The Competitive Line Rates/Competitive Connection Rates Provision As a Form of Railway Competitive Access - II

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I. Introduction

The mid 1980s witnessed a new era for the introduction of competition in rail transportation. It all began when the Minister of Transport proposed reforms in his Discussion Paper *Freedom to Move* in July 1985 which were later embodied in the *National Transportation Act, 1987.* It was supposed to signal "...a new era in Canada's transportation history - an era of greater competition, less regulatory intervention and more innovative transportation services. ... more choices and greater competition in rail transportation"[1] according to the National Transportation Agency of Canada (now the Canadian Transportation Agency).

In this paper, one of the competitive access provisions: competitive line rates (CLR) will be examined. First, the concept of CLR and the objectives of the CLR will be examined. Second, the CLR provision in the 1987 Act, issues in decisions on CLRs of particular interest and the 1996 amendments will be examined. Third, the underlying theory behind the CLR will be reviewed, various views on how it could be improved and the proposed competitive connection rates provision will be examined. Finally, a few remarks are made.

II. The Concept and Objectives of a Competitive Line Rate *a) The concept of a competitive line rate*

A competitive line rate (CLR) is a concept for a regulated railway rate that was introduced in Canada in the mid-1980s. It is a rate for the transfer of railcars beyond the 30 kilometre interchange to assist captive shippers. In other words, a shipper who has access to only one railway or is captive to one railway and is more than 30 kilometres from a rail interchange may apply to the regulatory body to impose a freight rate on the local rail carrier for movement of the shipper's cargo from the point of loading to an interchange with the connecting rail carrier.

b) The objectives of a competitive line rate

The objectives of a competitive line rate are implicitly stated in the document *Freedom to Move.* On the section for competitive line rates (or the section which

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* *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.*

it would replace) the document states “Section 278 of the *Railway Act* which provides for the fixing of maximum rates for captive shippers has been ineffective and will be repealed. Shippers formerly having access to the line of only one rail carrier will have access to the lines of competing carriers.”[2] “Although several rate cases before the CTC have referenced section 278, only one has proceeded through all the steps laid out in the legislation.. ... Wishing to encourage competition in all segments of the transportation system, the Government proposes to allow shippers captive to one rail line to have access to the lines of competing rail carriers, through provision in legislation for a joint-line rate from the traffic’s origin to its destination.”[3]

From the above, it can be inferred that the objective of a competitive line rate is first to give more choices to captive shippers by providing them access to alternative routes beyond the 18 mile radius. Shippers can benefit from alternative choices only if they can economically reach the lines of more than one carrier. A second objective of a competitive line rate is to encourage railways to compete for customers and to pass on cost-savings to them. By encouraging intra-modal competition, the railways are encouraged to become more efficient and to provide customers with better services. A third objective of a competitive line rate is to encourage shippers to select the most efficient route (i.e., not only the shortest mileage route but also the cheapest) to move their traffic.

Further, evidence of the above objectives can also be inferred. The document *Freedom to Move* states “The statement of transportation policy objectives, contained in Section 3 of the NTA, will be revised so as to promote actively both intramodal and intermodal competition; greater efficiency and the lowering of total unit costs for all transportation services; ... The new statement will also explicitly promote intra-modal competition (for instance, between railways) as well as intermodal competition (for instance, between railways and trucks). It will espouse minimal government intervention and permit more flexibility.”[4]

III. The CLR/CCR Provision

a) The 1987 competitive line rate provision

A competitive line rate was first introduced into the *National Transportation Act, 1987* as sections 134-143.[5] Subsection 134(2) which provides for shipper requests of a competitive line rate states:

> “Subject to this section and section 135, where a shipper has access to the lines of only one railway company at the point of origin or of destination of the movement of the traffic of the shipper and a continuous route between those points is operated by two or more companies, the local carrier serving the shipper at the point of origin or destination, as the case may be, shall on the request of the shipper, establish a competitive line rate applicable to the movement of the traffic to or from the point of origin or destination, whichever is served exclusively by the local carrier, to or from the nearest interchange with a connecting carrier.”

The definitions of 'connecting carrier' and 'local carrier' are stated in subsection 134(1). Subsection 134(3) provides for the establishment of a CLR by a local carrier and subsection 134(4) provides for the selection of the route by the shipper provided that route is within Canada (subsection 134(5)). It states:

> "Where the ultimate point of destination of a movement of traffic of a shipper is in Canada and there is available to the shipper more than one continuous route wholly within Canada that is cost-effective and over which it is considered reasonable to move the traffic of the shipper, the shipper shall, in order to have a competitive line rate established, designate a continuous route that is wholly within Canada."

The ultimate point of destination for exports for purposes of the above clause is a port in Canada, similarly for origination of imports the port in Canada is where it originates (ss. 134(6)(a)and (b)). The nearest interchange referred to in ss. 134(2) is the nearest interchange to the point of origin or destination served by the local carrier in the reasonable direction of the movement of traffic over the route designated by the shipper unless the local carrier can demonstrate that the interchange cannot be used for engineering or safety reasons (ss. 134(7)).

Section 135 indicates the conditions under which a CLR will be available. Subsection 135(1) requires the shipper to reach an agreement with all the connecting carriers on the continuous route. A CLR shall not be established for a shipper for which a rate is prescribed or determined under the interswitching provisions (subsection 135(2)). Further, a CLR is not available to trailers or containers on flat cars unless the container arrives by water at a port in Canada for further movement by rail or water (subsection 135(3)). A CLR shall not be established for more than 50 percent of the total miles over which the traffic is moved by rail or 750 miles whichever is greater (subsection 135(4)). If no interchange can be found within these limits within the meaning of subsection 134(7) the Agency can establish a CLR for a portion of a movement of traffic that extends over a distance exceeding the limit (subsection 135(5)). Subsection 135(6) provides for the establishment of only one CLR on the continuous route.

The Agency shall establish a CLR and related matters within 45 days (section 136) and the rate will remain in force for one year since it becomes effective (section 139). Section 137 provides for the way in which the CLR is to be calculated. However, if it is determined that such a CLR is non-compensatory, it shall be increased by the Agency to be compensatory. Where the CLR cannot be determined under section 137, the Agency can provide an alternative method for determining it under section 142. It can also make other regulations with the approval of the G-I-C under that section. The CLR is to be set out in a tariff or confidential contract (section 138). Section 140 provides for the supply of railways cars by the local carrier or connecting carrier to the shipper once a CLR

has been established. Finally, a public interest investigation or final offer arbitration is not available to a CLR (section 141) and an order with respect to a CLR can be suspended if it affects the financial viability of Canadian railways (on the basis of a review conducted under certain sections) by the G-I-C.

b) Issues in decisions on the CLR provision of particular interest

Of the six CLR applications, the Agency decided five, four of which were made by one carrier. Some of the interesting aspects of these decisions are mentioned.

Does the Connecting carrier have to be subject to the jurisdiction of Canada? On this, Order No. 1988-R-798 indicated that "The Act ... does not specifically remove US carriers from the definition of a connecting carrier. In addition, the Act clearly contemplates situations where a shipper may designate a continuous route from Canada through the U.S. and back into Canada. ... Participation of a connecting carrier in the movement of traffic for which the local carrier is to charge a CLR is at all times completely voluntary."[6] In other words, the connecting carrier does not have to be within the jurisdiction of Canada.

Does the destination have to be the final true destination? The Act does not define 'point of destination'. However, it makes a distinction between the 'point of destination' and the 'ultimate point of destination' in that if the ultimate point of destination is in Canada, the shipper does not have unrestricted freedom to select a continuous route which is partly in the U.S. CTA - Order No. 1988-R-798 indicated that "In such situations, the legislation makes it clear that where the ultimate point of destination is in Canada, the shipper must designate an all-Canadian route when such route is cost-effective."[7] Thus for purposes of the Act (based on an unreported decision of the Federal Court of Appeal - A-1167-88 and CTA - Decision No. 650-R-1989 - the application of CSP Foods Ltd.) once the applicant indicates that the ultimate destination is not in Canada further points for shipment by rail in the U.S. are not relevant.

Does a CLR require an 'agreement' for the movement of traffic over the balance of the movement? The Act specifies the need of an agreement. The Agency concluded in Order No. 1988-R-798 that for the purpose of establishing the CLR, if Shelby is the destination "...the existence of the published BN tariff for the movement of methanol would in itself be sufficient evidence that there is an agreement between AGCL and BN for the movement of traffic over the balance of the continuous route from the Coutts/Sweetgrass interchange to Shelby."[8]

Does the interchange of traffic have to be the nearest one?: The interchange of

traffic has to be nearest interchange 'with regard to the destination' and not other destinations. Thus the Agency in Order No. 1988-R-798 stated "If ...[it] accepts Shelby as the destination of the traffic, the Coutts/Sweetgrass interchange is clearly the CP-BN interchange in the reasonable direction of movement of traffic between Medicine Hat and Shelby."[9]

What rate should be relied on to determine the CLR? The Agency in Decision No. 650-R-1989 indicated that section 137 envisages two methods for the calculation of a CLR: one where a connecting carrier charges a rate set out in a published tariff (ss. 137(3)); and the other where the connecting carrier charges a rate set out in a confidential contract (ss. 137(4) and (5)). This section makes no provision for situations where the connecting carrier charges a rate which is a published tariff rate in conjunction with a confidential contract. Where the CLR cannot be calculated by any of these methods, s. 142 gives the Agency authority to establish an alternative method. The Agency also noted that ss. 137(3) contemplates a situation where a rate is not only set out in a tariff but is also charged by a connecting carrier. Further, the Act makes no provision for currency conversion where the tariff has application in the U.S. In such cases, the Agency has indicated (Order No. 1988-R-798) that the appropriate course of action would be to use s. 142. The Agency also ruled that the rate most appropriate would be one which takes into account the volume of traffic to be moved (Decision No. 497-R-1990). Finally, the rates have to be compensatory according to ss. 137(8). If the Agency's calculated CLR is not compensatory the rate will be raised [10].

Who should bear the cost of return of empty Cars? "The Agency has determined that in the present case [CTA Decision No. 507-R-1989], it is appropriate that the carrier moving traffic under the CLR should bear the cost of moving empty cars to the same extent that it receives revenue for moving traffic under the CLR. The CLR will be set with a fifth condition that empty cars be routed back to Medicine Hat via the reverse of the continuous route designated AGCL for the establishment of the CLR."[11]

In light of the above and based on the few applications for CLR, it is not surprising that the National Transportation Act Review Commission indicated that some aspects of the CLR mechanism simply do not work and should be improved. It therefore recommended that: first, s. 142 be repealed and s. 137 be amended to require that the Agency establish CLRs that are commercially fair and reasonable; second, section 134 be amended so that a shipper in applying for

a CLR disclose if its designated route has a factitious destination and that the Agency disregard the amount of the connecting carrier's rate in establishing a CLR; third, the requirement in ss. 135(3) that containers arrive by water for further movement by rail or by rail for further movement by water be repealed; fourth, CLRs for routing through Canada be applicable at both origin **and** destination if both shippers and consignee are captive to the same railway company; fifth, a CLR be applicable for up to three years if a shipper proves the need for it; and finally, ss. 140(1) be amended to clarify that the carrier on which a CLR is imposed is not required to supply cars for the traffic being moved.

c) The 1996 amendment to the CLR provisions

On July 1, 1996, the *Canada Transportation Act* (i.e., CTA) the successor to the *National Transportation Act, 1987* was enacted. The CLR was now contained in sections 129-139 formerly sections 134-144. The amendments included a number of changes in detail and style. For example, the Agency must first attempt to calculate the CLR using total revenue for similar traffic moving over similar distances. If there is no such traffic, the Agency calculates the CLR based on the system average revenue per tonne-kilometre. If it is unable to calculate the CLR using that method, the Agency may establish an alternative method of determining the CLR (ss. 133(3) which was similar to s. 142 of the NTA).[12] It did however introduce one major change to the CLRs. The CLR was now made subject to a substantial commercial harm test (ss. 27(2) and (3)) and the public interest test (in section 141of the NTA) was removed.

IV. Competitive Line Rate As a Competitive Access Provision

First, the underlying theory of a CLR (i.e., competitive access) in rail will be briefly discussed, then some of the views on how CLRs can be improved and the new competitive connection rate provision will be examined.

a) Theory

CLR 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: To begin with 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 he is maximizing its profits (i.e., $4 by charging 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

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.

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.

The monopoly theory leads to two distortions, shippers use the inefficient carrier and the quality of service is lower **or** the monopoly bottleneck theory leads to two distortions, diversion of traffic to the monopoly carrier and overall rates to shippers are higher. CLR as a form of competitive access provides a remedy to constrain anti-competitive abuses where an alternative is not available.

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.[17] They hold that the pricing of segments

would be as shown in table I-4. The Chicago theorist's views can be illustrated 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.

Apart from this issue, what is disquieting to anti-trust theorists is the implications of the theory that vertical integration by a bottleneck carrier will not affect welfare.[18] To resolve this matter in the railway industry, this theory has been subject to econometric tests by a group of economists.[19] Their results indicate that "the effect of interline carriers on the welfare difference is substantial and statistically reliable, thus refuting the applicability of the Chicago hypothesis. An additional interline carrier at the origin reduces ΔW [i.e., changes in welfare] by 3.0c per ton mile. An additional interline carrier at the destination has nearly the same effect on shippers' welfare, reducing ΔW by 2.8c per ton mile."[20] Further, recent theoretical studies in general have shown that the implications of the Chicago theory are not necessarily true. [Scherer & Ross (1990), Riordan & Salop (1995); and Riordan (1998)]. "The key to these various studies is that one cannot say a priori that vertical integration definitely will or will not lead to increased monopoly power. ... Empirical investigation is the only way to determine which outcome will result."[21] Two empirical studies on vertical integration in the railroads found that the bottleneck theory was not applicable. "Grimm, et al., found that interline competitors did have a positive effect on competition in the rail markets served by a carrier with a bottleneck portion of the route. Grimm & Plaistow found that the 'primarily end-to-end BN/SF consolidation' had negative competitive harms of approximately $250 million."[22] This analysis does not take into account the competitive impact of the vertical merger if there was another segment from C to D controlled by another railway Z. The vertical merger would reduce railway Z's choice of using two railways to one on the B to C segment to provide service from D to B. As a result, Railway X could now leverage its power on the B to C segment from the A to B segment and it could raise the price to Z (i.e., by charging $13 from A to

B and $13 from B to C rather than $9 from B to C) for the use of the BC segment.[23]

Turning away from the brief digression on vertical integration, if Railway X is prevented from using its bottleneck leverage by a regulated rate (or CLR rate - i.e. charging only $16 for the A to B segment instead of $17), use of the B to C segment of Railway Y would still be efficient (see table I-5 – $9 vs $11). Further, the total cost to shippers is lower than under situations where the monopolist exercises its monopoly powers (see table I-5 and I-4 – $25 vs $26).

In sum, by requiring railways to provide for CLR rates, regulation seeks to constrain the monopoly powers of the railways and to encourage competition between railways. Numerous studies in the US [eg. Corsi, Grimm & Evans (1990), GAO Report, etc.] on railroad competition have shown that competition leads to lower rates.[24]

b) The use of the competitive line rate provision and the reasons attributed for its ineffectiveness

Between January 1, 1988 and June 30, 1996, there were only six CLR applications. Of the six applications, the Agency decided five, four of which were made by one carrier. Between July 1, 1996 and December 31, 2001, there were 0 CLR applications. In other words, despite the 1996 amendments, shippers had no success with the CLRs. In the words of the CTARP "The ensuing legislative amendments did not result in greater use of CLRs."[13] As a result of this, captive shippers (i.e., those shippers only served by one railway) do not gain the benefits of competition. Several reasons have been attributed for the ineffectiveness for this provision.

First, the railways usually do not wish to bid on each others traffic by providing a CLR. The railways have been strong opponents of this provision. The "railways carriers expressed their opposition to the CLR provision because it does not take into consideration the effective intermodal competition, it is anti-competitive and it constitutes a regulated rate. The railways stated that the CLR provision was not needed since there are other provisions in the NTA, 1987 such as confidential contracts and final offer arbitration. Also, Canadian railways indicated that CLRs were unfair because no reciprocal rights exist in the United States."[14] Shippers on the other hand have indicated their desire to see this provision work, as it has given them negotiating power to obtain better rates and service conditions, and increased their transportation service.

Second, the major reason why the CLR provision has not worked is because prior to the application for a CLR, the shipper has to make an agreement with a second federal railway, the line haul carrier, for the movement of traffic from the interchange. This condition is seen as discouraging the usage of the CLR as railways have refused to provide a rate on the line haul portion of the traffic.[15]

Third, a CLR is made subject to the substantial commercial harm test as a result of an amendment to the CTA in 1996. In other words, when an application has been made to the Agency, it has to be satisfied that the applicant would suffer substantial commercial harm if the relief was not granted. According to a survey report, some shippers and provincial governments stated that "even if a second carrier quoted a rate, the 'substantial harm' provision of the *Act* (subsection 27(2)) was a further obstacle to using the CLR provision."[16] It has been pointed out by objectors that the test may be too intrusive, into their private financial matters, legalistic, adversarial and costly. This has added to the difficulties in making this provision viable. This ultimately led to widespread dissatisfaction with this provision, extensive debate and a proposed provision which will be discussed hereafter.

c) Views on competitive line rate as a competitive access provision

National Transportation Act Review Commission (NTARC): The NTARC in 1993 held that where there is little or no real competition to a single railway, the Act sought to encourage competitive behaviour with two main provisions: interswitching; and CLRs. The latter was intended to benefit shippers who are on only one rail line, who are outside the interswitching limit and whose goods cannot profitably be shipped by truck, i.e. there is no effective competition. Nevertheless, CLRs have proven to be controversial. "The railways have opposed them from the beginning, seeing them as an unwarranted intervention in the market. ... The Agency argues that these measures are cumbersome to administer. They are a disadvantage to shippers, who have to prove there is no other way to ship their goods and that the rate they are being offered is unreasonable."[25]

The NTARC expressed concerns about the CLR. They indicated that "No issue inspired more intense debate than the CLR provisions, and yet there are few examples of them actually being used. ... no party appearing before us could demonstrate that the provisions had a clear economic effect. ... While both railways called for changes to weaken these provisions, they, too, failed to prove that the provisions had significant effects." It concluded that "Philosophical

arguments aside, some aspects of the CLR mechanism simply do not work and should be improved."[26] It accordingly made a number of recommendations.

These recommendations were: the Agency establish a CLR that is commercially fair and reasonable; the shipper disclose if the designated route has a factitious destination and that the Agency disregard the amount of the connecting carrier's rate in establishing a CLR; the requirement that containers arrive by water for further movement by rail or by rail for further movement by water be repealed; a CLR routing through Canada be applicable at both origin **and** destination if both shippers and consignee are captive to the same railway company; a CLR be applicable for up to three years if a shipper proves need for it; the carrier on which a CLR is imposed is not required to supply cars; and an alternative method for determining the CLR rate be repealed (s. 142).

Canada Transportation Act Review Panel (Panel): The Panel reviewed the issue of a CLR eight years later in 2001and saw merit in a CLR "that is, creating a rate to connect with a second carrier – as an effective instrument for promoting competition in what are commonly referred to as 'bottleneck' situations. An alternative, which the Panel suggests be designated a Competitive Connection Rate (CCR), would achieve the same objective at reduced risk by targeting the remedy better."[27]

The Panel proposed that the CCR be available only to shippers with no "alternative, effective, adequate and competitive" means of transporting the goods involved in the CCR where the rate is substantially above rates paid by other shippers of the specific commodity under similar conditions and that cannot be explained by apparent cost and value of service considerations (i.e., rates shippers believe constitutes an abuse of market dominance). The shipper would no longer require an agreement with a connecting carrier before requesting a CCR from the Agency. Where the Agency concludes that a CCR is required, the railway and shipper would be given 30 days to negotiate a new rate. If this fails, the Agency would establish a rate, origin to interchange or interchange to destination. The CCR should be calculated using rates in the 75^{th} percentile to the 90^{th} percentile of revenue per tonne-km for movements of the same commodity over distances similar and under the same conditions and levels of service to the CCR portion, with the interswitching rate for the first 30 km.

To avoid overlapping shipper protection, the Panel recommended that a shipper have the choice of either a CCR or FOA (final offer arbitration) so as not to allow two regulatory interventions on the same movement. Further, to minimize the

use of regulated rates, the Panel recommended retaining the existing restrictions on availability of a CLR to one movement (origin or destination); and applicability to 50% of the distance the traffic moves or 1200 kilometres, which ever is greater. Furthermore, the Panel believes that the substantial commercial harm test be repealed as it focuses on the effect on the shipper, rather than the behaviour of the carrier. Finally, the Panel recommended that when establishing a CCR, the CTA continue to be guided by the requirement that rates are commercially fair and reasonable to all - a requirement added in 1996 - with G-I-C power to suspend the CCR if the railway viability is seriously affected.

A non-Canadian View: Grimm et al. indicate "A third area where the ICC should more aggressively promote competition under existing legislation involves reciprocal switching. A reciprocal-switching agreement allows traffic originating on a rival carriers' track to be switched to another carrier in the area. Local monopoly, in which a shipper is served by a single railroad, is perhaps the most serious structural feature that limits rail competition. Congress in the U.S. recognized that local monopoly could limit the benefits of rail deregulation and included the following provision in section 223 of the *Staggers Act*. 'The Commission may require rail carriers to enter into reciprocal switching agreements, where it finds such agreements to be practicable and in the public interest, or where such agreements are necessary to provide competitive rail service. The carriers entering into such an agreement shall establish the conditions and compensation applicable to such agreement, but if the carriers cannot agree upon such conditions and compensation within a reasonable period of time, the Commission may establish such conditions and compensation.' " The authors state "We advocate a more active policy to promote competition in the face of local monopoly power, particularly when a shipper has access only to one railroad and when a second railroad is a short distance away."[28]

d) The competitive connection rates provision (or CLR) to improve the effectiveness of the CLR proposed in Bill C-44

A new competitive connection rates provision in Bill C-44 was tabled in the House of Commons on March 24, 2005. The provision in this Bill (sections 42-47) largely reflects the recommendations of the Panel. Only the key changes in this provision are noted:

• The CCR provision will not have the requirement that a shipper have an agreement with the connecting carrier before it can obtain a CCR (s. 44) (i.e., ss. 131(1) of the former Act).

• The CCR provision does not contain a substantial commercial harm test ss. 7(1)

(i.e., ss. 27(2) and (3) of the former Act).
• The Agency may establish a CCR if 'the shipper has no alternative, effective, adequate and competitive means' for the movement of the CCR traffic (s. 44) (i.e., ss. 131.(2)(a)).
• The rate established by the local carrier for the CCR is above the 75th percentile of revenue per tonne kilometre for the movement by the local carrier of similar traffic under similar conditions (s. 44) (i.e., ss. 131.(2)(b)).
• The CCR established by the Agency must fall in the range of the 75th to the 90th percentile of revenue per tonne kilometre for the movement by the local carrier of similar traffic under similar conditions (s. 44) (i.e., ss. 133.1(1)).
• The information used by the Agency in the determination of the above two features is confidential and may not be disclosed to the applicant (s. 45)(s. 135.1).
• The Governor in Council may suspend the operation of the sections pertaining to the CCR in whole or part if it is of the opinion that the financial viability of a railway company has been seriously affected by the operation of the CCR provision or it may vary or rescind any decision of the Agency with regard to the application to it for a CCR (s. 47) (i.e., s.136.1).

The new amendments are a positive. The removal of the first two changes described above are major obstacles that shippers have attributed for the lack of success of the CLR provision and should encourage the use of this amendment. However, new tests have been introduced which could introduce new difficulties.

First, the captivity test (i.e., the shipper has no alternative, effective, adequate and competitive means for the movement of the traffic to which the application relates) does not apply to the current competitive line rate provision. The present level of captivity proposed will not only be difficult to satisfy but will also take a considerable degree of time, manpower and financial resources of most shippers. One, it appeared in the older 1967 legislation and no one was able to satisfy this test in twenty years till it was deleted; two, it includes a new requirement ‘adequate’; three, it will take shippers a considerable degree of time, manpower and financial resources to satisfy.

Second, the entry tests are new and likely difficult to satisfy as the Agency will have to determine whether the level of rates by the railway company is substantially above rates (i.e., above the 75^{th} percentile) for similar commodities under similar conditions. This could have a chilling effect on the application of this provision. Perhaps, the intent was never to make use of this provision too easy. If so, success with this competitive access provision is likely to be limited.

The Bill with the proposed provisions died when the Conservative Government was elected in early 2006. On May 4, 2006, a new Bill C-11 on the Canada Transportation Act was tabled in the House of Commons. The new bill did not contain any amendments to the current provision on competitive line rates.

V. Concluding Remarks

The last fifteen years of the previous millennium were an exciting period in the history of reforms in rail transportation. Key reforms to enhance competition signalled the dawning of a new era. Competitive access reforms such as interswitching, extended interswitching, CLR, and running rights brought new hope to shippers who began to envision relief from monopoly pricing or duopoly pricing among railways that did not wish to compete.

But this was not to be. This was hardly surprising as CLRs, like other mechanisms designed to enhance competition, were strongly opposed by the railways. Railways maintained that CLRs are an unwarranted intervention in the market. They suggested that CLRs were used principally as a negotiating tool, rather than a means of correcting justifiable rate concerns and that the Agency's formula for CLRs did not reflect railway prices adequately.[29]

Philosophically, the CLR provisions are a paradox as the thrust of deregulation was to eliminate regulation not to increase it. Nevertheless, CLRs are an important competitive access provision, notwithstanding the fact that in eighteen years there were only six CLR applications four of which were by one shipper. The sound underlying theory on which it is based and its potential to enhance competition also led to the introduction of a similar provision in the *Staggers Act* in the US and to recent proposed amendments to it in the *Canada Transportation Act* to make the provision workable.

The removal of the proposed CLR amendments from Bill C 11 will be a serious setback to the hopes that the government once planned and shippers anticipated fifteen years ago and continue to anticipate.

Endnotes

1. *The New National Transportation Act,* The New Framework for Rail Transportation, Pamphlet, 1987, p. 1.
2. *Freedom to Move,* A Framework for Transportation Policy, Transport Canada, 1985, p. 35.
3. *Id*. p. 36.
4. *Id*. pp. 17-18.
5. One may consider this as a 'captive shipper provision' and associate it with section 278 of the *National Transportation Act* 1970, R.S. c. R-2 or section 336 of the *National Transportation Act* 1966-1967, c. 69, but it is quite different though designed to help captive shippers. Section 278 states the conditions under which the CTC may specify and prescribe a maximum rate and the method by which the rate should be calculated. It is better to view it as a 'maximum rate protection' provision. It was based on the recommendation of the MacPherson Royal Commission. "The need for effective shipper protection was recommended when the monopoly power of the railways was sufficient to permit an unacceptable spread between railway cost and revenue. That is, the MacPherson Commission did not use the absence of competing modes as its criterion for the need for maximum rate protection.

It used the ability of the railways to charge rates 'many times higher than costs' because of the absence of competitive forces, intermodal, intramodal and market competitive forces." See *Railway Pricing Under Commercial Freedom: The Canadian Experience*, Heaver, T.D., and James C. Nelson, 1977, pp. 81-82.

CLR provision replaced section 278 because "... only one [application under s. 278] has proceeded through all the steps laid out in the legislation. This section is considered difficult in three respects: the requirement that a shipper be "captive" to rail, the 30, 000-pound carload base, and the 150%markup over variable cost. Therefore, the provision will be repealed in favour of a "family" of appeal provisions encompassing mediation, final-offer arbitration, and a more workable, equitable, and effective appeal mechanism in the NTA. Despite the additoinal appeal mechanisms, the captive shippers may well continue to be at risk in a rail transportation environment characterized by only two main railways. Wishing to encourage competition in all segments of the transportation system, the Government proposes to allow shippers captive to one rail line to have access to the lines of competing rail carriers, through provision in legislation for a joint-line rate from the traffic's origin to its destination." See 3.

6. CTA - Order No. 1988-R-798.
7. Id.
8. Id.
9. Id.
10. Decision No. 650-R-1989 where it raised the CLR for Altona, Manitoba to Winnipeg, Manitoba.
11. CTA Decision No. 507-R-1989.
12. CTARP, footnote 3, p. 97.
13. CTARP, p. 65.
14. *Canadian Transportation Agency*, Annual Report 1997, p. 66.
15. Id.
16. *Canadian Transportation Agency*, Annual Report 1998, p. 58.
17. The Chicago hypothesis argues that a monopolist over one link of the production chain will fully exploit that monopoly power by setting rates so that all the rents are obtainable from the A to B segment. Railway X would exercise its leverage over Railway Y but it would not pay it to foreclose Railway Y from the market.
18. The Chicago propositions in this area are: 1) piling one monopoly on top of another in a vertical chain can lead to *lower*, not higher profits; 2) integrating such monopolies vertically can enhance both profits and economic efficiency; and 3) if a firm has a monopoly over the supply of some indispensable input (that is, one without substitutes) at any stage in a vertical chain of markets, the firm's monopoly power cannot he enhanced by vertical integration into other competitive stages. From these three propositions it follows that if downstream vertical integration by a monopolist into competitive industries cannot enhance monopoly power but can improve efficiency when the downstream industry is monopolistic, how can the antitrust law find fault with such vertical integration mergers? See Scherer and Ross, p. 522.
19. Grimm C.M., Clifford Winston, and Carol A. Evans, Foreclosure of Railroad Markets: A Test of Chicago Leverage Theory, *Journal of Law and Economics*, Vol. XXXV, October 1992, pp. 295-311.
20. Δ is essentially a weighted price-marginal cost margin where the weights are the probability of a shipment being transported by a particular mode. Id. p. 303. In another study, it was also found that "an additional interline rail carrier at the origin lowers the welfare difference by 3.4c per ton mile when the number of single-line carriers on the route is allowed to vary. The effect of an additional interline carrier at the origin is 5.4c per ton mile when there are no single-line carriers on the route, 3.9c when there is one single carrier on the route, and 1.5c when there are two single line carriers on the route." See Winston, Corsi, Grimm and Evans (1990).
21. William B. Tye and James Horn, p. 16. What happens following integration depends upon at least four variables: 1) the elasticity of substitution between inputs (i.e., between the segments A to B and B to C; 2) the extent to which the monopolized input is important in the downstream production process (i.e., the importance of segment A to B as an input into the production of service A to C; 3) the elasticity of demand for the downstream product; and 4) the structure of the downstream market before integration.
22. William B. Tye and James Horn, pp. 16-17.
23. As indicated by Scherer and Ross "... there is also a minus that works contrary to the Chicago propositions. By extending its monopoly to downstream operations, the integrated firm gains control over the downstream industry's use of ***all*** inputs, and not merely the input X." p. 523.
24. See quotes above.
25. NTARC, p. 129.
26. NTARC, p. 130.
27. CTARP, p. 66.
28. See Grimm, Winston, and Evans, footnote 19, p. 307.
29. NTARC, p. 129.