Federal Court of Appeal  Cour d'appel fédérale

Date: 20210409

Docket: A-193-20

Citation: 2021 FCA 69

CORAM: **PELLETIER J.A.**
NEAR J.A.
GLEASON J.A.

BETWEEN:

CANADIAN PACIFIC RAILWAY COMPANY

Appellant

and

CANADIAN TRANSPORTATION AGENCY

Respondent

Heard by online video conference hosted by the Registry on March 16, 2021.

Judgment delivered at Ottawa, Ontario, on April 9, 2021.

REASONS FOR JUDGMENT BY: PELLETIER J.A.

CONCURRED IN BY: NEAR J.A.
GLEASON J.A.

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REASONS FOR JUDGMENT

PELLETIER J.A.

I. Introduction

[1] Canadian Pacific Railway Company (CP) appeals to this Court from Letter Decision No. LET-R-29-2020 (the Decision) in which the Canadian Transportation Agency (the Agency) modified the basis upon which CP's cost of capital (CoC) is determined. CoC is an element in

the determination of CP's volume-related composite price index (VRCPI), which, in turn, affects the maximum revenues it can earn for the movement of western grain in a crop year (Maximum Revenue Entitlement or MRE). More specifically, CP challenges the Agency's position that general purpose debt, including debt incurred for share buybacks, should be included in the CoC determination. In addition, CP appeals from Determination R-2020-81 which determines CP's VRCPI using the CoC arrived at after including general purpose debt in the calculation. Since the fate of Determination R-2020-81 turns on the outcome of the appeal of the Decision, these reasons will focus on the latter.

[2] CP advances three grounds of appeal. First, CP argues that the Agency breached its duty of procedural fairness by refusing to consult with it, as it had with its competitor Canadian National Railway Company (CN), as to the inclusion of general purpose debt, including the method of allocating that debt between regulated and non-regulated activities. Secondly, CP alleges that the Agency erred in law by applying to it a determination made with respect to CN's cost of capital. Finally, CP argues that the Agency erred in law when it included non-rail debt in the determination of its CoC.

[3] For the reasons which follow, I find that the process followed by the Agency lacked procedural fairness and, as a result, the Decision should be quashed, except for the parts from which no appeal is taken. Given this conclusion, it will not be necessary to deal with the issue of the inclusion of non-rail debt in CP's CoC determination.

II. Background

[4] The cost to producers of transporting western grain to port has been an issue for many decades. It was originally addressed by a statutory rate, the Crow's Nest rate, and more recently by the MRE which is mandated by section 150 of the *Canada Transportation Act*, S.C. 1996, c. 10 (the Act), and determined according to the formula set out in section 151 of the Act.

[5] While the operation of this formula is not implicated in this appeal, it is nonetheless helpful in understanding the issues and for that reason, section 151 is reproduced below:

151 (1) A prescribed railway company's maximum revenue entitlement for the movement of grain in a crop year is the amount determined by the Agency in accordance with the formula	151 (1) Le revenu admissible maximal d'une compagnie de chemin de fer régie pour le mouvement du grain au cours d'une campagne agricole est calculé par l'Office selon la formule suivante :
[A/B + ((C - D) × $0.022)] × E × F	**[A/B + ((C - D) × 0,022 $)] × E × F**
where	où
A is the company's revenues for the movement of grain in the base year;	**A** représente le revenu de la compagnie pour le mouvement du grain au cours de l'année de référence;
B is the number of tonnes of grain involved in the company's movement of grain in the base year;	**B** le nombre de tonnes métriques correspondant aux mouvements de grain effectués par la compagnie au cours de l'année de référence;
C is the number of miles of the company's average length of haul for the movement of grain in that crop year as determined by the Agency;	**C** le nombre de milles correspondant à la longueur moyenne des mouvements de grain effectués par la compagnie au cours de la campagne agricole, tel qu'il est déterminé par l'Agence;

D is the number of miles of the company's average length of haul for the movement of grain in the base year;	**D** le nombre de milles correspondant à la longueur moyenne des mouvements de grain effectués par la compagnie au cours de l'année de référence;
E is the number of tonnes of grain involved in the company's movement of grain in the crop year as determined by the Agency; and	**E** le nombre de tonnes métriques correspondant aux mouvements de grain effectués par la compagnie au cours de la campagne agricole, tel qu'il est déterminé par l'Office;
F is the volume-related composite price index that applies to the company, as determined by the Agency.	**F** l'indice des prix composite afférent au volume applicable à la compagnie, tel qu'il est déterminé par l'Office.

[6] A brief examination of the formula shows how it is intended to operate. The formula calculates the revenue per tonne of grain moved in the base year (A/B). It adjusts this amount to account for the difference in average length of haul between the year in issue and the base year (C – D) and applies a statutory rate to the total to produce an adjusted rate per tonne per mile based on the base year. This is then multiplied by the tonnes of grain moved in the year in issue and further multiplied by the VRCPI to yield the railway's MRE. Since A, B, and D are fixed in subsections 151(2) and (3) of the Act and the statutory rate is fixed in the formula itself, the revenue cap or MRE will only change as the average length of haul, the tonnes of grain moved in a year and the VRCPI change. Length of haul and tonnes of grain moved are factors over which railways have little control, given their level of service obligations: see subsection 113(1) of the Act. While the VRCPI is not the only factor affecting a railway's MRE, it is a significant factor.

[7] The VRCPI for the 2016-2017 crop year for both CN and CP is set at 1.3275 in subsection 151(4) of the Act. Thereafter, the Agency is required to make a separate determination of the VRCPI for each of them before April 30 of the following crop year.

[8] One of the elements in the calculation of the VRCPI is the cost of capital which takes into account the cost of a railway's debt as well as the cost of common equity. This appeal concerns the nature of the debt used in the calculation. In order to understand what follows, it is necessary to understand what the parties are referring to. In the exchanges between the parties and in the Agency's decisions, there are references to long-term debt, general purpose debt and non-rail debt. A short review of Agency decisions shows the distinction which is drawn between these kinds of debt.

[9] In 2018, CN approached the Agency about changing the basis on which its debt was allocated to the regulatory balance sheet. In its decision responding to that inquiry, the Agency described the allocation method in place at the time:

> In that Decision [Decision No. 125-R-1997], the Agency found that "using the corporate long-term debt reduced by the identifiable non-rail long-term debt is appropriate in assessing CN's long-term debt for cost of capital purposes." Debt is considered part of CN's RBS [regulatory balance sheet] unless CN can prove that the debt was raised for a specific non-rail purpose, or to finance American operations. Each debt instrument is assigned either 100% to Canadian rail operations, partially to Canadian rail operations, or excluded from Canadian rail operations.
>
> Letter Decision No. LET-R-33-2019 (the 2019 RTM [Revenue tonne mile] Decision)

[10] This passage shows the kinds of debt which were not considered in determining CN's CoC at the time of CN's inquiry: debt raised for specific non-rail purposes and debt raised to

finance CN's American operations. Each debt instrument was allocated in whole or in part to Canadian or US operations. The Agency agreed with CN that this method of allocation distorted the role of debt in its CoC determination. The Agency decided to launch a review of the issue but, in the meantime, it implemented an interim methodology, the RTM methodology, to allocate debt:

> The RTM methodology would allocate general purpose debt to CN's RBS based on the proportion of CN's total RTMs that are performed in Canada. The methodology ensures that the allocation of CN's long-term debt to its RBS is closely tied to the scope of CN's operations in Canada. The RTM approach alters the current practice of allocating specific debt instruments as follows:
>
> 1. any long-term debt that can be allocated specifically between the two jurisdictions would continue to be allocated in such a manner; and
>
> 2. all general purpose debt would be allocated to the RBS based on the proportion of CN's RTM's in Canada in the year in which the debt instrument was issued.
>
> 2019 RTM Decision

[11] The change of methodology means that, except for debt which can be directly linked to CN's US operations, all long-term debt, both rail and non-rail, will be considered and will be allocated between regulatory and non-regulatory purposes using the RTM methodology. This is the significance of the reference to general purpose in point 2 of the passage quoted above. Thus, insofar as the Agency is concerned, general purpose debt is all long-term debt (rail and non-rail) except for debt which can be directly linked to CN's US operations.

[12] On the other hand, while CP uses the expression general purpose debt in some of its representations to the Agency, it tends to put it in quotation marks, "general purpose debt", which I take to be a subtle expression of disagreement with the concept of general purpose debt

as utilized by the Agency. CP's preoccupation is the inclusion of non-rail debt in the determination of its CoC.

[13] As a result, I will use general purpose debt in the same way as the Agency does and will refer to non-rail debt when referring to CP's position.

[14] Another expression which recurs in the material on the file is "regulatory balance sheet". Regulated entities are required to account to the Agency in a prescribed way in order to ensure accurate and consistent reporting. That reporting results in a balance sheet which is used for regulatory purposes, including, but not limited to, the determination of the entity's CoC. For purposes of these reasons, references to inclusion on CN or CP's regulatory balance sheet should be taken as a reference to the inclusion of the entry in the railway's CoC determination.

[15] With that lexicon in mind, I return to the historical narrative. In 2009, the Agency rejected CN's submission that debt incurred for the purpose of buying back shares should be excluded from the CoC calculation because it was an identifiable non-rail activity. The Agency reasoned that since CN's primary, if not exclusive, business line was the railway business, it did not consider such debt to be non-rail debt: see Letter Decision No. LET-R-49-2009 (2009 Buyback Decision).

[16] CP alleges that the 2009 Buyback Decision was a confidential decision which it was not aware of until it demanded its production in 2019. The Agency agrees that CP did not receive a

copy of the decision in a timely manner but says that the failure to disclose it was an administrative error.

[17] As we have seen, one of CN's issues with respect to the CoC determination was the inclusion of debt associated with its US rail operations. In its memorandum of fact and law, at paragraph 25, the Agency described CN's concerns as follows:

> In August 2017 and on May 24, 2018, CN raised with the Agency the issue of how it should allocate general purpose debt as part of its CoC determinations, in the context of a re-determination of CN [*sic*] and CP's VRCPI for the 2018-2019 crop year. This re-determination was prompted by legislative amendments to Part III, Division IV of the CTA, which called for a re-determination of the railway companies' VRCPI in that year. Specifically, CN requested that the Agency consider the use of a North American-based approach for determining its capital structure, or in the alternative, establish how CN might apportion its reported debt between its Canadian and American operations.

[18] The Agency replied by indicating that this issue should be addressed in the Cost of Capital Determination process. In its subsequent 2019 RTM Decision, which we touched upon earlier in clarifying the terms used by the parties, the Agency advised that it proposed to adopt an interim approach to apportionment, the RTM method. An RTM is the movement of one tonne of revenue traffic over one mile. The RTM method allocates general purpose debt between regulated rail use and other uses in the proportion that RTM's of regulatory traffic are of the railway's total RTM's.

[19] The Agency gave CN until May 1, 2019 to respond to its position on the apportionment of long-term debt (which was later extended to July 15, 2019) and April 1, 2019 with respect to the RTM method. The significance of the April date is that the Agency is required to establish a

railway's VRCPI on or before April 30 of the following crop year (see subsection 151(5) of the Act) which begins on August 1 of that year (see section 147 of the Act).

[20] In the interim, CP was provided with a copy of the 2019 RTM Decision sometime in April 2019, which prompted it to inquire whether it would be part of the consultation process. The Agency replied that the consultation would occur exclusively with CN.

[21] In keeping with the statutory deadline, in Decision No. LET-R-41-2019 (the 2019 CN CoC Decision), the Agency applied the 2019 RTM Decision to the determination of CN's CoC for the 2019-2020 crop year.

[22] This decision was not shared with CP at the time.

[23] In December 2019, the Agency informed CP that it intended to apply the RTM method to CP's general purpose debt in determining its CoC. CP objected and asked that the Agency launch a consultation process before imposing this method on CP but the Agency declined to do so.

[24] A short while later, on January 14, 2020, the Agency wrote to CP (the Call Letter) asking for information for use in determining CP's CoC for the 2020-2021 crop year. Specifically, the Call Letter required CP to submit revenue ton miles data for any years in which CP issued general purpose debt, indicating that, except for debt directly linked to CP's US operations, "all other general purpose debt [would] be allocated to [CP's] regulatory balance sheet based on the proportion of total network Revenue Ton Miles in Canada in the year in which the debt is issued

until another methodology is approved by the Agency": Appeal Book, p. 31 (Call Letter). This information was to be provided by February 14, 2020.

[25] CP responded to the Call Letter on February 3, 2020 (CP Response). CP questioned the use of the term general purpose debt by putting that expression between quotation marks ("general purpose debt") in its introductory comments. CP's position on the characterization of debt appears later in its letter when it says: "CP issues debt for two primary reasons. The first is to finance the acquisition and maintenance of railroad assets. The second is for general, non-regulated, corporate purposes which includes share buybacks", in other words, non-rail debt: Appeal Book, p. 40. From CP's perspective, debt issued to fund share buybacks is non-rail debt, but there are other non-rail uses of long-term debt. Thus, while CP's comments focus largely on share buybacks, they are intended to include all non-rail debt:

> The CTA's proposal to allocate non-regulatory debt to the regulated railway operation is not consistent with the UCA [described below], it is not consistent with prior practice, and the CTA does not have a mandate to implement this proposal.
>
> CP Response, Appeal Book, p. 40

[26] CP's position on non-rail debt was that it could not properly be allocated to CP's regulatory balance sheet because of the direction given in the Uniform Classification of Accounts and Related Railway Records (2014), (the UCA, available online at https://otc-cta.gc.ca/eng/publication/uniform-classification-accounts-and-related-railway-records-2014). The UCA "provides accounting instructions and the framework of accounts for the rail operations of such carriers. It also provides instructions for the recording of operating statistics and defines the categories for such data": UCA, Section 1000.

[27] CP identified a number of provisions of the UCA which, in its view, precluded treating "general purpose debt" (referring to the non-rail portion of that debt) in the way proposed by the Agency including:

> 1202.07 The Agency will not receive submission on, or prescribe accounting principles and methods for, non-rail activities of carriers.
>
> ...
>
> 1203.01 All accounts provided in this UCA are intended to contain only transactions and balances resulting from Canadian Rail operations defined as follows:
>
> 1203.02 Rail operations consist of the transportation by rail of goods and passengers (both inter-city and commuter) and include intermodal transportation, which may involve the railway in transport modes other than rail, where such operations are required to complete a rail move.
>
> ...
>
> 1203.06 When items such as cash, accounts receivable and accounts payable are the responsibility of a separate treasury function and not of the rail division, the prescribed UCA accounts for such items will not be used.

[28] To summarize, CP's argument is that to the extent that debt is used for share buybacks, a transaction undertaken by its parent corporation (CPL), that debt relates to non-rail activities so that its integration into the regulatory accounts is precluded by the provisions identified above. In CP's view, "… the CTA does not have a mandate to regulate debt issuances that were issued for the purpose of financing share buy-back programs": CP Response, Appeal Book, p. 40.

[29] In addition, CP argued that the change proposed by the Agency had important consequences for its financial reporting and that of CPL, reporting which was undertaken on the basis of "existing regulations, the accounting standards prescribed by the UCA, and long-

established practices of the CTA in the application of these rules and standards": Appeal Book, p. 41.

[30] CP concluded by asking that it be placed on an equal footing with its commercial competitor (CN) and that it be allowed a reasonable period of time to assess and address issues related to the proposed new rules for calculating CoC.

[31] The Agency's response came in the form of Letter Decision No. LET-R-29-2020, the subject of this appeal.

III. The Decision Under Appeal

[32] The Decision deals with three issues: the inclusion of general purpose debt in the determination of CP's capital structure, the inclusion of commercial paper in the calculation of working capital, and the determination of CP's CoC to be used in the calculation of CP's VRCPI for the 2020-2021 crop year. Since no appeal was taken from the decision as to the inclusion of commercial paper in the calculation of working capital, that finding will remain undisturbed regardless of the outcome of this appeal. Obviously, the CoC determination is caught by this appeal.

[33] The Agency began its analysis by addressing CP's arguments based on the UCA. It noted that CP did not provide any information as to the proportion of its debt issuance "dedicated" to share buybacks while noting that CP indicated that "general purpose debt" was not used exclusively for share buybacks.

[34] The Agency rejected CP's argument that share buybacks are not a rail division treasury function, but rather a CPL treasury function and so, should not be included in its CoC determination pursuant to section 1203.06 of the UCA. The Agency countered this argument by pointing to section 1203.05 of the UCA which states:

> 1203.05 The rail division will become involved from time to time in non-rail activities, which will result in transactions which will affect current assets and current liabilities, and, in some cases, on a temporary basis, other assets and liabilities. The UCA balance sheet accounts are to be used to record such assets and liabilities.

[35] The Agency's view was that the fact that share buybacks are managed through CPL's treasury does not mean that these transactions have no impact on CP or that CP is therefore not relieved of the obligation to account for those impacts.

[36] The Agency went on to find that debt issued for share buybacks is rail-related because there is a general corporate benefit derived from buying back issued shares. In the Agency's view, the issuance of debt in lieu of issuing more shares to fund rail-related investments lowers the company's cost of capital because debt costs less than common equity. This means that the lower cost of raising capital "might allow [CP] to increase investments in other rail-related projects, or to lower freight rates paid by its customers": Decision at para. 16.

[37] The Agency also commented that share buybacks will reduce the number of outstanding shares on the market which increases the relative ownership stake of the remaining shareholders, including CP employees who receive shares as a form of incentive-based compensation. The Agency reasoned that the possibility of an increase in ownership stake could lead to an increase in employee performance, which is rail-related.

[38] Finally, the Agency referred to its 2009 Buyback Decision in which it held that debt incurred for share buyback "in a company whose primary, if not exclusive, business line is the railway business" cannot be classified as identifiable non-rail debt. It concluded that, consistent with that decision, general purpose debt, including when issued for the purposes of share buyback, is rail-related and must be included in the determination of CP's capital structure.

[39] The Agency concluded by saying that it would hold consultations with CN and CP in the coming year "to confirm a methodology with respect to the allocation of general purpose debt for rail purposes that is consistent for CN and CP" for use in the determination of the CoC rate of each railway. In the interim, the Agency would apply the RTM methodology to CP's general purpose debt.

[40] The Agency's decision means that it will allocate long-term debt, including the non-rail portion of that debt, to CP's regulatory balance sheet on a proportionate basis using the RTM method. The consultation which is to follow will deal only with the methodology by which that allocation will be effected.

IV. Standard of Review

[41] Since this is a statutory appeal pursuant to subsection 41(1) of the Act, the standard of review is the appellate standard, namely correctness on questions of law: see *Canada (Minister of Citizenship and Immigration) v. Vavilov*, 2019 SCC 65, 441 D.L.R. (4th) 1, at paras. 18, 36-37 and 50 [*Vavilov*]. Since there is no right of appeal from decisions of the Agency on questions of

fact and mixed law and fact, this is sufficient to dispose of the issue of the standard of review on substantive questions.

[42] That leaves the question of the nature of questions of procedural fairness, a question which is raised by the statutory exclusion of a right of appeal on questions of mixed fact and law. Subsection 41(1) limits the right of appeal to this Court to questions of law and jurisdiction. Whether a person is owed a duty of fairness is a question of law, while whether that duty has been breached is a question of mixed fact and law. At first blush then, this Court could determine whether a duty of fairness was owed but not whether it was breached. This would bifurcate questions of procedural fairness, with this Court dealing with the legal question and the Governor in Council dealing with the question of whether the duty of fairness found by this Court had been breached: see section 40 of the Act. Such a result is inimical to any notion of a practical and efficient system of justice.

[43] As the Supreme Court observed at paragraph 19 of *Canada (Attorney General) v. TeleZone Inc.*, 2010 SCC 62, [2010] 3 S.C.R. 585: “Access to justice requires that the claimant be permitted to pursue its chosen remedy directly and, to the greatest extent possible, without procedural detours.”

[44] However, a careful reading of sections 40-43 of the Act discloses that Parliament intended this Court to deal with questions of procedural fairness comprehensively. That careful reading was undertaken by this Court, *per* Stratas J.A., in *Canadian National Railway Company v. Emerson Milling Inc.*, 2017 FCA 79, [2018] 2 F.C.R. 573, paras. 6-57 [*Emerson*].

[45] The Court reasoned that since the Supreme Court teaches that questions of jurisdiction are essentially questions of statutory interpretation and thus, questions of law, the phrase "a question of law or a question of jurisdiction" contains a redundancy. On the theory that Parliament does not deal in redundancies, the Court examined the scope of "a question of jurisdiction" and concluded that, historically, jurisdiction included questions of procedural fairness, citing the *Toronto Newspaper Guild* case, [1953] 2 S.C.R. 18, [1953] 3 D.L.R. 561. This was the state of affairs when the predecessor of subsection 41(1) was included in the predecessor to the Act, the *National Transportation Act*, R.S.C., 1985, c. N-20. Since the phrase "on a question of law or a question of jurisdiction" has remained in the Act ever since, it is reasonable to conclude that Parliament intended to continue to treat procedural fairness as an aspect of jurisdiction which means that questions of procedural fairness, even though factually suffused as noted above, can be appealed to this Court which can then deal with them comprehensively: see *Emerson* at para. 19.

[46] *Vavilov* did not address the standard of review for questions of procedural fairness, an issue on which the courts have variously said that there is no standard of review or that the standard is correctness. In *Canadian Pacific Railway Company v. Canada (Attorney General)*, 2018 FCA 69, [2019] 1 F.C.R. 121, at paras. 33-56 [*CPR v. Canada*] this Court, *per* Rennie J.A., canvassed this issue and concluded as follows:

> A court assessing a procedural fairness argument is required to ask whether the procedure was fair having regard to all of the circumstances, including the *Baker* factors. A reviewing court does that which reviewing courts have done since *Nicholson*; it asks, with a sharp focus on the nature of the substantive rights involved and the consequences for an individual, whether a fair and just process was followed. I agree with Caldwell J.A.'s observation in *Eagle's Nest* (at para. 20) that, even though there is awkwardness in the use of the terminology, this

> reviewing exercise is "best reflected in the correctness standard" even though, strictly speaking, no standard of review is being applied.
>
> *CPR v. Canada*, at para. 54

[47] With that in mind, I propose to address questions of procedural fairness by asking whether a fair and just procedure was followed, which, as noted in the passage quoted above, captures what is caught, though awkwardly, by the use of "correctness standard" in the context of procedural fairness.

V. Analysis

[48] In its memorandum of fact and law, CP raises two issues of procedural fairness. First, the Agency's failure to consult on the issue of inclusion of non-rail debt in the determination of CP's CoC. Second, the Agency's failure to give it notice of its intention to rely on the 2009 Buyback Decision which held (in relation to CN) that debt incurred for the purpose of share buyback is rail-related and is therefore included in a railway's cost of capital determination.

[49] The Agency appeared and was heard on this appeal, as is contemplated by subsection 41(4) of the Act. The jurisprudence has established that where a tribunal is entitled to be heard, it is not entitled to argue the merits of the appeal or to take a position which puts it into an adversarial position with a party who will continue to appear in the future: see *Canada (Attorney General) v. Quadrini*, 2010 FCA 246, [2012] 2 F.C.R. 3, at para.16; *Ontario (Energy Board) v. Ontario Power Generation Inc.*, 2015 SCC 44, [2015] 3 S.C.R. 147, at para. 72.

[50] The Agency responded to CP's arguments as to procedural fairness by focussing on the RTM issue and pointing out that its decision on that point is merely an interim decision, meant to ensure fairness and consistency in reporting. As for the issue of debt incurred for share buybacks, the Agency notes that the Decision is simply consistent with its 2009 Buyback Decision. It argues that the disposition of the share buyback issue in the Decision is not a simple application of the 2009 Buyback Decision but a fresh decision which it made after consideration of the arguments made by CP in its response to the Call Letter.

[51] In my view, there are two issues to be addressed in this appeal. The first question is whether the Agency was obliged to consult CP with respect to the inclusion of non-rail debt in the determination of its CoC.

[52] The next question is whether that duty was discharged when the Agency considered and rejected the arguments which CP made in its response to the Call Letter. I will address each of these questions in turn.

A. *Was the Agency obliged to consult with CP before including non-rail debt in the determination of its cost of capital?*

[53] Ever since *Nicholson v. Haldimand-Norfolk Regional Police Commissioners*, [1979] 1 S.C.R. 311, 88 D.L.R. (3d) 671, it has been recognized that administrative decision makers have a duty to act fairly. While the cases in which the question arose often involved adjudicative tribunals, the principle does not flow from the nature of the tribunal but from the effect of the decision on the interested party. This was recognized, though not for the first time, in *Cardinal v.*

Director of Kent Institution, [1985] 2 S.C.R. 643, 24 D.L.R. (4th) 44 at 653 when the Court wrote:

> ...This Court has affirmed that there is, as a general common law principle, a duty of procedural fairness lying on every public authority making an administrative decision which is not of a legislative nature and which affects the rights, privileges or interests of an individual: *Nicholson v. Haldimand-Norfolk Regional Board of Commissioners of Police*, [1979] 1 S.C.R. 311; *Martineau v. Matsqui Institution Disciplinary Board (No. 2)*, [1980] 1 S.C.R. 602; *Attorney General of Canada v. Inuit Tapirisat of Canada*, [1980] 2 S.C.R. 735. ...

[54] In this case, CP alleges that the Decision has very significant financial consequences. While there is no direct evidence on the point, it is indisputable that CP and CN's MRE's are in the hundreds of millions of dollars, as evidenced by the statutory baselines set out in subsections 151(2) and (3) of the Act. Those provisions show that CN and CP each had revenues from the movement of western grain in excess of $300 million in the 2000-2001 crop year, the base year. In argument, we were advised that CP's current revenues from the movement of western grains are in the region of $1 billion. In the circumstances, it is apparent that the Agency's decision affects CP's rights and interests and gives rise to a duty of fairness.

[55] Fairness is an elastic concept which varies according to the circumstances. As the Supreme Court wrote in *Knight v. Indian Head School Division No. 19*, [1990] 1 S.C.R. 653, 69 D.L.R. (4th) 489, at 682 and confirmed in *Baker v. Canada (Minister of Citizenship and Immigration)*, [1999] 2 S.C.R. 817, 174 D.L.R. (4th) 193 at para. 21 [*Baker*], "the concept of procedural fairness is eminently variable and its content is to be decided in the specific context of each case".

[56] *Baker* sets out a number of factors to be considered in determining the content of the duty of fairness. One of these is the legitimate expectations of the person concerned. In this case, CP claims that it had legitimate expectations that it would be consulted before the manner of determining its CoC was changed, expectations which were based on the Agency's past practice and its own undertaking to act transparently.

[57] Legitimate expectations can only arise as a result of an administrative tribunal's conduct or its representations:

> …If a public authority has made representations about the procedure it will follow in making a particular decision, or if it has consistently adhered to certain procedural practices in the past in making such a decision, the scope of the duty of procedural fairness owed to the affected person will be broader than it otherwise would have been. ...
>
> *Agraira v. Canada (Public Safety and Emergency Preparedness)*, 2013 SCC 36, [2013] 2 S.C.R. 559 at para. 94

[58] This Court has explained the interests underlying the legitimate expectations doctrine as follows:

> The interests underlying the legitimate expectations doctrine are the non-discriminatory application in public administration of the procedural norms established by past practice or published guidelines, and the protection of the individual from an abuse of power through the breach of an undertaking. These are among the traditional core concerns of public law.
>
> *Apotex Inc. v. Canada (Attorney General)*, [2000] 4 FC 264, 188 D.L.R. (4th) 145 at para. 123

[59] To its credit, the Agency has a long history of consulting with stakeholders on CoC issues.

[60] In 1996-97, as a result of the passage of the Act, the Agency undertook a review of its 1985 decision setting out the methodology for determining the cost of capital in railway operations. The Agency wrote to interested parties asking for comments, and received responses from CP, CN and from the Provinces of Alberta, Manitoba and Saskatchewan and the prairie Wheat Pools. As a result of that review, the Agency issued Decision No. 125-R-1997 which updated the 1985 methodology.

[61] In 1998, the Agency reviewed material filed by CP, CN and the governments of Alberta and Manitoba, and determined that a distinctive CoC rate would be used by CP for regulatory purposes “outside of grain and interswitching rates”: see Decision No. 601-R-1998.

[62] In 2003, the Agency initiated a dialogue with CP, CN and other interested parties about recurring issues in the Agency's determination of the cost of common equity. This resulted in Decision No. 52-R-2004 in which the Agency reviewed many of the elements in the determination of the cost of common equity.

[63] This was followed, beginning in 2009, by another review which led to Decision No. 425-R-2011 (the 2011 Decision) in which the Agency took a fresh look at the many elements going into the determination of the CoC.

[64] As part of this review, the Agency initiated consultation and held hearings:

> The review has been conducted in two phases: a study phase and a hearing phase. In the study phase, after a consultative process involving a wide range of stakeholders to develop the terms of reference for the study, an independent consultant examined existing cost of capital methodologies and principles, and

> reviewed the Agency's current cost of capital methodology, as well as the cost of capital methodologies used by other economic regulatory bodies.
>
> ….
>
> In Decision No. LET-R-185-2010, the Agency initiated the hearing phase of the review and a consultation with a broad list of stakeholders, including railway companies, shippers, producers and others, on certain recurring issues identified by the Agency for discussion. Interested persons were given the opportunity to express their points of view on these issues and any other issues they thought pertinent to the Agency's examination, as well as to provide comments on the Brattle Report [which resulted from the consultation phase].
>
> 2011 Decision, at paras. 3, 5

[65] Both CN and CP made submissions in the course of that consultation and provided the testimony of their chosen experts.

[66] The 2011 Decision concluded as follows:

> [388] The Appendix A methodology [the cost of capital methodology] will be applied by the Agency until at least 2018. The Agency retains the discretion to make adjustments to that methodology in the event of extraordinary circumstances that warrant such adjustments. Where such circumstances apply, any adjustments will be made by the Agency in a transparent manner.

[67] Later, in working out how to determine the capital structure for regulatory purposes of all regulated railway companies, the Agency undertook industry consultations from August to November 2016, and from April to May 2017, in order to seek industry views and comments on issues relevant to capital structure determination: see Determination No. R-2017-198 at para. 12.

[68] It is clear from this review that the Agency has a history of consulting with the railways before making changes to the methodology for determining CoC and other issues. In addition to

this history, CP emphasizes the Agency's undertaking in the 2011 Decision to act transparently in the event that "extraordinary circumstances" warranted adjustments. CP construes this as a commitment to consult with the railways if a change of methodology is to be made. While making adjustments "in a transparent manner" is not synonymous with consultation, it is reasonable, in light of the Agency's history of consultation both before and after 2011, to construe the Agency's undertaking to act transparently as including a consultation process.

[69] As a result, I conclude that CP had a legitimate expectation – based primarily on the Agency's past practice and, to a lesser degree, on the Agency's undertaking to do so – that the Agency would consult with it before altering the basis on which its CoC is determined.

B. *Did the Agency satisfy its duty of procedural fairness when it considered and rejected the arguments which CP made in its response to the Call Letter?*

[70] Before dealing with the issue of the Call Letter, it is worth noting that, upon receipt of the 2019 RTM Decision, CP inquired of the Agency whether the review would include consultation on capital structure and if not, would it be involved in any way in the review. The Agency advised CP that the review would be "addressed exclusively with CN", but noted that CP would be notified of a consultation on inter-switching rate methodology to be launched shortly, which would include questions on CoC: Appeal Book, p. 27.

[71] When the Agency issued the 2019 CN CoC Decision following the review described above, it decided that, except for debt that could be directly linked to CN's US operations, "all

other general purpose debt will be allocated to the regulatory balance sheet based on the proportion of total network [RTM] in Canada in the year in which the debt is issued".

[72] I note that this decision dealing with the issue of the treatment of non-rail debt was resolved without hearing from CP.

[73] When the Agency sent its Call Letter to CP, it referred to the treatment of general purpose debt found in the 2019 CN CoC Decision. The Agency asked CP for RTM information, explaining that, except for debt directly linked to CP's US operations, "all other general purpose debt will be allocated to the regulatory balance sheet" on the basis of the RTM methodology. The Agency indicated that this methodology would be used "until another methodology is approved by the Agency": Appeal Book, p. 31. CP, which had not previously received a copy of the 2019 CN CoC Decision, requested one, which was duly provided.

[74] The Call Letter did not invite submissions on the Agency's decision to subject all non-US debt to the RTM methodology.

[75] As part of its response to the Call Letter, CP advised the Agency that the decision to allocate all non-US debt to the regulatory balance sheet using the RTM method would "represent a significant change to CP's regulatory financial statements and [might] materially impact CP's regulatory cost of capital". As pointed out earlier in these reasons, CP then went on to explain why some of its debt was not rail-related and should not be included in the determination of its CoC.

[76] The Agency rejected CP's submission in the Decision, giving rise to this appeal.

[77] With that in mind, can it be said that the Agency discharged its duty to consult CP during the process which began with the 2019 RTM Decision and ended with the Decision?

[78] CP says the Agency did not discharge that duty because it was not consulted, it was not advised of the case it had to meet and, in particular, the Agency applied to it a rule about the inclusion of all non-US debt, including debt used for share buybacks, a rule of which CP had no knowledge. The Agency responded by saying that CP received copies of decisions in which these issues were raised and that it responded to the issues raised by CP in its response to the Call Letter in the Decision.

[79] CP makes two further points. The first is that even debt incurred by CP itself (as opposed to CPL) can only be included in the regulatory balance sheet if it is rail-related, a position founded in the specific provisions of the UCA such as 1202.07 and 1203.01. CP's second point is that debt incurred by CPL, which is not a regulated entity, cannot be included on the regulatory balance sheet because CPL is not the regulated entity.

[80] The answer to the question of whether the Agency respected CP's right to be consulted can be approached in two ways. The first is to ask whether the Agency sought CP's input before making the Decision. The second is to see if, notwithstanding its failure to reach out to CP, the Agency considered CP's objection to the inclusion of non-rail debt on the regulatory balance sheet.

[81] It is apparent from the exchanges between CP and the Agency, beginning with the 2009 RTM Decision, that the Agency did not consult with CP. As noted earlier in these reasons, when CP wrote asking if it would be included in the review announced in that decision, the Agency excluded it. When the Agency issued the Call Letter, it did not invite CP's submissions on the inclusion of non-rail debt on the regulatory balance sheet. It simply required CP to provide information on long-term debt, excluding only debt tied directly to CP's US operations. In short, not only did the Agency neglect to consult CP, it refused to do so.

[82] As a result, it cannot be said that the Agency consulted with CP prior to making the Decision.

[83] The Agency's response is that, nonetheless, CP was aware of the issues and its submissions were addressed in the Decision so that, in substance, CP was heard. This approach focusses on whether CP's voice was heard, despite the absence of a consultation process. It seeks to address the substantive reality rather than the procedural formalities. There is something to be said for this since the point is that CP was entitled to be heard, not that it was entitled to be heard in a particular way or forum.

[84] On the other hand, it is apparent that the Agency had made a decision on the inclusion of non-rail debt before the Call Letter went out. To that extent, CP was confronted with a *fait accompli*. It is always more difficult to persuade someone who has already decided a question, than someone who is considering a question. But even this could be overcome if the Agency was prepared to consider CP's submissions with an open mind, that is, with a willingness to change

its position as a result of CP's submissions. The only way to determine this is to examine the Decision.

[85] CP began its submissions to the Agency by pointing to the provisions of the UCA which make it clear that only rail-related amounts incurred by the regulated entity are subject to inclusion on the regulatory balance sheet. In this case, this referred to debt incurred to fund share buybacks, a non-rail use of capital, undertaken by CPL, which is not a regulated entity.

[86] The Agency responded to this by pointing to section 1203.05 of the UCA which provides that:

> 1203.05 The rail division will become involved from time to time in non-rail activities, which will result in transactions which will affect current assets and current liabilities, and, in some cases, on a temporary basis, other assets and liabilities. The UCA balance sheet accounts are to be used to record such assets and liabilities.

[87] The Agency continued by saying that even though transactions are managed through a (separate) treasury function, they may nonetheless impact on the rail entity and must be properly accounted for. This is a reference to section 1203.06 of the UCA quoted at paragraph 27 of these reasons.

[88] The difficulty with this is that section 1203.05 deals with non-rail activities by the rail entity which will affect its assets and liabilities. CP's argument was that share buybacks were activities by its parent company, CPL, which is not a rail entity (*i.e.* a rail division, as defined in section 1000 of the UCA). As a result, the Agency's answer is not responsive to the point made by CP.

[89] In its response to the Call Letter, CP addressed the effect of share buybacks on its operations. CP began by noting that it reports on a consolidated basis the financial holdings and results of all subsidiaries of CPL which are involved in Canadian railway operations. It observed that share buybacks are a CPL corporate treasury function which has no impact on railway operations. CP concluded its remarks with a literary flourish, pointing out that trains do not run faster or slower after a share buyback event.

[90] In response, the Agency took the position that debt issued for share buybacks is rail-related because there is a general corporate benefit from buying back issued shares. It made two arguments in support of this position. The Agency expressed the first argument as follows:

> …The issuance of debt in lieu of issuing more shares to fund rail-related investments lowers the company's cost of capital, as the cost rate of debt issuance is lower than the cost of common equity rate that is expected from investors. Lower cost rates paid by the railway company for its investments might allow it to increase investments in other rail-related projects, or to lower freight rates paid by its customers.
>
> Decision at para. 16

[91] The Agency's statement that the issuance of debt in lieu of issuing shares lowers the company's CoC may well be true, but it is non-responsive to CP's argument. The fact that debt is cheaper than equity is not a reason for including non-rail debt in the calculation of the CoC. Buying back shares using borrowed money is not a way of raising capital since the amounts used to purchase outstanding shares are no longer available to the company to invest in rail-related assets.

[92] The point is not whether the Agency was right but whether its decision was the result of an open-minded assessment of CP's submissions. In my view, it is not. The Agency's response does not engage with the argument which CP was advancing as to non-regulated entities and non-rail expenditures.

[93] The Agency's second argument on corporate benefit was based on CP's 2019 Annual Report which reported that CP had awarded $58 million of stock based compensation, which (according to CP's VRCPI submission) was distributed to approximately 12 percent of CP's workforce. The Agency suggested that the reduction in the number of outstanding shares as a result of a share buyback increases the relative ownership of these employees which may lead to an increase in employee performance.

[94] In this reasoning, the Agency attributes a motivational factor to a shareholder's relative stake in the railway, over and above the motivational value of the share ownership itself. This point about relative ownership is doubtful since shareholders do not own the corporation's assets, but that is not the issue here. The question is whether this reasoning shows a serious attempt to deal with the arguments advanced by CP against the inclusion of non-rail debt on the regulatory balance sheet. In my view, it does not.

[95] If one compares the sophisticated financial analysis in other Agency decisions such as the 2011 Decision to this reasoning, one is struck by its superficiality. Share buybacks may increase each outstanding share's portion of corporate profits and potential share of property upon winding up, but new share issues decrease that notional share, and debt decreases the notional

amount available for distribution on winding up. But the most obvious weakness of this argument is that it was offered only as a possibility. It is simply speculation which is not indicative of a serious attempt to deal with CP's submission.

[96] The Agency then invoked the 2009 Buyback Decision, in which it found that debt incurred for a share buyback was rail-related. The Agency argued that this demonstrates a consistency in decision making but once again, that is not the issue here. The juxtaposition of the 2009 Buyback Decision and the Decision under appeal demonstrates consistency of result but not consistency of reasoning. The only reasoning offered in the 2009 case was that the Agency did not consider "debt incurred for the purpose of buying back shares in a company whose primary, if not exclusive, business line is the railway business to be appropriately classified as identifiable non-rail debt". The decision turned on whether share buybacks could be identified as non-rail debt. CP offered reasons why such buybacks could be identified as non-rail debt, arguments which were not addressed by the Agency.

[97] In addition, the Agency argued that the RTM Decision as to the allocation of debt is an interim decision until the Agency can conclude its consultations about the allocation methodology. With respect, that argument is beside the mark. CP's issue is not the method of allocation; it is whether non-rail debt should be allocated at all.

[98] All of these factors persuade me that the Agency did not give serious consideration to CP's submissions that non-rail debt should not be included in the determination of CP's CoC. The Decision does not grapple in a meaningful way with CP's submissions and gives every

indication that it was written to justify a decision which had already been made. As a result, I conclude that the Agency breached its duty of procedural fairness when it failed to consult with CP or, putting it another way, when it failed to consider CP's submissions with an open mind.

C. *Remedies*

[99] In its memorandum of fact and law, CP asks that the two decisions in issue be quashed and that the Agency be directed to re-determine its CoC on the basis that non-rail debt is not to be considered in the determination of CP's CoC.

[100] As was pointed out earlier, this appeal does not challenge the findings as to commercial paper and working capital in the Decision. For that reason, the Decision and the VRCPI Decision can only be quashed to the extent that they relate to the inclusion of non-rail debt in the determination of CP's CoC and the determination of CP's CoC through a method which includes non-rail debt. CP also asks for a declaration that debt issued for share buybacks is not rail-related and should not be included in the determination of CP's cost of capital and VRCPI. It is not this Court's function to identify what is or is not to be included in a railway's cost of capital when that issue will presumably be the subject of consultation between CP and the Agency. All this Court can do is to set aside the decisions made in breach of the duty of fairness. If the Agency wishes to proceed with the change to the determination of CP's cost of capital, it must give CP a chance to be heard before the decision is made.

[101] I would therefore quash the Agency's determination of CP's cost of capital for the 2020-2021 crop year, and return the matter to the Agency with the direction that CP's cost of capital

for the 2020-2021 crop year be determined on the same basis as it was for the 2019-2020 crop year. This direction is driven by the statutory deadline for making the cost of capital determination which, given the point in time at which we find ourselves, leaves no time for adequate consultation. I would therefore maintain the status quo, leaving it to the Agency to decide how it wishes to proceed. I would also quash the Agency's determination of CP's VRCPI for the 2020-2021 crop year in Determination R-2020-81 and return the matter to the Agency with the direction that CP's VRCPI for the 2020-2021 crop year be determined using the cost of capital determined as directed by this Court.

[102] The Agency has not asked for costs and asks that costs not be awarded against it. CP, on the other hand has asked for costs. When a tribunal such as the Agency appears and provides context as to its procedures and its jurisdiction, it is assisting the Court and should not be ordered to pay costs for doing so. In such a situation, the tribunal neither wins nor loses and should not be treated as if it had. The situation is not the same when a tribunal appears and inserts itself into an adversarial debate against a party who appeared before it and may appear before it again. In that case, the tribunal may well come across as a winner or a loser and may expose itself to costs. This is particularly so when the tribunal is the only respondent.

[103] CP alleged that some of the Agency's submissions crossed the line and amounted to defending its decision. While I do not necessarily agree, I can see why CP made the allegation.

Some positions were close to the line. But the line was not crossed so I would make no order as to costs.

"J.D. Denis Pelletier"
J.A.

"I agree
D. G. Near J.A."

"I agree
Mary J.L. Gleason J.A."

FEDERAL COURT OF APPEAL

NAMES OF COUNSEL AND SOLICITORS OF RECORD

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