially meaningless. Since Canadian rail carriers routinely transport bulk commodities such as grain, coal, potash, and others many hundreds of miles from origin to destination, they will

necessarily have a disproportionately longer average length of haul relative to countries such as Germany and Japan, whose land mass simply would not allow for movements of such length. The RAC figure has simply identified large countries that would contain relatively long rail movements, thereby obfuscating any meaningful revenue information. In other words, they have solved for distance, not rates.

### **Uses of Rail Carrier Costing Information**

Given the lack of access that shippers have to useful comparable rail carrier rate data, and given the lengths to which rail carriers will go to justify their rate levels, including misleading data such as the above figure, access to accurate and reliable rail carrier costing data is all the more critical as a means to evaluate the reasonableness of a rate for an O/D Pair.

Shipper access to accurate rail carrier costing data disaggregated to individual accounts is vital to shipper interests in various circumstances. A shipper that is party to a negotiation or FOA requires an Agency determination of the rail carrier's long run variable cost of a relevant O/D Pair.<sup>14</sup>

Also, regulated interswitching is a widely used shipper protection mechanism, the rates for which are dependent on an accurate determination of rail carrier variable costs in respect of switching movements.<sup>15</sup> Competitive line rates, a remedy that has been declared inoperative in practice, are set by the Agency using a variety of information sources, including accurate determinations of rail carrier variable costs.<sup>16</sup>

Furthermore, the large volume of Canadian rail freight traffic that is subject to the rail carriers' maximum revenue entitlement for the movement of western grain is impacted by the accurate determination of railway costs by the Agency. That is because the Agency's determination of the volume-related composite price index, which is used to determine the rail carriers' maximum revenue entitlement for the movement of grain in a crop year, which in turn indirectly affects

rates paid by grain shippers, is impacted by the interpretation of the UCA (as defined below).<sup>17</sup>

### **Sources of Rail Carrier Costing Information**

Federally-regulated rail carriers are currently obligated to disclose certain data as prescribed by the Agency.<sup>18</sup> The data required is prescribed in various regulations and specified in the Uniform Classification of Accounts (“UCA”).<sup>19,20</sup> The stated purpose of the UCA is “to define the method of accounting for railways subject to regulation by the Canadian Transportation Agency” and provides accounting instructions and the framework of accounts for the rail operations of such carriers.<sup>21</sup> The UCA also provides instructions for the recording of operating statistics and defines the categories for such data.<sup>22</sup> The Agency has recently initiated a consultation with interested stakeholders in respect of certain proposed changes to the UCA.<sup>23</sup>

Another publicly available document that was useful to shippers seeking to estimate rail carrier costs is “Rail in Canada” published by Statistics Canada.<sup>24</sup> Rail in Canada formerly contained financial and statistical data disaggregated into individual accounts based on the UCA. Stats Canada has indicated that it will discontinue this publication beginning with data in respect of 2010 because one of the railways declined to provide the required permission to publish the data.

### **The U.S. Approach**

In the United States, rail carriers are required to report and publicly disclose detailed financial and statistical data (disaggregated to individual accounts), which are made available on the website of the Surface Transportation Board (“STB”).<sup>25</sup> Notably, both CN and CP are required to provide these reports to the STB in respect of their United States operations.

Furthermore, the STB has established a railroad general purpose costing system known as the Uniform Rail Costing System

(“URCS”). URCS is used by the STB in connection with its statutory functions, but is also intended “to provide the railroad industry and shipper with a standardized costing model”.<sup>26</sup>

The data supplied to URCS allows shippers to apply rail carrier unit costs to user-defined rail carrier shipments.<sup>27</sup> This permits shippers to readily assess U.S. rail freight rate competitiveness, much to the credit of the URCS system.

### **Conclusion**

In order to support the competitiveness of Canadian shippers, and the broader Canadian economy, Canada should move towards the elimination of barriers to the disclosure of rail carrier costs, for individual shipments in particular, and implement mechanisms to allow shippers in Canada access to the same quantity and quality of information available to shippers using CN and CP’s services in the United States. Keeping this information confidential only serves to preserve or enhance market power, contrary to the most basic principles of a market economy.

## Endnotes

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- <sup>3</sup> *Canada Transportation Act*, S.C. 1996, c. 10, ss 117-120.1 govern rail carrier tariffs.
- <sup>4</sup> *Canada Transportation Act*, S.C. 1996, c. 10, s 118.
- <sup>5</sup> *Canada Transportation Act*, S.C. 1996, c. 10, ss 119(2).
- <sup>6</sup> *Canada Transportation Act*, S.C. 1996, c. 10, ss 119(1).
- <sup>7</sup> *Canada Transportation Act*, S.C. 1996, c. 10, s 126 governs confidential contracts.
- <sup>8</sup> For example, see the submission of Canadian National Railway Company (1 March 2011) in the Canadian Transportation Agency's Consultation in respect of "Limited Distribution Tariffs in Railway Transportation" announced on July 21, 2010, accessed online on February 28, 2013: <[http://www.otc-cta.gc.ca/sites/all/files/consultations/CN%20Response%20Letter%20to%20CTA%20DT%20Discussion%20Paper\\_1.pdf](http://www.otc-cta.gc.ca/sites/all/files/consultations/CN%20Response%20Letter%20to%20CTA%20DT%20Discussion%20Paper_1.pdf)>
- <sup>9</sup> *Ibid* at 2.
- <sup>10</sup> Canadian Transportation Agency's Consultation in respect of "Limited Distribution Tariffs in Railway Transportation" announced on July 21, 2010, accessed online on February 28, 2013: <<http://www.otc-cta.gc.ca/eng/consultation/limited-distribution-tariffs-railway-transportation>>
- <sup>11</sup> Canadian National Freight Tariff 512737-AG, item 101000-AA, accessed online on February 28, 2013: <[http://ecprod.cn.ca/ebusiness/eDistribution/english/public/DisplayPage?URL=PriceDocuments?s\\_icid=PriceDocs-feature-right-pricedocs](http://ecprod.cn.ca/ebusiness/eDistribution/english/public/DisplayPage?URL=PriceDocuments?s_icid=PriceDocs-feature-right-pricedocs)>
- <sup>12</sup> Railway Association of Canada, *2012 Rail Trends*, (Ottawa: Railway Association of Canada, 2012), accessed online on February 28, 2013: <[http://www.railcan.ca/assets/images/publications/2012\\_Rail\\_Trends/2012\\_RAC\\_TrendsE\\_Jan10a.pdf](http://www.railcan.ca/assets/images/publications/2012_Rail_Trends/2012_RAC_TrendsE_Jan10a.pdf)>, 7
- <sup>13</sup> *Ibid* at 7
- <sup>14</sup> *Canada Transportation Act*, S.C. 1996, c. 10, ss 159 – 169.3.
- <sup>15</sup> *Canada Transportation Act*, S.C. 1996, c. 10, s 128 and Canadian Transportation Agency Decision LET-R-66-2010 – Review of the Railway Interswitching Regulations.
- <sup>16</sup> *Canada Transportation Act*, S.C. 1996, c. 10, ss 111 and 151.
- <sup>17</sup> *Canada Transportation Act*, S.C. 1996, c. 10, s 151 and Canadian Transportation Agency Decision No. 149-R-2012, Determination by the Canadian Transportation Agency of the 2012-2013 volume-related composite price index required for Western Grain Revenue Caps pursuant to Part III, Division VI of the *Canada Transportation Act*, S.C., 1996, c. 10, as amended.
- <sup>18</sup> *Canada Transportation Act*, S.C. 1996, c. 10, s 156.
- <sup>19</sup> Carriers and Transportation and Grain Handling Undertakings Information Regulations, SOR/96-334 and the Railway Costing Regulations, SOR/80-310.
- <sup>20</sup> Uniform Classification of Accounts and related railway records (February 2009), Canadian Transportation Agency, accessed online on February 28, 2013:

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<<http://www.otc-cta.gc.ca/sites/all/files/altformats/books/Uniform-Classification-of-Accounts.pdf>>

<sup>21</sup> *Ibid* at 1001.

<sup>22</sup> *Ibid* at 1001.

<sup>23</sup> *Consultation on Amendments to the Uniform Classification of Accounts*, Canadian Transportation Agency, announced September 28, 2012, accessed online on February 28, 2013: <<https://www.otc-cta.gc.ca/eng/consultation/consultation-amendments-uniform-classification-accounts>>

<sup>24</sup> *Rail in Canada, 2009* (released September 2011), Statistics Canada, Catalogue No. 52-216-X, accessed online on February 28, 2013:

<<http://www5.statcan.gc.ca/bsolc/olc-cel/olc-cel?catno=52-216-X&chprog=1&lang=eng>>

<sup>25</sup> 49 USC § 11145 and 49 USC § 11161. Various data can be found on the STB's website as accessed on February 28, 2013:

<<http://www.stb.dot.gov/econdata.nsf/AllData?OpenView>>

<sup>26</sup> STB website, accessed online on February 28, 2013:

<<http://www.stb.dot.gov/stb/industry/ures.html>>

<sup>27</sup> Railroad Cost Program (December 2011), Surface Transportation Board, accessed online on February 28, 2013:

<[http://www.stb.dot.gov/stb/docs/URCS/2011/Railroad%20Cost%20Program%20Release/Railroad%20Cost%20Program\\_User%20Manual\\_Dec2011.pdf](http://www.stb.dot.gov/stb/docs/URCS/2011/Railroad%20Cost%20Program%20Release/Railroad%20Cost%20Program_User%20Manual_Dec2011.pdf)>, 1.