# What You Need to Know About Service Level Agreements and Financial Consequences for poor Rail Service

**Railways already negotiate contracts with shippers, including grain shippers, why does the law need to require Service Level Agreements (SLAs) for grain shippers?**

In a truly commercial environment, the threat of competition is a healthy motivator to offer customers the most efficient and timely service at the best rate. It is only logical that without this threat, the railway companies make business and logistical decisions based solely on what is in their self-interest. SLAs which include financial consequences for breaking the terms are the only way to rebalance the power between customer and service provider.

> *"One of the purposes of the ("common carrier") provisions is to enable the Agency to establish the level of service, which, in a normal competitive environment, would be expected to be set naturally by market forces. That is to say, the provisions are intended to ensure that the level of service is not established solely on the basis of a railway company's interests and preferences, especially where railway companies can exercise monopoly power over captive shippers…."*
> ***CTA October 3, 2014 decision: Louis Dreyfus Canada Ltd. against the Canadian National Railway Company, pursuant to section 116 of the Canada Transportation Act (Case No. 14-02100)***

Other shippers have the flexibility to scale back production and reduce shipments to put pressure on the railways to secure better service. The reality is that grain shippers are required to ship all of the grain that prairie farmers produce, and deliver it on time to keep ships moving, while the railways take the view that grain can always be shipped tomorrow. Legislation is needed to force railways to negotiate balanced SLAs with enforceable penalties to ensure railways provide grain shippers the service they require.

*"Mr. (Hunter) Harrison highlighted the different service levels demanded by the various sectors the railway handles... He said bulk shipments of coal, potash, and grain have been 'modestly' affected by the severe winter [of 2013/14], even though 'some people in Ottawa or a farmer would disagree.' But domestic intermodal traffic... has held up 'very well... Because that's one commodity that we're sensitive to,' Mr. Harrison said. 'If you miss, you miss.* ***It's not like grain or it's not like coal, [where] if you're a little bit late you're still going to haul it."***
***Globe and Mail, March 2014 (emphasis added)***

**Hasn't the Federal Government already provided a mechanism for SLAs?**

While it is true there are provisions in the Canada Transportation Act for shippers and railways to enter into a service contract, or SLA, they do not allow a shipper to arrive at a balanced SLA that includes reciprocal penalties with a railway. Due to the fact that they operate as monopolies, the railways can write the terms of an SLA any way they wish, knowing shippers have no alternatives.

Over the years, the railways have used SLAs to write in terms that deny shippers the full benefit of the Canada Transportation Act and in some cases, these terms run completely contrary to the Act.

Here are some examples:

- Railways require a term in a shipping contract or a simple siding agreement that states the shipper cannot use interswitching to access other railways within range.
- Railways have required shippers to waive their rights under the common carrier obligations to enter into other agreements.

**Where does the current legislation fall short?**

The current legislation has no financial consequence for the railways when they fail to meet the terms. Today, shippers have no meaningful mechanisms to hold railways accountable for service levels. While shippers are subject to tariffs unilaterally imposed by the railways, if they deem performance to be poor, shippers do not have the option to do the same. For example, if a shipper fails to load a train within 24 hours of delivery, demurrage charges apply ($100/car/day ).[1] In fact, every player along the value chain from grower to shipper, to port terminal to vessel carrier, are subject to penalties when terms are not met, with one glaring exception – the railways. Shippers are asking for the commensurate ability to negotiate, and if need be arbitrate, penalties against the railway companies for poor

[1] Source – CN's "Passport 2015 Carload, April 1, 2015" Circular and CP's "Railcar Supplemental Services Tariff 2, May 1, 2015" Circular)

performance. This can be provided by making an amendment to the SLA provisions in the Act to make it clear that performance penalties are eligible for arbitration into an SLA.

There is no dispute resolution process available to shippers when arbitrating the terms of the SLA. Again, without the threat of a customer taking their business elsewhere, the railways have no reason or motivation to stay at the table and negotiate a deal that is fair to both parties. In fact, as noted above, the railways have used SLAs to further abuse their monopolistic power and write in terms that run counter to the spirit of the Act.

Shippers seek timely, meaningful, tools to resolve disputes that will arise from time to time in the context of an SLA. Like performance penalties, shippers require the ability to request an arbitration process into an SLA. This will allow them to negotiate, and if need be arbitrate, balanced commercial contracts rather than having to rely on government to impose measures, such as weekly volume thresholds. The inability to secure access to an expeditious and cost effective dispute resolution process to resolve SLA disputes limits the practical use of an SLA to shippers.

**Bill C-30 gave shippers the ability to recover expenses after a Level of Service Complaint. Why is this not enough?**

Bill C-30 included a provision providing the Canadian Transportation Agency the authority to order a railway to compensate any person for any expenses they incur as a result of the railway's failure to fulfill its service obligations. This amendment was made in section 116 of the Canada Transportation Act and only applies to Level of Service complaints. It does not apply to a railway's failure to adhere to the terms of a Service Level Agreement.

Filing a level of service complaint is a lengthy ordeal. While the timelines for shippers and railways are identified, the timelines for the Agency to render decisions is not. It has been shippers experience that even on matters that are narrow in scope, it takes up to a full year for decisions to be rendered. Given that the value of a favourable decision is in correcting the behaviour that resulted in the poor service, the value diminishes with time. The longer it takes for a decision to be provided, the less relevant or applicable the decision is to future service levels.

The WGEA supports the retention of the C-30 provision to award compensation for Level of Service complaints.

Here is how it can be improved:

- Allocated proper resources to the Agency to provide Level of Service decisions within some reasonable time parameters
- Change the term "expenses" to "damages": The term expenses may include items such as added labour costs. The legal community understands and operates on the term damages, and the WGEA believes the Agency should

have the authority to award damages in the circumstances of a finding of inadequate service from a railway company

Even with strengthened provisions around Level of Service Complaints, there are still many deterrents from using the Level of Service provisions. Deterrents include, a lack of human resource capacity and financial resources to launch a successful challenge and the extended wait for a decision.

It is clear, the best way to avoid a costly complaint process is to start up front with both: (a) a clear definition of what is "adequate and suitable" accommodation as it relates to receiving, loading, carriage, unloading and delivering of shippers' traffic, and to carry it without delay; and (b) An SLA with clear terms and financial consequences if those terms are broken. This is why a Level of Service complaint provision on its own is not enough.

# Grain shippers' requests regarding Service Level Agreements and financial consequences for poor rail service

Make it clear:
To ensure that Level of Service provisions are meaningful, the legislation must define "adequate and suitable accommodation", give the Agency investigative powers, and the ability to launch a Level of Service action of its own volition. (See Paper: What You Need to Know about the Definition of Adequate and Suitable)

Make it explicit:
The only way to achieve permanent balanced accountability for service is to give the statutory right to introduce financial penalties and commercial arbitration into service level agreements to mimic what naturally occurs in a competitive transportation market.

Make it effective:
Give shippers, through legislation, the right to apply financial penalties against the railways in instances where the railways have failed to perform against pre-established criteria. This would be the same as what railways currently do against shippers that fail to meet load or unload performance criteria.

A provision must be made in the legislation to allow a shipper to ask the arbitrator to include provisions in an SLA to govern the resolution of disputes under an SLA. The inability to secure access to an expeditious and cost effective process to recover from breaches of an arbitrated SLA limits the practical use of an SLA to shippers.

Have a "fast-tracked" arbitration process for every rail car shipment that would allow either the shipper or the railway to resolve a penalty-related dispute (whether a penalty applied or not). This could be applied through an SLA or another explicit contractual obligation.