

Canadian Grain Freight Regulation and and Ongoing Processes

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THE DIVISION OF LABOUR FOR THIS SESSION

▶ Richard Gray:

- ▶ The Canadian Grain Freight Regulation and the role of the CWB
- ▶ The markets for freight and incentives
- ▶ Potential improvements

▶ Bill Wilson:

- ▶ The operation of the US freight rate market
- ▶ Potential for change in Canada

▶ Terry Whiteside:

- ▶ Discussant – US shipper's perspective

CWB ROLE IN RAIL TRANSPORTATION

- ▶ **Through Single Desk Marketing Function:**
 - ▶ CWB played a large role in rail car allocation and logistics
 - ▶ increased access for producer cars via marketing
 - ▶ increased use of Rupert/Churchill ports
- ▶ **CWB – was a producer voice**
 - ▶ In the development of the WGTA/ CTA
 - ▶ in regulatory hearings/ review processes

CANADIAN GRAIN FREIGHT REGULATION

- ▶ The Crow's Nest Pass Agreement (1897)
- ▶ The Statutory Crow's Nest Rates (1925)
- ▶ Western Grain Transportation Act (1983)
- ▶ CTA with Revenue CAP (2000)
 - ▶ Service obligations
 - ▶ Rate Reviews

THE REVENUE CAP (QUORUM)

- ▶ statutory limit on the amount of revenue railways can earn from the movement of grain in western Canada
- ▶ export shipments from western Canada handled through the west coast ports Churchill, Thunder Bay & Armstrong
- ▶ The revenue limits for CN and CP were based on an estimate of each carrier's total tonnage, average length of haul, and revenues for the 2000-01 crop year

THE REVENUE CAP

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	CN Estimation	CP Estimation
Tonnes Moved (000)	12,437.0	13,894.0
Average Length of Haul (miles)	1,045.0	897.0
Allowable Revenue (\$M)	\$348	\$362.9
Average Revenue per Tonne ₂₀₀₀	\$27.98	\$26.12

THE REVENUE CAP IS A DYNAMIC REVENUE REGULATING MECHANISM

- ▶ Based on the estimates of 2000-01 rail costs but provides for adjustments that take into consideration changes in:
 - ▶ The total number of tonnes of grain actually moved each year by the carrier.
 - ▶ The carrier's actual average length of haul
 - ▶ Inflation

THE “REVENUE CAP” IS AN AVERAGE RATE CAP

- ▶ is a Regulated *Average Freight Rate* multiplied by Tonnage
- ▶ Defined by the formula:

$$\text{Revenue Cap}_{2011} = [(\text{Rate}_{2000-01}) + \text{distance adjustment}] \times \text{Inflation Factor}_{2011} \times \text{Tonnes shipped}_{2011}$$

INFLATION FACTOR

- ▶ This is calculated each year by the CTA based on input prices
- ▶ labour, fuel, material, leased cars, depreciation and cost of capital, each having its own price index
- ▶ In 2007-08 there was a reduction of 8% due to hopper car maintenance

<u>Year</u>	<u>Inflation Factor</u>
2007-08	1.06
2008-09	1.14
2009-10	1.06
2010-11	1.13
2011-12	1.17

EXAMPLE

- ▶ Inflation factor for 2011 is 1.17
- ▶ CN Rate 2011 (if average haul is 1045 miles)
- ▶ Average rate = $27.98 \times 1.17 = \$32.73/t$
- ▶ Revenue CAP= $32.73 \times \text{Tonnes shipped}$

Eg. $32.73 \times 10 \text{ Million tonnes} = \327.3 million

DISTANCE ADJUSTMENT:

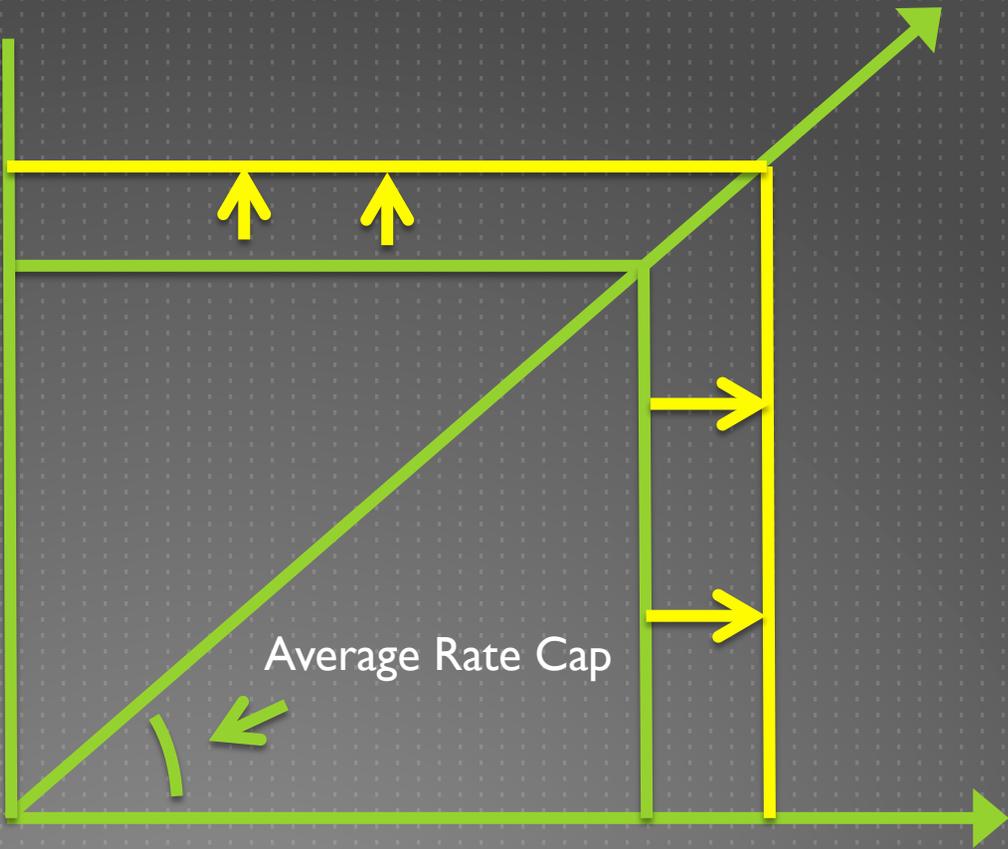
- ▶ (Change in miles hauled) x tonnes x .022 x input price index
- ▶ In CN example if average haul distance was 1145 miles instead of 1045 ie. extra 100 miles
- ▶ Distance adjustment would be (1145 – 1045) or:

$$100 \times .022 = \$2.20 \text{ per tonne}$$

$$\text{Eg. } (32.73 + \$2.20) \times 10 \text{ Million tonnes} = \$349.3 \text{ million}$$

REVENUE IS PROPORTIONAL TO VOLUME

Revenue



Average Rate Cap

Tonnes Shipped

INCENTIVE TO MOVE GRAIN EARLY

- ▶ Average rate Cap does not change when shipment is made in August versus the following June but:
- ▶ Railways get paid when they ship – earlier is better for shareholders
- ▶ Railway can expand total volume by moving more early
- ▶ but Railways want to fully utilize their capacity- this is efficient and reduces cost

POTENTIAL IMPROVEMENTS TO THE REVENUE CAP

- ▶ Some sharing of rail cost efficiency gains (Railways are receiving 100% of efficiency gains made since 2000-01) – But this could reduce incentives to invest in grain versus other capacity
- ▶ The Revenue Cap formula provide some additional incentives to move grain earlier in the crop year but this could distort incentives and increase costs

GOVERNMENT PROCESSES UNDERWAY

- ▶ Follow up to the 2008 Rail Freight Services Review
- ▶ Follow up to C18

FOLLOW UP TO RAIL FREIGHT SERVICES REVIEW

- ▶ The government accepts the CTA panel's commercial approach:
 1. Initiate a six-month facilitation process with shippers, railways and other stakeholders to negotiate a template service agreement and streamlined commercial dispute resolution process;
 - ▶ This process has already started and should wrap up before summer 2012.
 2. Table a bill to give shippers the right to a service agreement to support the commercial measures;
 - ▶ This process has not started yet.

FOLLOW UP TO RAIL FREIGHT SERVICES REVIEW

3. Establish a Commodity Supply Chain Table - involving supply chain partners that ship commodities by rail, to address logistical concerns and develop performance metrics to improve competitiveness;
 - ▶ This process has not started yet, but will likely be initiated near the end of the facilitation process outlined above.

FOLLOW UP TO RAIL FREIGHT SERVICES REVIEW

4. In collaboration with Agriculture and Agri-Food Canada, Transport Canada will lead an in-depth analysis of the grain supply chain to focus on issues that affect that sector and help identify potential solutions.
 - ▶ The analysis has been started and will run parallel to the facilitation process.

C18- CROP LOGISTICS WORKING GROUP

- ▶ The Crop Logistics Working Group will be co-chaired by Agriculture and Agri-Food Canada Deputy Minister John Knuble and Gordon Bacon, the Chief Executive Officer of Pulse Canada.
- ▶ The role and objectives of the new working group will be:
 - ▶ To allow agriculture stakeholders to exchange views about issues and support of the Transport Canada facilitation process flowing from the Rail Freight Service Review;
 - ▶ To also provide a forum for stakeholders to exchange information and views about any transportation and supply chain issues that may arise from the transition to marketing freedom for wheat and barley;
 - ▶ To allow stakeholders to exchange information and develop views on performance measurement along the supply chain; and
 - ▶ To provide a forum for agriculture stakeholders to exchange information and views on other supply chain logistics issues.

CONCLUSIONS

- ▶ Rail Revenue Cap is still in effect and there are no concrete plans to change it
- ▶ There are several process in place to smooth the transition to a post C18 world.