



Government of Canada Hopper Car Fleet 2015 Annual Report



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The Minister of Transport, the Honourable Marc Garneau

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Key Commitments by the Government of Canada

When the Government of Canada (GC) signed new operating agreements for the federal grain hopper car fleet with Canadian National Railway (CN) and Canadian Pacific Railway (CP) in 2007, the GC made commitments to grain producers and taxpayers to:

- Provide hopper cars to the railways at no cost for the transportation of regulated grain;
- Continue a taxpayer benefit of \$10-15 million per year from railway payments for using the cars for purposes other than moving regulated grain;
- Monitor the railways to make sure they keep the hopper cars in good operating condition throughout their service life and ensure the railways maintain capacity as cars are retired from service;
- Ensure railway accountability and transparency through appropriate reporting requirements; and
- Produce a publicly available report, annually.

Purpose

The 2015 Government of Canada Hopper Car Fleet Annual Report details the use of the GC's hopper car fleet. This is the eighth annual report produced under the CN and CP 2007 Hopper Car Agreements. It covers a 12-month period starting January 1, 2015 and ending December 31, 2015. The report:

- Summarizes the monthly operating reports as received from CN and CP;
- Details changes in the grain fleet – retirements, destroyed cars and additions;
- Outlines the results of refurbishment and maintenance inspections and revenue audits; and
- Summarizes information on revenues received from the railways.

Car Use

As per the Operating Agreements, the railways provide a monthly report of the use of the GC hopper car fleet as measured by:

- The average number of cars in active grain service;
- The number of cars on-line and off-line;
- The number and location of cars in storage; and
- The condition of the cars.

Background

Between 1972 and 1994, the GC purchased 13,500 rail hopper cars to carry Western Canadian grain to port for export. Under the past and current operating agreements, the GC provides these hopper cars at no cost to CN and CP to transport grain for export from the Prairies to the ports of Vancouver and Prince Rupert, British Columbia; Churchill, Manitoba; and Thunder Bay, Ontario. This exported grain is referred to as “Regulated Grain,” as it is regulated under the *Canada Transportation Act, Schedule II*. The GC receives monthly Alternate Use revenue when the railways use the railcars to move non-grain commodities and for domestic North American movements. In return, the railways manage, maintain and operate the cars on a day-to-day basis, ensuring sufficient car supply to move Western Canadian grain for export to the ports listed above.

Context for 2015

A review of the *Canada Transportation Act* (CTA) was conducted in 2015 and the final report with findings and recommendations was publicly released in February 2016, including recommendations with respect to the transportation of grain by rail. A full review of the Canadian grain transportation system is a mandate commitment for the Minister of Transport.

2015 Information

The information in this report covers the 2015 calendar year. The period of this report covers portions of both the 2014-15 and 2015-16 crop years (January 2015 to July 2015 and August 2015 to December 2015 respectively), as the industry reports much of its information on a crop year basis, which runs from August 1st to July 31st.

Highlights

In 2015, Transport Canada (TC), on behalf of the GC, monitored how CN and CP maintained, refurbished and operated the federal hopper cars.

- In total, over the period January 1, 2015 to December 31, 2015, \$14.8 million was collected for Alternate Use and salvage value and deposited into the GC Consolidated Revenue Fund.
- A total of \$12.58 million of that revenue was collected for Alternate Use.
- A total of \$2.22 million of that revenue was collected from damaged and destroyed cars.
- 8,406 federal hopper cars were available for grain movements as of the end of December 2015.
- The number of defective cars, known in the industry as bad order cars, has shown an increase over 2014. According to the railways, the increase can be attributed to normal wear and tear given the age of the fleet.

Capacity and Replacement

In accordance with the Operating Agreements of 2007, all GC Hopper Cars have now been refurbished. As a result of this refurbishment, the useful life of the hopper cars has been extended from 40 to 50 years.

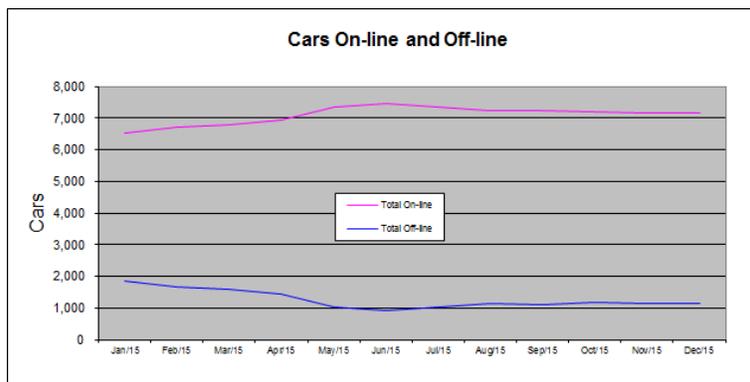
These Agreements set out that the railways are to maintain capacity by refurbishing cars, upgrading cars to carry heavier loads, improving car cycle times and replacing some of the retired federal GC cars with larger capacity (“jumbo”) hopper cars.

Size of Government Fleet

As of January 1, 2015, the GC’s hopper car fleet consisted of 8,410 hopper cars. As part of Transport Canada’s annual hopper car review, the balance of the fleet was adjusted and increased by 81 cars. The adjustment is the result of improved methods and reports used in the fleet review process. As of December 31, 2015, there were 8,406 cars in active grain service taking into account the initial adjustment of 81 cars and the retirement of 85 damaged or destroyed cars.

Cars On-line and Off-line

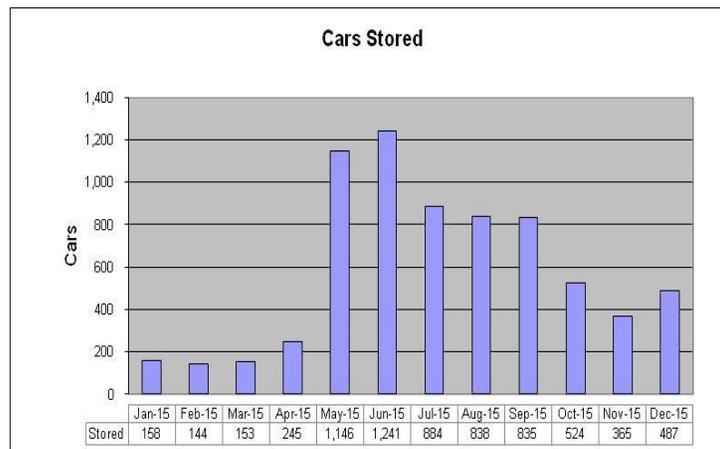
On-line cars refer to equipment that is located on CN or CP lines, while off-line refers to cars located on another carrier's line. On-line and off-line is monitored in order to verify that the hopper cars are being used by the railways in order to move regulated grain. Cars that are off-line are typically hauling grain, but can be doing so on Canadian shortlines or on lines in the United States. On average, 85% of the cars were on-line, an increase of 5% over last year indicating the hopper cars are being used to move grain to port for export.



Cars in Storage

Rail capacity required by producers and shippers is linked to crop production and car supply. Given the seasonal nature of grains and oilseeds, higher rail capacity to move the new crop to an export position is normally required immediately following harvest during the fall and winter. As a result, the railways typically bring hopper cars out of storage in peak shipping season to increase rail capacity, and return hopper cars to storage once the peak shipping season has passed. This was the pattern that took place in 2015.

Note: The cars listed below are typically not stored for the entire month. They include cars that have a stored status at any point during the month.

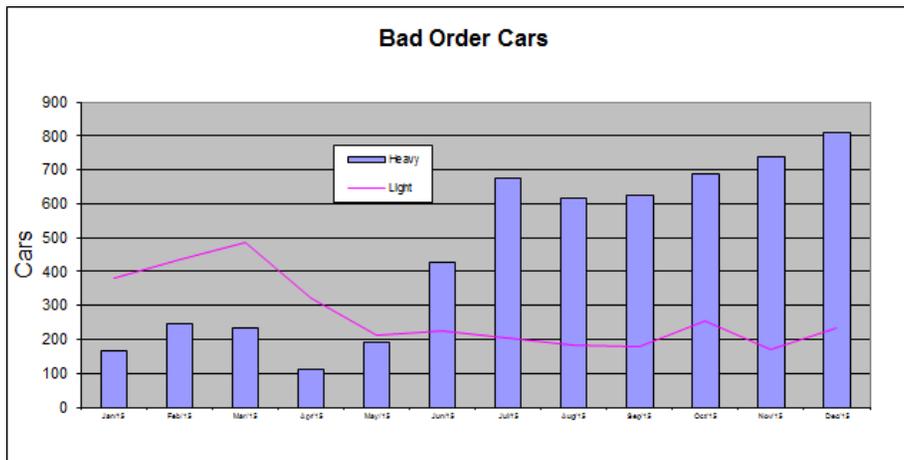


Condition of Cars

As hopper cars are used extensively, they often require repairs. Transport Canada ensures that cars are well-maintained so the efficiency of grain movement is not impeded. The number of cars under repair is monitored to ensure that efficient and timely maintenance is done in a manner consistent with industry norms. As well, Transport Canada may inspect the condition of cars to ensure the proper maintenance of the fleet during the lifespan of the agreements.

Bad Order Cars

Bad order status refers to cars being repaired and therefore not in active use. Cars are considered to be in ‘heavy’ bad order status if they require more than 24 hours to repair and in ‘light’ bad order status if they require less than 24 hours to repair.



Commencing January 2016, Transport Canada revised its reporting requirements for bad order cars. Previously, bad order cars were monitored and reported by Transport Canada on a net basis, identifying the number of cars still needing repair at the end of each month. Given the hopper cars are in the last decade of their useful life, Transport Canada now tracks the total number of cars that go in to bad order status each month as well as the number of cars that remain in bad order at the end of the month. This allows Transport Canada to more closely monitor the overall condition of the fleet as we enter the last decade of their useful life.

The number of light and heavy bad order status cars in 2015 was above seasonal norms for both railways. The railways confirmed that the increase in bad order statistics was due to the age of the hopper car fleet. Transport Canada will be closely monitoring this statistic in the future.

Statement on Maintenance

Transport Canada inspected a random sample of approximately 330 GC Hopper Cars in 2015. The outcome of the physical inspections confirmed the results in the data provided by the railroads of a 5.5% bad order rate. Since 2011, Transport Canada has reported a 2% bad order rate as noted in the refurbishment audit as well as the sampling completed in 2012, 2013 and 2014. Transport Canada will continue to monitor bad order cars to determine whether the finding this year is a one year anomaly or a new trend, due to age of the fleet.

Revenues

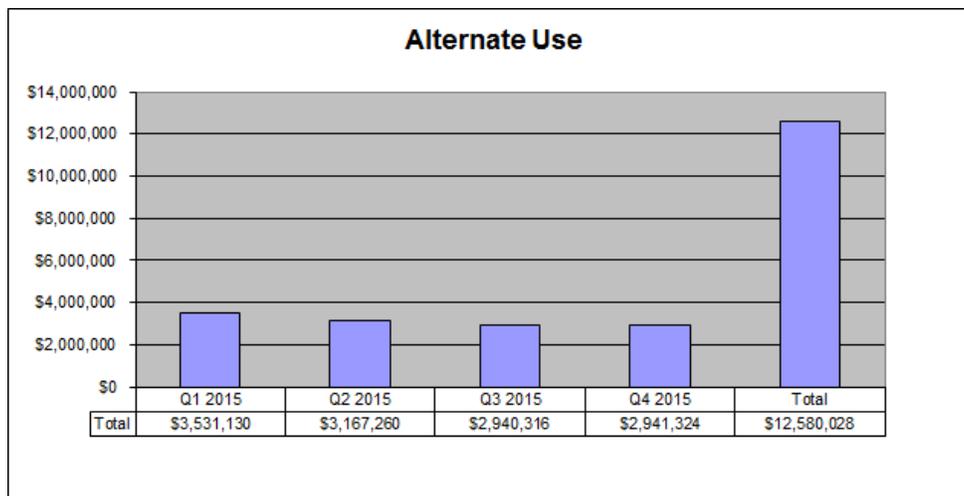
Railways are allowed to use GC hopper cars to haul grain for domestic use or other commodities when not being used to move regulated grain. When this occurs they are required to pay an Alternate Use fee. Additionally, monies received for the salvage value of damaged and destroyed cars is paid to the GC.

Total Revenue

Revenue of \$14.8 million was received in 2015. This includes \$12.58 million for Alternate Use of the hopper cars and \$2.22 million for the salvage value of the destroyed cars.

- It represents an overall decrease of approximately \$2.35 million from 2014 receipts. Alternate Use payments decreased by \$577,000 while Damaged and Destroyed car settlements decreased by \$1.77 million.
- The total number of hopper cars damaged and destroyed in 2015 was 85; a decrease of 418 cars from 2014.

The \$12.58 million in revenues received for hopper cars used in alternate service meets the commitment by the GC to ensure a taxpayer benefit of \$10-15 million annually.



Scrapped Cars

The value received for a car depends upon factors such as the age of the car and scrap metal price when it is salvaged.* In 2015, \$2.22 million was received as salvage value for the destroyed cars, which is a decrease from 2014 receipts of about 44%. This decrease is attributed to the bulk retirement of 1972 and 1973 hopper cars completed in 2014.

The average scrap value received for a destroyed car for the period January 1, 2015 to December 31, 2015 was \$26,141.71, an increase of \$18,202.41 average scrap value per car from 2014. This is attributed to the fact that the cars now being retired are newer cars with a much higher scrap value per car.

*Hopper cars are disposed of utilizing the Association of American Railroads (AAR) Rule 107, using different calculations for pre and post 1974 built cars.

Bulk Retirements

Due to the age of the original GC hopper car fleet, in 2013 and 2014 there were a significant number of bulk retirements from the fleet. Of the remaining 8,406 cars in the current fleet, the next major groupings of cars to reach the end of their useful service life (50 years) and be bulk retired will occur:

- Between 2026 and 2027 (approximately 40% of the fleet).
- Between 2032 and 2035 (almost all the remaining fleet).

By 2044, all of the hopper cars in the GC of Canada fleet will be retired and the fleet will no longer exist. While under agreement with the GC, the railways will continue to provide equivalent capacity for the cars taken out of service. Transport Canada will continue to monitor the fleet to ensure they meet their full useful service life.

Conclusion

The reporting requirements of the railways are outlined in the respective 2007 Hopper Car Agreements. This includes information such as the number of cars on-line and off-line, the number and location of cars in storage, the number of bad order cars and the number of cars required for the movement of the grain harvest in a crop year.

In 2015, total revenues of \$14.8 million were collected. This consisted of \$12.58 million from Alternate Use, ensuring that taxpayers benefitted when the cars were used to haul commodities other than regulated grain. This is in keeping with the GC's commitment to receive \$10-\$15 million annually from the railways for hopper cars used in alternate service. In addition, \$2.22 million was collected from the salvage value of cars that were taken out of service.

As of the end of 2015, there were 8,406 hopper cars for active grain service in the GC fleet. Transport Canada will continue to administer operating agreements with CN and CP to ensure the federal hopper car fleet is well-positioned to provide capacity until the end of their useful life.
