

The Interswitching Provision and its History - A Form of Railway Competitive Access - I

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I. Introduction

Regulated interswitching as a form of competitive access is not new. Its use can be traced to the turn of the last century in the London Interswitching Case of 1905 involving a disagreement between the Canadian Pacific and Grand Trunk railways. It however became a matter of right as early as 1918 when the Commissioner speaking for the Board of Railway Commissioners said "I am of opinion that interswitching should no longer be carried on as a matter of grace, but as a matter of right. The general order ought not to be merely a tariff but an order which provides for and compels the service to be given." [1] Interswitching gained increased prominence in the early 1980s when the Minister of Transport proposed a number of reforms in his Discussion Paper *Freedom to Move* in 1985.

In this paper, the interswitching and extended interswitching provisions are examined. First, the concept of interswitching and its historical objectives are briefly reviewed. Second, the history of the interswitching provisions and its regulations are examined. Finally, interswitching as a form of competitive access is examined with a few concluding remarks on how this provision can be made more effective.

II. The Concept of Interswitching and its Historical Objectives

a) *The Concept of Interswitching*

In everyday language, interswitching is the transfer between railway companies of railcars at an interchange. One source defines it as follows: "Interswitching is the movement of carload freight by the terminal carrier between the point of loading or unloading on such carrier's terminal tracks and the point of interchange with the line-haul carrier." [2]

The concept of interchange of traffic can be traced to section 253 of the *Railway Act* (1903) though it was not specifically defined. [3] It

* The views expressed here are those of the author and are not purported to be those of the Commissioner or the Competition Bureau, Industry Canada.

appeared in the *Railway Act* 1908 for the first time but again was not defined.[4] The first time it was defined was in General Order No. 4988 on interswitching dated July 8, 1908.[5] Today, it is used to describe a situation where a shipper can have his traffic interchanged at the origin or destination with another railway, when the point of movement of traffic is within 30 kilometres or 18 miles of the interchange.[6]

b) The Historical Objectives of Interswitching

The objectives of interswitching have not been stated in the legislation. The first interswitching case (1907) suggests the following:

Making service available: Shippers and manufacturers in the past required access to an extensive network in order to ensure that traffic moved to its customers and plants or to remote areas especially when the main line carriers did not provide such service.[7] Making service available to satisfy shippers has never been explicitly stated as an objective of interswitching but was likely the most important.

Avoiding wasteful use of resources: It was generally uneconomical to have all places served by all railways, given the high cost of constructing and maintaining railway lines. This is particularly so in urban areas and it is therefore not unreasonable to require railways to interchange traffic.[8] This objective like the previous one has also to be inferred though mention exists in the 1905 case of affording to the public traffic facilities without the unnecessary multiplication of lines.

Endorsing intramodal competition: The objective of intramodal competition was first commented on in the report of the Board's Chief Traffic Officer in 1907 in his examination of several complaints on interswitching charges. He noted that it had always been a practice of the railways to absorb the switching charges on competitive traffic and recommended that the railways be allowed to continue the practice. This was endorsed by the Board in a July 1908 Order when it declared that it was lawful for the contracting carrier to absorb interswitching charges.[9]

Promoting public interest and convenience: The objective of public convenience and necessity was stated by the Supreme Court in the London Interswitching Case of 1905. "The provisions of the Railway Act which require railway companies thus to interchange traffic at connecting points are introduced not for the purpose of benefiting one

railway company at the expense of another, but solely in the interest of the public." It was later emphasized in the report of the Board's Chief Commissioner in May 15, 1918.[10]

"From all this we may deduce that, from an historical point of view, the original interswitching regulations were based on the premise that interswitching is in the public interest and, as a direct consequence, is considered a right." [11] The regulators were concerned with: providing uniform interswitching charges; providing adequate compensation; reducing complaints; and ensuring competition.

In sum, the objectives have to be inferred from interswitching cases and government reports. It largely reflects the concerns of the time - the need for service and the bankruptcy of a number of railways. It was not until the mid 1980s, that the objective of interswitching as a means of promoting competition became more prominent. It is this objective today that is of paramount importance. Other objectives that have also been since put forward are the need to use a more efficient (shorter) route and better service to customers (eg. shorter time to provide the service).

III. Interswitching Provisions

The need for interswitching did not arise until the first interchange point between Canadian Pacific Railway (CPR) and Grand Trunk Railway (GTR) was built in Toronto at the turn of the century. In 1904, the second interchange point was built in London, Ontario between the same companies.

a) The Interswitching Provisions and its History

1) *The Period 1900-1950:* In 1904, CPR petitioned the Board of Railway Commissioners to order GTR to provide proper facilities for interchange under section 253 of the *Railway Act (1903)*, as the latter refused to interchange traffic. The Board, in its decision dated July 25, 1905, ordered GTR and CPR to interchange traffic as it is in the public interest and convenience and set the rate at one cent per hundred pounds with a minimum charge of five dollars per car.[12]

After the Board's decision several complaints were received. As a result, the Board's Chief Traffic Officer prepared a report discussing interswitching in general and making recommendations for its regulation. His report indicated that the *Railway Act* of the day made no particular

mention of switching tolls. He advanced the proposition that they be considered under sections 266 and 267 (or 333 and 334 of the *Railway Act*, R.S. 1908) dealing with joint rates.[13] These sections state in part:

"Where traffic is to pass over any continuous route in Canada operated by two companies or more companies, the several companies may agree upon a joint tariff ..." (s. 266)

In the event, the railways fail to agree on a joint tariff over a route and where the Board considers it reasonable and practical, it:

"... may require such companies, within the prescribed time, to agree upon and file in like manner a joint tariff for such continuous route, satisfactory to the Board, or may, by order, determine the route, fix the toll or tolls and apportion the same among the companies..." (s. 267)

The Officer stated "Traffic lifted or delivered locally by one company for another, under tariffs agreed upon by the companies or prescribed by the Board would seem to be covered by these sections." [14] There had in the past been no fixed basis for interswitching rates and his goal in regulation of interswitching charges was to standardize charges for the convenience of the shipper and railways alike so as to avoid excessive complaints.

The Board accepted the recommendations of the Officer which formed the basis of the first General Order No. 4988 on interswitching on July 8, 1908. It adopted as a nation-wide rule: 1) an interswitching limit of 4 miles from the point of interchange; and 2) a rate of one cent per hundred pounds. The Board's order contained eleven provisions which formed the basis for interswitching.[15]

The word 'interswitching' first appeared as a sub-title in section 285 of the *Railway Act* 1908 R.S., c. 37. Section 285(1) covers interchange of traffic between connecting lines, interswitching, and reciprocal duties of companies. In brief, it states in part:

"Where a branch of one railway joins or connects the line or lines of such railway with another, the Board may on application ... order that the railway company which constructed such branch line shall afford all reasonable and proper facilities for the interchange, by means of such branch, ... between the lines of said railway and those of the railway with which the said branch is so joined or connected ...; and the company owning or controlling the secondly mentioned railway

shall furnish similar reasonable and proper facilities to the first mentioned railway, ..."

Sub-section 285 (2) provides for the charge to be regulated by the Board (i.e., 'determine as questions of fact and direct the price per car which shall be charged by and paid for such traffic'). Finally, sub-section 285(3) provides for application of this section (i.e., 'This section will apply whether or not the point of connection is within the same city, town or village as the point of shipment or delivery, or so near thereto that the tolls to and from such points are the same').

Between 1919 and 1927, no changes were made to section 313 of the *Railway Act* 1919 or 1927 formerly section 285 (R.S., c 37).

2) *The Period 1950-1987*: During the period 1950-1987, no changes of significance were made to section 263 of the *Railway Act* 1970 (formerly s. 316 of the *Railway Act*, R.S.C. 1952 or s. 313 of the *Railway Act*, R.S.C. 1927) dealing with interchange of traffic between connecting lines, other than the word 'Board' which was replaced by 'Commission'.

3) *The Period 1987-2004*: In 1987, specific provisions on interswitching and extended interswitching were introduced in the *National Transportation Act, 1987*. The provisions deal with application (s. 152(1)), interswitching limits (s.152(2)) and extension of limits (s. 152(3)) and regulations (s. 152(4)).

According to section 152(2) of the Act "Where the point of origin or destination of a movement of traffic is within a radius of thirty kilometres or a prescribed greater distance from an interchange, no company shall transfer that traffic at the interchange otherwise than in accordance with the terms, conditions and rates prescribed or determined under subsection (4)."

The Agency may make regulations pertaining to interswitching under section 152(4) prescribing the terms and conditions governing interswitching traffic; determining the interswitching rate per car; and prescribing distances greater than 30 km from an interchange for subsection 152(2) and (3). In prescribing the interswitching rate, the Agency shall take into consideration the cost reduction resulting from economies of scale in moving a number of cars at the same time (s. 152(5)). Further, in determining whether interswitching rate is

compensatory, the Agency shall consider the average variable costs of all movements of traffic that are subject to the rate (s. 152(6)). The Agency shall review the regulations when the circumstances warrant and at least once in every five year period after the regulations are made (s. 152(7)).

On July 1, 1996, the *Canada Transportation Act* (i.e., CTA) the successor to the *National Transportation Act, 1987* was enacted. The provisions relating to interswitching (now sections 127(1) to (4) and 128(1) to (5)) remained virtually unchanged. Subsections 127(1) and (2) were previously 151(1); and a subsection was added to the regulations (s. 128(4) indicating that a transfer of a railway line or interest in it does not affect entitlement to an interswitching rate. The provision pertaining to non-compensatory rates were repealed (but consideration of average variable costs in determining interswitching rates was retained s. 128(4) formerly s. 152(6)) and a substantial commercial harm test was added s. 27(2). Section 112 of the Act contained a new feature pertaining to interswitching rates which stipulates that rates established by the Agency shall be “commercially fair and reasonable to all parties.”

The interswitching regulations that were made under the various Acts on railways described above will be described under Section c below.

On March 24, 2005, Bill C-44 (formerly Bill C-26) - An Act to amend the Canada Transportation Act and the Railway Safety Act, to enact the VIA Rail Canada Act and to make consequential amendments to other Acts - was tabled in the House of Commons. The bill indicates that the rates in s. 128(1)b) of the *Canada Transportation Act* are maximum rates. This amendment (section 40) largely reflects the recommendations of the Canada Transportation Act Review Panel.

b) The Extended Interswitching Provisions

In 1987, provision was also made for extension of the interswitching limits beyond the 30 kilometres limit. Section 152 (3) states:

On application of any person or body referred to in subsection (1), the Agency may determine that, in any particular case, where the point of origin or of destination of a movement of traffic is more than thirty kilometres or a prescribed greater distance from an interchange and the Agency is of the opinion that, in the circumstances, the point of origin or of destination is

reasonably close to the interchange, the point of origin or of destination, as the case may be, shall be deemed, for the purposes of this section, to be within that distance.

In the 1996 amendments to the NTA, this section appeared as 127(4). Though the language of the section was changed the intent remained the same.

c) *The Interswitching Regulations*

1) *The Period 1900-1950:* On July 8, 1908, Order No. 4988 (or General Order No. 11) was adopted as a nation-wide rule following numerous complaints to the Board against railway companies regarding the charges made for interswitching. The Order contained eleven provisions. These provisions deal with: i) the interpretation of the terms 'interswitching' and 'contracting carrier'; ii) the absorption of the toll for interswitching competitive traffic; iii) the interswitching toll of 20 cents per ton for any distance not exceeding four miles; iv) an additional toll of 10 cents per ton for any distance not exceeding four miles; v) the computation of distance to or from the nearest interchange; vi) the toll is to include the empty movement of the car; vii) the traffic consigned 'to order' is subject to provisions iii) and iv) above; viii) the traffic interswitched at point of shipment is subject to provision iv) above; ix) the clear and explicit disclosure of points and circumstances under which interswitching services will be performed and its costs; x) the tolls for interswitching are not to supersede lawfully published freight rates; and xi) the provision of free service or other arrangements to equalize the facilities of competing companies are prohibited except as lawfully published.

Its two basic features were: an interswitching limit of 4 miles from the point of interchange; and a rate of one cent per hundred pounds. The rates were based on the principle of giving reasonable compensation for the service furnished by the respective companies.

2) *The Period 1950-1987:* In 1951, the Board issued General Order No. 76886. It contained seven provisions dealing with: i) tariff schedules; ii) exceptions; iii) minimum charge; iv) differentials; v) disposition of fractions; vi) combination of rates; and vii) changes in rates. An important feature of the Order was an increase in the rate for interswitching by 50 percent to one and half cents per hundred pounds.[17] It stated under section 1(e) of the order that

“Charges for interswitching and immediate switching services may be increased 50 per cent.”[15]

On February 1, 1965, the Board of Commissioners for Canada under the provisions of section 316 (now section 263) of the *Railway Act* which permits the Board to set charges for the interchange of traffic between Canada issued General Order No. T- 12 containing the interswitching regulations. It contained fifteen provisions. These provisions deal with: i) the interpretation of the terms interswitching and interchange; ii) the non-applicability of this order for certain movements; iii) the equality in providing interswitching service and the service accorded their own traffic at prescribed tolls; iv) the toll per car within three miles or four miles; v) the toll of the terminal carrier of one and half cent per hundred lbs; vi) the toll of the terminal carrier for all other traffic not referred in section v above; vii) the absorption of the proportion of tolls prescribed in the rate of the line carrier; viii) the tolls not be exceed those prescribed for specified distances; ix) the toll for an extra car or idler; x) the toll (no charge) for accessory of interswitching of the empty car; xi) the absorption of the entire toll for interswitching competitive traffic; xii) the applicability of the order to U.S. traffic; xiii) the limitation of the total charge to certain amounts in case of an exceptional published rate; xiv) the toll in lieu of the toll prescribed in section vi above for team track shipper; and xv) the withdrawal and cancellation of previous schedules for certain services.[18]

The Board (later the Canadian Transport Commission in 1967) continued to issue its decisions on interswitching under sections 284-285 of the *Railway Act* of 1970 (formerly sections 341-342 of the 1952 Act or 336-337 of the 1927 Act) which remained virtually unchanged.

In the early 1980s, the Railway Transport Committee of the Canadian Transport Commission received a number of complaints regarding interswitching. This led to a notice on June 21, 1983, whereby it gave notice that it was undertaking a review of General Order T-12 to clarify certain ambiguities of regulated interswitching. The results of this inquiry led to the April 1985 Report. It was the first detailed review of the issues involved in interswitching since 1908 and provided an analysis and discussion of four major aspects of regulated interswitching: the interswitching limit; the interswitching charges; the

absorption of charges; and the general areas of concern. The Committee recommended that all interested parties be canvassed for responses to the questions set out in the report, as additional information was required to assess the potential effects of the various alternatives for revising General Order T-12.[19] The matter was subsequently overshadowed by the regulatory reforms proposed by the Government in its document *Freedom to Move*.

3) *The Period 1987-2005*: The first *Railway Interswitching Regulations* made under the *National Transportation Act 1987* were issued in 1988. It contained ten provisions which deal with: i) title; ii) interpretation (car block, siding and terminal carrier); iii) application[20]; iv)-vi) general (i.e., equality in the provision of its own and other interswitching services, delivery of empty cars and the toll for delivery of empty cars (i.e., no charge)); vii) interswitching distance zones (namely four: 1-6.4km; 10km; 20km, and 30km.); viii)-ix) interswitching rates; and x) interswitching rates for calculating competitive line rates. In addition, it also contained a schedule of interswitching rates for each of the four zones and the interswitching rate for a point of connection between zone four and a siding more than 40km from the interchange. Under the NTA 1987, the Agency was required to review the regulations “not later than five years after the day on which the regulations are made.”

On December 5, 1991, section 3 of the interswitching regulations was amended indicating that the interswitching regulations do not apply where in the preceding three-year period that company derived at least 90 percent of its gross revenue from interswitching.[21] It also provides for a reapplication by a company after one year where the Agency finds that in the initial application that it does not qualify. This amendment was based on a petition of Essex Terminal Railway Company of Windsor to the Governor-in- Council.

In 1992 after conducting its review, the Agency concluded that “the present structure was an appropriate reflection of the current policy set out in the in the NTA 1987 and, therefore, recommended no changes to the current regulations.”[22].

In 1997, the Agency reviewed the regulations, including a review of the rate levels and a consideration of section 112 of the Act, a new

feature which stipulated that rates established by the Agency shall be “commercially fair and reasonable to all parties.” On November 20, 1997, section 9 of the interswitching regulations was amended providing for deletion of the reference to an actual rate so that future rate changes can be made by amending the schedule of regulations. In addition, the schedule provided for a new column (i.e., V) for rates that apply for each car of a car block. It also clarified the existing language of the section to ensure that the rates are not maximum rates (i.e., an amount not exceeding) as the Agency’s jurisdiction under the law extends to setting rates - not maximum rates.[23]

In 2002, the Agency began its review again and on February 1, 2004 new interswitching regulations came into force. The rates in the four zones for blocks of less than 60 cars decreased on an average by 13 percent and for blocks of more than 60 cars decreased on an average by 16.7 percent.[24] On September 23, 2004, sections 1; 3(1)(b); 8; and 10 were amended to reflect changes to: the definition ‘siding’ and Act; the repeal of section 344 of the *Railway Act*; the prescription of interswitching rates and not maximum rates; and the heading (which was changed in part to ‘determining’ from ‘calculating’) of section 10.

d) Issues in Decisions on the Interswitching and Extending Interswitching Provisions of Particular Interest

A few interesting issues in these decisions will be briefly mentioned.

Notional interchanges: Do notional interchanges known as ‘phantom’ or ‘ghost’ interchanges meet the definition of interchange in the Act? These notional interchanges are interchanges that once existed but cease to exist except on paper for rate purposes. These interchanges do not meet the criteria of an “interchange” under the section 110 of the new NTA, 1987 which requires an existing connection of tracks between two (or more) companies where empty or loaded cars may be stored until delivered or received by any other company.[25]

Interchange: Can an interchange exist if there is only one railway? An “interchange” is defined in section 110 of the NTA . It ‘means a place where the line of a railway company connects the line of another railway company and where loaded or empty cars may be stored until delivered or received by that other company.’ Therefore, where there is only one railway line or where running rights are provided by the only railway there the definition of an interchange as described in the NTA, 1987 is not met.[26]

Circumstances: What is meant by circumstances for purposes of section 152? In considering the word circumstances for extended interswitching in the C.I.L. Inc. (CIL) application, the Agency considered: the existence of an agreement; the relative position of competitors; the supply of car, services and rates; and the distance. It denied this application as it found that there was no evidence that CIL was disadvantaged presently in its marketplace in relation to Cominco and Esso. Further, it could not draw any conclusion respecting alleged problems in the negotiation of rates and service levels with CP, as CIL never formally applied to it due to chronic shortages of covered hopper cars.[27]

Reasonably Close: What is reasonably close? In determining this issue in the Domtar application, the Agency decided to review the specific circumstances of Domtar's operation, the CN service and the competitive position of the Domtar operation vis-à-vis that of neighbouring pulp and paper producers. The Agency found that the eastern switch at the Domtar facilities is approximately 37 radius kilometres from the midpoint of the interchange (i.e., it exceeds the 30 radial kilometre limit by 23.3%) and that the granting of the application for extended interswitching would remove the competitive disadvantage vis-à-vis competitors. It therefore granted the application.[28]

Rates: Can rates be below those set in the schedule and must each rate at each interchange be compensatory? First, a terminal carrier may charge 'any rate' up to the maximums as set out in the Regulations. Second, "While a scheduled rate at a specific interchange may be non-compensatory due to local circumstances, it may be considerably higher than 'compensatory' at another location." These rates are compensatory on a Canada-wide basis as required by section 112 of the NTA, 1987 and are calculated on the system-wide costs of both CN and CP.[29]

Car: Is an articulated five-platform flat car a 'car' for purposes of the schedule in the Regulations? The articulated flat car is quite different from a typical rail car. The flat car is slower to switch, longer and a great deal heavier. The result is increased switching costs and greater track maintenance costs. The Agency therefore concluded that it would be unreasonable to find that 'car' in this instance means a car requiring the car rate set out in the schedule.[30]

The following observation by the Agency is worthwhile “... to suggest that a captive shipper situation should be perpetuated because one carrier is not perceived to be taking advantage of a monopoly situation or that access to competition does not give a shipper an advantage in negotiating with carriers vis-à-vis a captive shipper is inconsistent with the referenced policy objective.”[31]

In conclusion, the interswitching provision and its regulations have evolved over the last hundred years to emphasize competition by increasing the limits over which interswitching can be made and by making the interswitching rates reflective of prevailing railway costs. It is also worthwhile noting that though questions on the interpretation of certain words in the statute did raise concern, they were not such as to affect the operation of this competitive provision.

IV. Interswitching As A Form Of Competitive Access

In this section, the underlying theory for the need to provide interswitching service and to regulate interswitching rates shall be examined.

a) Theory

Interswitching as a form of competitive access provides a remedy to constrain the use of monopoly power where alternative transportation is not available.

Monopoly/Monopoly bottleneck theory: Suppose Railway X is providing its monopoly service on its lines between points A to B and B to C. Being a unregulated monopolist it is assumed that it is maximizing its profits (i.e., \$4 - by charging a price of \$13 on each of the segments for a total price of \$26 - see table I - 1) by determining its price on the average revenue curve at the point where marginal revenue is equated to marginal cost.

Suppose Railway Y later starts up by providing service from B to C on its own lines and its costs are lower than the cost of Railway X from B to C. Railway Y can also provide service from A to B but must interchange at B or obtain running rights from Railway X for A to B (i.e., B is an intermediate point between A and C as Railway Y has lines only from B to C). With the entry of Railway Y, Railway X can now become a bottleneck monopolist if Railway Y wants to provide service

on A to B and may deny Railway Y access to its lines from A to B creating a bottleneck since no alternative lines are available.

Then X's control at the bottleneck distorts the competitive options available to the shipper. If Railway X provides access, it may however still control Railway Y's movement from A to B to C by cross-subsidizing its less efficient segment from B to C with its profits from its monopoly segment A to B by raising its rate on the A to B segment (see table I - 2). Railway X may go even further by using its monopoly power to foreclose Railway Y from competing even on the B to C segment (see table I - 3) if its profits in the A to B segment are more than the loss it would incur in cross-subsidizing.

Table I - Monopoly Pricing/Competitive Pricing and Total Cost

	Monopoly Segment A to B	Competitive Segment B to C	Total Cost A to C	Profits
1. Railroad X only	\$15	\$11	\$26	\$4
2. Railways X and Y	\$18	\$9*	\$27	\$5
3. Railway X only	\$17.5	\$8.5	\$26	\$4
4. Railways X or Y	\$17	\$9	\$26	\$5
5. Railways X and Y	\$16	\$9	\$25	\$3

* Represents the cost of providing service by Railway Y. The numbers, in part, for this analysis have been taken from Massa, Salvatore, Injecting Competition in the Railroad Industry Through Access, *Transportation Law Journal*, Volume 26, 1999, pp. 283-318.

The monopoly theory leads to two distortions: i) shippers use the inefficient carrier and ii) the quality of service is lower **or** the monopoly bottleneck theory leads to two distortions: i) there is diversion of traffic to the monopoly carrier and ii) overall rates to shippers are higher.

Chicago Leveraging theory: The Chicago leveraging theory challenges these conclusions. It holds that Railway X would have an incentive to route the traffic on segment B to C using Railway Y the cheaper more efficient route and obtain a higher return on its investment.[32] They hold that the pricing of segments would be as shown in table I-4. The Chicago theorist's views can be illustrated by assuming that the cost to Railway X of operating segments A to B is 12 and B to C is 10. From table I-1, the monopolist's profits are 4 [i.e., $(15-12) + (11-10)=4$] vs 5 according to the Chicago leveraging theory shown in table I-4. In other words, shippers will not use the inefficient carrier and overall rates to shippers are not higher.

From the above example, up to that point, the Chicago leveraging theory is correct. However, the applicability of this theory to the railways has been challenged by some writers. They argue that the bottleneck monopolist will not be able to leverage its power (i.e., the assumptions do not hold) given the practices in the railway industry.

If Railway X is prevented from using its bottleneck leverage by regulating the rate for interchange (i.e. charging only \$1 for interchange instead of \$3), interchange at B would still be efficient (see table I - 5). Further, the total cost to shippers is lower than under situations where the monopolist exercises its monopoly powers (see table 1-1 and 4).

In sum, by requiring railways to provide interswitching services and by regulating interswitching rates, regulation seeks to constrain the monopoly powers of the railways and to encourage competition.

b) Use of Interswitching and Extending Interswitching

The number of cars interswitched is shown in the following table. It shows a 21% decline over ten years from 1992 to 2001 or a 2.1% decline each year. However, from 1998 there has been 9.2% increase.

Table II - Interswitching (1992-2001)

	1992*	1993*	1994*	1998**	1999**	2000**	2001**
Cars Interswitched	238,000	222,586	221,679	144,269	144,750	157,957	188,757

* Source: Cars switched by Class I carriers CN and CP. National Transport Agency Annual Reports.

** Refers to CP cars switched by CN and CN cars switched by CP - Submission of CNR.

Sixty percent of the interswitching occurs within Zone 1 i.e., the six mile limit. The extension of the limits to 18 miles or 30 kilometres resulted in a reasonable increase in the cars interswitched indicating that extending the limits were successful.

Table III - Interswitching by Zone

	1989	1990	1991	1992	1993	1994
Zone1	60%	60+%	57%	52%	50%	70%
Zone 2-4	40%	40-%	43%	48%	50%	30%

Zone 1 - 6.4 km; and Zone 2-4 - 6.4 to 30 km.

Most of the interswitching occurs in the Provinces of British Columbia and Ontario each accounting for about 34%. Quebec and the

Prairie provinces account for about 15% each of the cars interswitched.

Table IV - Interswitching in Certain Province

	British Columbia	Ontario	Quebec	Prairie	New Brunswick
1992	35%	34%	15%	14%	2%
1993	35%	33%	NA	NA	NA

NA=Not available.

Between January 1, 1988 and June 30, 1996, there were ten extended interswitching applications. Of these the Agency decided three. Between July 1, 1966 and December 31, 1999, there were 0 extended interswitching applications. In 2003, the Agency issued decisions on two applications for interswitching rates.

c) Views on Interswitching as a Competitive Access Provision

NTA/CTA Reports: From 1988 to 1991, the NTA conducted surveys on shippers views on interswitching. The surveys reveal three types of effects: 1) Interswitching had a positive or very positive impact on their firms [33]; 2) Shippers also reported that interswitching was important in achieving competitive terms and conditions and that it had been used as a bargaining tool[34]; 3) The new interswitching provisions resulted in an increase in competition between CN and CP Rail. For example, "... shippers and carriers indicate that there has been an increase in competition between CN and CP Rail as a result of the new interswitching provisions..."[35].

NTARC: In 1993, the NTARC indicated that shippers have responded positively to the extension of the interswitching distance. A survey indicates that shippers having access to two or more railways increased from 54% to 80%, since 1987 and the number of cars switched by CN and CP Rail has approximately doubled. Shippers reported to the NTA that extended interswitching rights increased their bargaining position with the railways. Thus, extending the limit of interswitching – the maximum distance within which a railway must switch the freight cars of its competitors – from 6.4 kilometres (four miles) to 30 kilometres was successful.

CTARP (Panel): In 2001, some Western participants in the Panel’s consultations called for expanded interswitching limits. In the Panel’s view, expanding the interswitching limits would worsen the market-

distorting aspects of the interswitching rate regime and would be a step backward. The proposal ignores market conditions and the averaging effects of a fixed rate – all shippers pay the same rate, regardless of their circumstances.[36]. According to the Panel the “Government should be involved in regulating commercial relationships only when one party is abusing monopoly power. Proposals to extend the interswitching limit assume that railways are behaving in this manner.”[37] It therefore recommended that the existing interswitching limits be retained. It also recommended that the interswitching rates determined by the Agency be maximum rates as it makes no sense to deny shippers and railways the opportunity to negotiate interswitching charges that are lower than the Agency’s interswitching rates, where commercial considerations permit.

Other: In the US too, provision exists for interswitching traffic. The Interstate Commerce Commission permits shippers to petition it for interswitching under 49 USC s. 10705 (a)(1). The Commission “could prescribe a ‘through route’ between two or more railroads. The through route remedy establishes the interchange points at which the railroads switch traffic on their respective networks. To further allow access for shippers, the through route remedy can be supplemented with the prescription of a joint rate covering the movement as well as establishing the division of the rate.”[38]

In sum, the underlying theory for regulating rates, the use of this provision, and views on interswitching all indicate the importance of this provision as a means of ensuring competition.

V. Concluding Remarks

One of the key features of the *National Transportation Act* 1987 was to enhance competition between the railways to benefit shippers and ultimately consumers. However, the benefits of competition to shippers cannot be achieved unless shippers can reach the lines of more than one railway economically. To achieve this, a number of access provisions were expanded or introduced. One of these access provisions is regulated interswitching. It is not new. It was available to shippers as far back as 1908 but its objective at that time was to satisfy the need for service rather than to provide competition.

A historical review of the objectives and the interswitching provisions indicate that all this has changed today. As noted by the Panel, 'today, interswitching rates are advocated as a means of achieving competitive access'. To date, it is not only the most important access provision but the most successful of the access provisions. In the last few years, about 190,000 cars were interchanged by the Class I carriers CN and CP achieving a growth rate of nearly 9 percent. Its success can largely be attributed not only to the expansion of the limits to 30 kilometres in 1987 but also to the regulation of rates at which access is provided. This was also noted by the CTA.[39]

Given, the underlying theory for regulating rates [40] and the views on the importance of interswitching as a form of competitive access, the question remains how can this provision be made more effective? The Panel is of the view that expanding interswitching limits would worsen the market-distorting aspects of the interswitching rate regime and would be a step backward. At the same time, one should not expect too much from the Panel's proposal of requiring rates to be specified as maximum rates in the expectation that it would foster lower rates through private negotiations. This is because where regulated rates are significantly below commercial rates it is unlikely that private negotiations will bring about lower rates.

It is my belief that the answer lies in careful monitoring railway costs and the cost of moving cars in block sizes. The Agency's recent downward revision of the interswitching rates to reflect lowering of costs or economies achieved by the railways is a positive step and a move in the right direction. A further examination of the structure of rates to determine if efficiencies can be achieved from movement of cars in block sizes may provide further lowering of rates and encourage shippers to move cars in block sizes to achieve further efficiencies. Appropriate rates are one of the keys to ensuring that the interswitching provision remains a useful competitive tool as higher rates discourage the use of this provision.

Endnotes

1. Enquiry into Freight Traffic Interswitching Regulations, Staff Report, Railway Transport Committee, Canadian Transport Commission, April 1985, p. 29.
2. Heaver, T.D. and James, C. Nelson, *Railway Pricing Under Commercial Freedom: The Canadian Experience*, 1977, p. 217.

3. Section 253 states in part "All companies shall, according to their respective powers, afford to all persons and companies all reasonable, and proper facilities for the receiving, forwarding and delivering of traffic upon and from their several railways, for the interchange of traffic between their respective railways, and for the return of rolling stock; ..." The 1903 Act did not provide for interswitching rates which may indicate why the chief officer did not use it in 1908 though it was used in the 1905 case.
4. It appeared at the side of section 285, chapter 37, of the *Railway Act* 1908, Revised Statute.
5. "'Interswitching' means the movement of freight in cars between the unloading or loading tracks of one carrier, hereinafter called the 'terminal carrier,' and the point of interchange with another carrier by whom, singly or jointly with a further carrier, the said traffic has been carried from its point of shipment or is to be carried to its destination, hereinafter called, singly or jointly, the 'line carrier', both the terminal carrier and the line carrier which interchanges with the terminal carrier being subject to the jurisdiction of the Board; the said movement being performed with or without the aid of an intermediate carrier whether subject or not subject to the jurisdiction of the Board, hereinafter called the 'intermediary'."
6. NTA Annual Report 1989, p. 61; 1990, p. 64.
7. In the London Interswitching Case of 1905, solicitor for the City of London states "The power of the Board to order interchange of freight is not conferred merely for the convenience of the railways, but is conferred for the convenience of the public and with a view of affording to the public traffic facilities without the unnecessary multiplication of lines."
8. *Vision and Balance*, CTARP, p. 63. Also see footnote above.
9. See Enquiry into Freight Traffic Interswitching Regulations, Staff Report, Railway Transport Committee, Canadian Transport Commission, April 1985, p. 28 and *Vision and Balance*, CTARP, p. 63.
10. He stated "I am of the opinion that interswitching should be no longer carried on as a matter of grace, but as a matter of right. ... The only justification for subjecting the facilities of one company to the business of the other is that of public interest and convenience. Such a course cannot be justified in any case where public interest does not demand and require it." Enquiry into Freight Traffic Interswitching Regulations, Staff Report, Railway Transport Committee, Canadian Transport Commission, April 1985, p. 29.
11. "The regulators who developed interswitching regulations were concerned primarily with bringing about uniform charges for interswitching, and for the obvious reason that it would reduce the number of complaints to the Board. The regulators were also concerned that the carrier performing the interswitching should be reasonably compensated and that shippers should be able to receive the benefits of competition by means of services and facilities which can be the result of interswitching traffic." p. 31.
12. 1905, 6 C.R.C. 327.
13. See footnote 1, p. 26.
14. See footnote 1, p. 27.
15. Id.
16. Order No. 76886, July 1951.
17. Summary of Submissions, Enquiry into regulations affecting freight traffic interswitching between railway companies under federal jurisdiction, Railway Transport Committee, Canadian Transport Commission, April 1984, p. 6.
18. General Order No. T-12, The Board of Transport Commissioners for Canada, Interswitching of Freight Traffic, File Nos. 2846, 6713-184, 55 B.T.C., February 1, 1965, pp. IV-34-37.
19. More specifically, the Commission made the following recommendation "The discussion of the issues leads to the conclusion that a larger quantity of additional information is required to assess the potential effects of the various alternatives: statistical and cost information; and responded to question respecting the possible effects of a revised General Order." *Enquiry into Freight Traffic Interswitching Regulations*, Staff Report, Railway Transport Committee, Canadian Transport Commission, April 1985, pp. 55-56.
20. The regulations do not apply in respect of the transfer of the traffic by the terminal carrier to

another siding at the request of a shipper or another railway company. See SOR/88-41, 17 December, 1987.

21. See Railway Interswitching Regulations, amendment, Canada Gazette Part II, Vol 125, No. 26, SOR/91-715, 5 December 1991, pp. 4810-4816. Another amendment relates to the French version.

22. NTA Annual Report 1993, p. 80, 1993

23. See Regulations Amending the Railway Interswitching Regulations, Canada Gazette Part II, Vol 131, No. 25, SOR/97-519, 20 November 1997, pp. 3402-3411.

24. It should be noted that the schedule of rates has been reviewed and revised as required by statute. See SOR/89-113, SOR/90-36, SOR/91-12, SOR/92-39, SOR/92-738, SOR/93-614, SOR/94-786, SOR/95-596, SOR/97-84, SOR/97-519 and SOR/2004-201. Also see SOR/2004-203.

25. Canadian Transportation Agency, *Decision No. 206-R-1988*, August 2, 1988.

26. Canadian Transportation Agency, *Decision No. 439-R-1989*, September 5, 1989.

27. Canadian Transportation Agency, *Decision No. 165-R-1990*, March 23, 1990.

28. Canadian Transportation Agency, *Decision No. 269-R-1988*, August 17, 1988.

29. Canadian Transportation Agency, *Decision No. 206-R-1988*, August 2, 1988.

30. Canadian Transportation Agency, *Decision No. 298-R-1993*, May 27, 1993.

31. Canadian Transportation Agency, *Decision No. 269-R-1988*, August 17, 1988.

32. Massa, Salvatore, Injecting Competition in the Railroad Industry Through Access, *Transportation Law Journal*, Volume 26, 1999, p. 297.

33. NTA Annual Report 1988, p. 29; 1989, p. 61.

34. NTA Annual Report 1989, p. 61; 1990, p. 64.

35. NTA Annual Report 1991, p. 89.

36. "...the Panel sees them [IR] partly as an anomaly, representing a trade-off between regulation and the market. On the other hand, they induce an element of competition between connecting railways. The Panel is not convinced that upsetting this balance in favour of further regulation would serve the interests of shippers or Canada." *Vision and Balance*, CTARP, p. 63.

37. *Id.* p. 63.

38. Massa, Salvatore, Injecting Competition in the Railroad Industry Through Access, *Transportation Law Journal*, Volume 26, 1999, p. 297.

39. The CTA stated "Regulated interswitching rates benefit shippers by extending their access to the lines of competing railways at rates close to the cost of moving the traffic to or from the interchange point. Regulated rates thus ensure that rail shippers derive, where available, the benefits of price competition, improved service levels and varying routing options and that railways receive, in turn, compensation for the costs incurred in providing interswitching services." See Regulations Amending the Railway Interswitching Regulations, Canada Gazette Part I, November 8, 2003.

40. Philosophically, regulating rates may appear to be a step backward when price deregulation in most industries is being phased out. But to go forward, it may be necessary to take a step backward given the duopolistic structure of the industry and the fact that railways do not wish to compete by taking each others traffic together with their view that other mechanisms such as confidential contracting and final offer arbitration exist to provide shippers with relief.