Executive Summary

This report examines the issues that currently threaten large segments of New Brunswick's rail sector. In particular, three critical challenges arose in swift succession during 2012. They are:

- CN's announcement of the pending abandonment of 139 miles of the Newcastle Subdivision, the route of VIA's *Ocean*, between Moncton and Belledune;

- VIA Rail Canada's reduction in the frequency of the Montreal-Moncton-Halifax *Ocean* from six times weekly to three, effective October 2012; and

- The bankruptcy of the Moncton rail equipment remanufacturing firm, Industrial Rail Services, Inc., as a result of the cancellation of three VIA contracts totalling $117.3 million.

The detailed analysis contained in this report explores the underlying causes of the problem, and suggests solutions and alternatives based on the experience of other jurisdictions in similar situations elsewhere in Canada and the U.S.

Historical Background

The era of main line railroading in New Brunswick began with the completion of the government-owned Intercolonial Railway of Canada (ICR) in 1876 between Halifax and Rivière-du-Loup, with a direct connection to the Grand Trunk route to Montreal, Toronto and southwestern Ontario. Today's CN Newcastle Subdivision is part of this through route.

CN owns and operates a second line through New Brunswick, also originally built as a public enterprise. The National Transcontinental Railway (NTR) between Moncton and Quebec via Edmundston opened in 1913, and over time became the principal freight route linking the Maritimes with central Canada, while the ICR remained the main passenger line.

Canadian National Railways was formally constituted as a Crown corporation in 1922 to consolidate several bankrupt private sector lines and the federal government's own rail operations. The company was privatized in 1995, in a process initiated under the Mulroney Progressive Conservative Government and completed by the Chrétien Liberal administration.

As the traditional resource and manufacturing industries in Atlantic Canada declined, so did the CN route network, with 52 per cent disappearing in the 1980s and '90s. The Newcastle Subdivision lost much traffic through the closure of paper mills at Miramichi, Bathurst and Dalhousie, as well as the large zinc and lead mines at Heath Steele and Bathurst Mines.

CN sold a large portion of the ICR route to the Quebec Railway Corporation (QRC) in 1999, but bought it back in 2009, ostensibly to secure the portion of the line serving the industries of Baie-Comeau, Quebec, via the Matane railway car ferry.

CN's Newcastle Subdivision

CN's proposed abandonment of the 139 miles of the Newcastle Subdivision from just north of Moncton to Belledune has extreme implications for future rail freight and passenger service. This would sever the route of VIA's *Ocean*, depriving the North Shore communities of all passenger service. It would also eliminate freight service to shippers in Miramichi, Bathurst and area.

The Newcastle Subdivision is suffering from years of deferred maintenance, leading to the downgrading of the 60 miles from Rogersville to Bathurst from 70 to 30-mph passenger operation, significantly lengthening the *Ocean's* schedule. Freight service is now suspended between Miramichi and the Nepisiguit Subdivision junction south of Bathurst. Meanwhile, several on-line forest products shippers have complained that CN is failing to provide an adequate supply of cars for the movement of their products.

CN has made various statements about the line requiring $30-50 million in upgrading in order to remain in service and accommodate VIA's *Ocean* at a reasonable speed. No assurances of retaining the line beyond three to five years have been given by CN, which has emphasized that it expects public agencies to pay for most of the costs.

VIA Rail Canada Passenger Service

Established by the federal government in 1977 to take over and supposedly improve the remaining passenger services then being operated by CN and CP, VIA Rail Canada has never had the legislation and funding required to properly operate a quality and cost-effective coast-to-coast network. Services in Atlantic Canada have been steadily reduced over the years – an apparent victim of VIA management's growing focus on the Quebec City-Windsor Corridor, with little interest in the continuation of the long-haul routes that make it a national rail passenger service.

The October 2012 reduction of the *Ocean* from six departures weekly to three has inflicted mobility problems on many communities along its Halifax-Montreal route, particularly the portion from Moncton to Campbellton. The decision demonstrates that VIA management completely fails to recognize that the true value of long-haul trains in the modern context lies in the service they provide to intermediate communities along the route – rather than the end points.

Management also has ignored another key principle – a lesson learned long ago by the U.S. public passenger rail carrier Amtrak. A daily train better meets the public need, offers greater potential to build ridership, results in better equipment and crew utilization, and ultimately reduces the subsidy requirement per passenger mile – in other words, better value per dollar of expenditure.

A recent Amtrak study estimated that increasing one of its two remaining tri-weekly trains, the Cardinal, to daily service will require less than 10 per cent more public funding than currently, while providing more than double the service.

A critical contributor to the present high cost structure of VIA's *Ocean* would appear to be the use of problematic British-built Renaissance equipment, retrofitted in a less-than-successful attempt to adapt it to Canadian operating conditions. It has been prone to maintenance issues, and lacks the flexibility to respond to changing demand because it is configured in semi-permanently coupled train sets that cannot be easily modified.

VIA management insists that the decision to cut its Maritime service in half was part of its attempt to "right-size" the corporation, and match capacity to demand. This is in stark contrast with VIA's U.S. equivalent, Amtrak, which has gone through many difficult times, but is now in growth mode thanks to politicians and policies that recognize the need for a national rail passenger service and are enabling federal and state investment in its upgrading and expansion.

Reviving Industrial Rail Services

The bankruptcy of Moncton rail equipment rebuilder Industrial Rail Services, Inc. (IRSI), as a result of the cancellation of three major contracts with VIA, is a classic illustration of all that is flawed with Canada's rail passenger policy, funding, management and service delivery. In its wake, 240 skilled jobs have been lost in Moncton, public and private sector funds have been wasted, and VIA still has a large number of un-rebuilt cars that are growing ever older and less reliable, driving up the cost of providing service.

Since its start-up in the former CN diesel maintenance shop at Gordon Yard in 1999, IRSI had proven itself to be a reliable, high-quality provider of motive power and rolling stock repair and rebuilding services. Based on positive experience with smaller previous projects, VIA awarded the company three major car rebuilding contracts in 2009 and early 2010, valued at approximately $100 million in total.

As detailed in Section 5 of this report, it appears that both parties took overly optimistic risks in signing the contracts, while VIA's decision to rebuild aluminum-bodied LRC cars – already beyond their original design lives – was highly questionable at best. Both VIA and IRSI made many mistakes in executing all three contracts, and the relationship eventually turned toxic.

All three contracts were cancelled and the company was placed in receivership. VIA subsequently obtained permission from the receiver to bring another equipment rebuilder into the IRSI plant to complete some of the work, but it is unclear how many cars in VIA's original fleet renewal plan were actually rebuilt – or at what cost.

Today, VIA is having a difficult time mustering enough equipment to provide its timetabled trains with sufficient cars to meet passenger demand, turning away paying passengers at a time when its revenues are declining and its costs rising.

Economic Considerations

The traditional North American railroading model is in transition. Although much of Canada's earlier rail history saw a large public sector involvement in building and extending a network fuelled by a little too much optimism, the current situation in this country is similar to that in the United States; most of the infrastructure is owned and operated by investor-owned companies.

However, in the U.S. today there is a steadily growing trend toward both federal and state support of strategic rail infrastructure projects. A substantial body of research underlies these investments, but unfortunately the same kind of initiative has not been evident in Canada. We must rely chiefly on success stories from south of the border.

A noteworthy example exists in northern Maine, where an endangered network of branch lines was acquired by the state government to prevent its abandonment. Ironically, the operation was then contracted out to a Canadian company, and shippers in New Brunswick's Upper Valley region are among the rejuvenated short line network's customers.

The efficiency of rail transportation offers extremely important benefits and incentives to industrial development, and it is widely recognized that locations without rail service can be at considerable disadvantage. This is particularly evident in the forest products sector, which is vitally important in northern New Brunswick.

Rail freight offers both superior energy and environmental advantages over highway transport, and despite some recent high-profile accidents, the rail industry's safety record is exceptionally good.

The payback on investment in rail infrastructure is also very significant, with $3 in economic activity generated for each dollar spent. It should be noted that Canada's railways themselves reinvest 40 cents on infrastructure from every dollar of revenue – more than double the rate of many other industries, including airlines, trucking, marine transportation, agriculture, mining, manufacturing, construction and even retailing.

Diverting passengers from highways to rail offers numerous public benefits, including reduced personal injuries from traffic accidents, lower environmental footprint, higher energy efficiency, and stimulus of tourism and commercial development activity. The runaway success story of Amtrak's *Downeaster* in Maine is an excellent case in point.

Unfortunately, successive Canadian federal and provincial governments have tended to ignore these advantages, and have for the most part taken a negative view of supporting passenger rail. Typically, Canadian governments characterize it as a subsidy, while referring to public spending on highways, air facilities and marine infrastructure as investments.

Conclusions and Recommendations

CN's Newcastle Subdivision

The imminent threat confronting the Newcastle Subdivision makes this issue one of immediate priority. It is imperative that the abandonment process be placed on hold to allow time to explore all reasonable potential solutions. In so doing it must be recognized that the Class I railroad business model embraced by CN might not be the most appropriate answer for this troubled line, nor does the current operator necessarily represent the most cost-effective option to bring about the necessary rehabilitation of the infrastructure.

The following are the key recommendations for the Newcastle Sub:

- All ownership and operational alternatives must be carefully examined, including the possibility of ownership by the federal and/or provincial governments, with operation contracted out to an experienced short line company.

- The rehabilitation cost estimates offered by CN should be verified by a qualified third party, and the net salvage value of the property should also be established.

- The creation of a freight car pool for forest products shippers must be explored, with attention paid to solutions that have been successful elsewhere.

- Consideration should be given to redirection of federal funds earmarked for the delayed Shining Waters rail project between Peterborough and Toronto. Timelines are such that these funds cannot now be used in Ontario before they expire, and they could and should be used for rehabilitation of the Newcastle Subdivision instead.

- If public funds are to be used for the necessary rehabilitation of this line – as Transport Action Atlantic believes they should be – the taxpayers' investment must be protected by a public ownership stake in the property.

VIA Rail Canada Passenger Service

In addition to its importance to present and potential future industry on the North Shore, preserving the Newcastle Subdivision is also vital to the survival of the only remaining passenger train in Atlantic Canada. It must be recognized from the outset that rerouting VIA Rail's *Ocean* to the CN line through Edmundston is <u>not</u> an option. Such a move would isolate the communities who need and use the service the most, and running the train through a sparsely populated area with no significant revenue potential would surely prove to be a fatal blow that would soon result in the end of all rail passenger service east of Quebec.

The recommendations pertaining to VIA which follow include several essential steps applicable to passenger rail throughout Canada, in addition to the focus area of this report:

- The *Ocean* should be returned to daily frequency as quickly as possible. This represents much more than simply better meeting the public need; as referenced previously, it would also deliver much better value for each dollar of expenditure.

- VIA should consider using its presently idle and recently rebuilt Budd rail diesel cars (RDCs) between Moncton and Campbellton to augment service until such time as the *Ocean* can be returned to daily operation.

- VIA should make maximum use of its most durable, reliable, and flexible equipment – the rebuilt Budd stainless steel passenger cars, many of which are now idle for six months of the year – while reducing or eliminating use of the un-satisfactory Renaissance equipment presently employed on the *Ocean*.

- Investigate transfer of lower-revenue rail stations to municipal ownership, as is the case in large numbers of smaller towns and cities throughout the U.S.

- Promote better integrated and co-ordinated operation between VIA and Maritime Bus services.

- Introduce the long-delayed act of Parliament to properly establish VIA Rail as a full Crown corporation with a clearly defined mandate, rights and obligations, supported by stable year-to-year funding, and reconstitute its board of directors to include expertise in rail operations and passenger transportation.

- Develop a long-term plan to re-equip VIA with modern, functional, comfortable, and cost-efficient rolling stock.

Reviving Industrial Rail Services

Despite the unfortunate saga of Industrial Rail, there remains reason for optimism about the future of the traditional railcar rebuilding and repair industry in Moncton. Extensive expertise still exists in the area, and the facilities at the Gordon Yard – carefully managed – have a demonstrated record for producing quality work.

Given that the provincial government made a substantial investment in IRSI, and that VIA has an urgent and ongoing need for refurbishment and repair of its aging equipment, particularly the LRC cars, it is recommended that:

- The minister of transport initiate a process to restore a productive business relationship between VIA and the owners of Industrial Rail.

- Recognizing that the bankruptcy of Industrial Rail absorbed a large amount of public money but failed to achieve the desired results for VIA – as a result of missteps by both parties – a thorough investigation be undertaken to identify what went wrong, and implement safeguards to prevent any recurrence of this type of unfortunate situation.

A Critical Role for Municipalities:

While the decisions affecting all three of the challenges now facing railroading in New Brunswick are largely in the hands of the federal and provincial governments, the municipalities that have funded this report (and others in the area) can exert their considerable influence to bring about the desired results.

The timing to do so is opportune. The appointment of a new federal minister of transport on July 15, 2013, the imminent arrival of a new VIA president, the scheduled in-depth audit of VIA by the Office of the Auditor General, heightened public awareness of the inadequacy of Canadian rail investment and regulation, and growing awareness of the commitment of other G8 nations to build and maintain effective and responsive rail systems are creating a climate that is right for the long overdue revision of Canada's national rail policies.

On CN's proposed abandonment of the Newcastle Subdivision, it is recommended that the municipalities join with existing shippers and potential customers to seek an immediate meeting with the Strategic Rail Assets Committee for an update on their progress, and to insist that they be included and consulted on an ongoing basis in the development of a solution that will retain and upgrade this vital asset.

Consistent with the recommendations above, the municipalities should request that the committee hire an independent rail engineering firm to investigate and report on the condition of the line, and that alternate quotes be obtained from independent contractors for comparison with any costing produced by CN regarding its rehabilitation.

They should also be emphatic that a study be undertaken to determine if it would be advantageous to have the line purchased and/or transferred to federal and/or provincial ownership for continued operation by a qualified short line operator, similar to the approaches that have been taken in the Gaspé, Maine and other jurisdictions.

With respect to VIA's unilateral slashing the frequency of the *Ocean* by half, it is essential that the municipalities become more assertive on this issue. They should begin by immediately passing resolutions calling on the federal government to prepare a plan to restore the *Ocean* to daily service and, in the interim, provide daily service over the Moncton-Campbellton route segment following a plan similar to the one outlined in recommendations above. They should also encourage the Federation of Canadian Municipalities (FCM) to intensify its efforts to make VIA an issue of major concern with the appropriate federal cabinet ministers.

Additionally, the sponsors of this report should jointly make a direct approach to Minister of Transport Lisa Raitt to make her fully aware of the community impact of the reduction in the *Ocean's* frequency, its serious value-for-money implications, and the need for quick corrective action by VIA.

The municipalities should also suggest to the minister that an effective first step in the renewal of VIA would be the appointment of former Amtrak president and Cape Breton resident David Gunn to the board of directors; that VIA be required to establish a consultation committee to allow for municipal input into its corporate planning; and that there be a thorough investigation of the advantages in transferring ownership of closed passenger stations, and/or those at risk of closing, to the municipalities.

The tri-communities of Greater Moncton should also ask the minister to initiate a process to bring the owners of Industrial Rail Services and VIA back to the table for a full and frank discussion of the situation that led to the company's collapse, with a view to reconstructing the fractured business relationship and resuming the remanufacturing of rolling stock in Moncton.

Finally, the report sponsors should contact the Office of the Auditor General to request a thorough investigation of the value for money implications of both the reduced service level of VIA's *Ocean* and of the ill-fated IRSI situation contracts, as part of its periodic audit of VIA's activities and finances.

The clock is ticking on all three of these vital aspects of New Brunswick's rail sector. The time for action by all levels of government is now. By taking the actions recommended above, the municipalities that have funded this report – and others – can play an important role in making that happen.