# TABLE OF CONTENTS

**Articles**

- Recent Decisions of the Interstate Commerce Commission
  - Edward J. Schack
  - Bruce M. Kasson
  - Page 1

- An Economic Analysis of Airline Fare Deregulation: The Civil Aeronautics Board's Proposal
  - James C. Miller III
  - Page 15

- Collective Ratemaking by Motor Common Carriers: Economic and Public Policy Considerations
  - Jesse J. Friedman
  - Page 33

- Inedible Tallow, The Maximum Charges Rule, And Other Fables; Motor Carrier Regulation by the ICC
  - Joe Sims
  - Page 55

- The Antitrust Aspects of Oil Company Ownership of Deepwater Ports
  - Christopher A. Hart
  - Page 67

- Recent Developments in the Transportation of Hazardous Materials
  - Russell S. Frye
  - Page 97

- Toward Responsible State Regulation of Air Pollution: Oregon's Mandatory Inspection/Maintenance Program
  - Phillip F. Schuster, II
  - Olivia L. Smith
  - Alan T. Nettleton
  - Page 121

- Coal Slurry Pipelines: A Railroad Perspective
  - Norman M. Lorentzen
  - Page 153

- Commercial Zones and Terminal Areas: History, Development, Expansion, Deregulation
  - Daniel W. Baker
  - Raymond A. Greene, Jr.
  - Page 171
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# TABLE OF CONTENTS

## Articles

- **Work in Progress—The Latest Solution to the Small Shipment Problem**
  Robert E. McFarland .......... 201

- **International Air Transportation: The Effect of the Airline Deregulation Act of 1978 and the Bermuda II Agreement**
  Benjamin A. Sims .......... 239

- **The Scheduling and Route Impacts of Increased Fare Flexibility**
  Mahlon R. Straszheim .......... 269

- **The Impact of Section 13(c) of the UMTA on Labor-Management Relations at BART**
  John G. Kilgour .......... 289

## Motor Carrier Deregulation

- **Price Competition and the Role of Rate Bureaus in the Motor Carrier Industry**
  A. Daniel O’Neal .......... 309

- **Collective Ratemaking: A Case Analysis of the Eastern Central Region and an Hypothesis for Analysing Competitive Structure**
  Andrew F. Popper .......... 365

- **Motor Carrier Regulatory Reform and Its Impact on Private Carriers**
  William H. Borghesani .......... 389
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IN MEMORIAM

MARION FAY JONES
(1898-1978)

With profound sorrow we announce the passing of Marion Fay Jones.

Marion Jones was one of the earliest motor carrier practitioners. He leaves his mark in many ways upon the motor carrier industry. Marion Jones assisted in forming the predecessors of the Colorado Motor Carriers' Association. He was a founder and past president of Motor Carrier Lawyers Association. His energy was further demonstrated in the early days of Transportation Law Institute and the Transportation Law Journal.

Marion Jones' great loves were his family, his profession, and his friends. He enjoyed them all. Marion and his wife Margie, who survives him, made their home in Wheatridge, Colorado. He is survived by two daughters, two sons, 18 grandchildren, and one great grandchild.

Marion Jones was a lawyer's lawyer—a true professional.

Marion Jones never knew an enemy. He was a fierce competitor, but he never took unfair advantage of anyone. All in all, he practiced law with distinction and honor for more than 55 years. Marion Jones truly enjoyed his professional associations and colleagues. He ordered his life around that ancient maxim "strive mightily, but eat and drink as friends".

He leaves us a great legacy of love, affection and enjoyment of family, professionalism and honor in our endeavors, enjoyment and love of friends, and a compassionate understanding of human error.
IN MEMORIAM

HAROLD SAVIN SHERTZ, ESQ.
(1882-1979)

We announce the death of Harold Savin Shertz, Esq., with a deep sense of loss shared by his many friends.

Harold Shertz ("Pop" as he was known to most) was among the first Motor Carrier Lawyers, having been an active participant in drafting the 1935 Motor Carrier Act, a founder of the American Trucking Associations and a Charter Member of the Motor Carrier Lawyers Association. With a practice spanning 62 years, Harold Shertz utilized his energies wisely and profoundly teaching business law, railway law, and highway transportation at the Wharton School of the University of Pennsylvania and assisting in the founding of the Pennsylvania Motor Truck Association.

Endowed with an outgoing personality, Harold Shertz was not only devoted to his profession but also to his family and his friends. He is survived by his son, Robert H. Shertz, of Westtown, Pennsylvania, two daughters, Mrs. Charles G. Roach, of Gladwyne, Pennsylvania, Mrs. Stephen S. Gimber, of Nashua, New Hampshire, eight grandchildren and seven great-grandchildren.

While Harold Shertz was indeed a "Philadelphia Lawyer," he demonstrated forcefully that this not only meant adhering to a high degree of professional competence but also that it should include a true appreciation of friendship and compassion for those that were younger or less experienced.

His passing, while mourned by his friends, shall not occur without a tribute to his substantial and important contribution to the development of transportation law.
ERRATUM

In the article by Philip Schuster, Olivia Smith, and Alan Nettleton in the last issue of this journal, *Toward Responsible State Regulation of Air Pollution: Oregon's Mandatory Inspection/Maintenance Program*, the sentence in text following note 94 on page 139 should read:

A state may also choose to exempt its own vehicles, but this would be ill-considered in light of predictable public hostility.
Recent Decisions of the Interstate Commerce Commission

Edward J. Schack*
Bruce M. Kasson**

I. Operating Rights Generally

The Interstate Commerce Commission has liberalized policies in the area of entry control. Numerous reported decisions in the past calendar year have refined standards used to evaluate applications for motor common and contract carrier authority. These decisions are unique. When viewed separately they open new areas for aspiring entrepreneurs to enter the industry in a wide range of circumstances and when viewed as a whole indicate the Commission's positive commitment to easing entry barriers that had formerly existed while at the same time improving motor carrier entry regulation.

Perhaps the most significant overall policy shift has occurred in the Commission consideration of the motor common carrier standards set forth in the Pan American Bus Lines decision.¹ These standards normally are applied to determine whether or not to grant motor common carrier authority pursuant to the statutory requirement of public convenience and neces-

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* Associate Director, Office of Proceedings, Interstate Commerce Commission. B.A., Ohio State University, 1960; J.D., Ohio State University, 1962.
¹ M.C.C. 190 (1936).
sity. The first of these standards is whether the new operation will serve a useful purpose, one that is responsive to a demonstrated public need.2

Responsiveness to public need was examined in Superior Trucking Co., Extension-Agricultural Machinery,3 which involved an applicant who sought a certificate to transport various kinds of agricultural and industrial machinery from Pella, Iowa, to points in eighteen states. Applicant had been transporting shipper’s size and weight commodities under appropriate authority and the application sought to broaden the commodity authority to enable applicant to provide a complete service. The Review Board denied the application on the ground that shipper failed to show that it had any present need for service which existing carriers could not provide;4 that shipper’s evidence for expanded commodity authority was too speculative, and that shipper’s preference for one carrier with broad authority is an insufficient reason for a grant especially in view of the shipper’s failure to specify any difficulties experienced as a result of using existing carriers. The Division reversed and granted the application concluding that even if existing carriers are not found inadequate in any material respect a grant may be fashioned if other factors require the operation5 and that inadequacy of existing service is not an interchangeable concept with that of the “public convenience and necessity.”6

In Superior, the Division was also influenced by the fact that applicant was already serving shipper and merely sought to broaden its commodity authority, that protestants’ authorities suffered from the same defect as applicant’s, and the finding that a substantial diversion of traffic from protestants was unlikely since shipper would continue to use protestants to the extent of their authority.7

Therefore, even though existing services are not found to be inadequate in any material respect, the confluence of a number of factors in applicant’s favor will result in a grant of authority. Under this principle, the Commission has placed increased emphasis on the fact that applicant can provide an improved service over that which exists today.8 This “improved

2. Id. at 203.
4. Two protestants held authority to handle shipper’s commodities from Pella and a third desired the exclusion of commodities in bulk from the authority.
5. Id. at 297 (citing Patterson, Ext.—York, Pa., 111 M.C.C. 645 (1970)).
6. Id. (citing Ace Freight Line, Inc., Ext.—Canned Goods, 124 M.C.C. 799 (1976)).
7. Id. at 298-99.
service'” theory manifests itself in a number of specific factual contexts, notably: (1) where applicant seeks to substitute single line service for joint line service,9 (2) where applicant seeks to broaden the commodities it can transport,10 (3) where applicant seeks to transport certain special commodities,11 (4) where deadhead miles are eliminated, fuel saved, and energy conservation and efficiency is enhanced,12 (5) where lower rates are a result of the unique service proposed,13 or (6) where the volume of traffic necessitates additional carrier competition.14

The other two Pan American criteria relate to whether existing carriers can meet the public need as well as applicant and whether applicant can meet the need without endangering the operations of existing carriers contrary to the public interest.15 In accordance with these two standards the ICC has granted applications based on applicant's participation in the traffic,16 protestants' lack of full authority,17 the frivolous nature of the pro-


15. 1 M.C.C. at 203.


test, applicant's status as compared to protestant's, protestants' monopoly over the traffic, and protestants' limited or non-participation in the traffic.

Simultaneously, the Commission has liberalized procedural hurdles faced by applicants seeking both motor common and contract carrier authority, most notably those requirements enumerated in the Novak Contract Carrier decision. This applies generally as well as to such specific factual situations as passenger applications, joint line cases, future need cases, and evidence of operations conducted under temporary authority.

II. CONTRACT CARRIAGE

The contract carrier area has also undergone a change in policy direction. While in the recent past the Commission had concentrated on questions involving the criteria of section 203(a)(15) of the Interstate Commerce Act in determining whether to grant a permit, it has now turned its focus on

22. 103 M.C.C. 555 (1967). The decision states: [S]hippers and consignees supporting an application for the transportation of property are asked to "identify clearly" the commodities they ship or receive, the points to or from which their traffic moves, the volume of freight they would tender to applicant, the transportation services now used for moving their traffic and any deficiency in existing service.
Id. at 557.
28. 49 U.S.C. § 303(a)(15) (1970). This section states that a contract carrier by motor vehicle is one who has a continuing contract or contracts: with one or a limited number of persons either (a) for the furnishing of transportation services through the assignment of motor vehicles for a continuing period of time to the exclusive use of each person served or (b) for the furnishing of transportation services designed to meet the distinct need of each individual customer.
on the factors of analysis contained in section 209(b).29

For instance, C-Line, Inc., Extension—New Orleans,30 points out that under the second criterion of section 209(b) of the Act—the nature of the proposed service—the burden on applicant no longer requires a showing that its proposed service is one so specialized that it cannot be provided in ordinary common carrier service; rather, applicant is required to demonstrate the particular needs of the shipper, however normal they may be, and the particular manner in which its service is tailored to meet those needs. In this respect applicant’s burden is similar to common carriage and this process would again require bringing out a number of factual points to be used in applicant’s favor.31

Further, Charter Express, Inc., Ext.—Truck and Trailer Parts32 and White Contract Carrier Application,33 measurably increase protestants’ burden under the third criterion of section 209(b) of the Act—the effect which granting the permit would have upon the services of the protesting carriers to show actual adverse effect. Finally, the fourth criterion of section 209(b) of the Act—the effect which denying the permit would have upon the applicant and/or its shipper has been liberalized. An adverse impact now clearly results to an applicant when the Commission denies an applicant’s first effort to obtain interstate operating rights.34 The implication here is that such applications for initial authority will now rarely be denied.

III. DUAL OPERATIONS

The effects of the Commission’s more liberal attitude are also to be found in the area of dual operations questions under section 210 of the Act.35 The recent case of Delaware Express Co. v. Milford Express, Inc.36


29. 49 U.S.C. § 309(b) (1970). This section states:
In determining whether issuance of a permit will be consistent with the public interest and the national transportation policy declared in this Act, the Commission shall consider the number of shippers to be served by the applicant, the nature of the service proposed, the effect which granting the permit would have upon the services of the protesting carriers and the effect which denying the permit would have upon the applicant and/or its shipper and the changing character of that shipper’s requirements.

30. 126 M.C.C. 228 (1976).


34. Id.

revised the way the Commission had traditionally resolved dual operations problems. Formerly, if a "mere possibility" of discriminatory practices could arise as a result of a grant, the Commission withheld approval of the holding of dual operating authorities. Division 1 has reversed this policy and now holds that if a "realistic possibility," or a "real-world likelihood" of discrimination would not result from a grant, then an affirmative finding under section 210 of the Act should be made.37

IV. HOUSEHOLD GOODS

The Commission has, during the past year, taken a number of actions to provide increased protection for individual shippers of household goods. Carrier estimating practices have been made the subject of an intensive investigation.38 At the time of the institution of this investigation, the Commission asked various respondents (motor carriers, other regulatory agencies, and shippers) a set of questions including: (1) whether estimating should be abolished, (2) whether estimates should be made, binding on the carriers performing them, or (3) whether other changes, besides those involved in the previous questions, would improve the quality of estimating. The Commission is presently analyzing the answers to those questions and a report on that investigation and suggested revisions to the estimating regulations39 will be published shortly.

Additional regulations were adopted to prohibit carriers from collecting transportation charges when all or a portion of a shipment is lost or destroyed in transit.40 In the report adopting those regulations,41 the Commission found that the practice of motor common carriers of household goods of collecting full tariff charges—despite the loss or destruction of goods in transit—was unjust, unreasonable, and, therefore, unlawful.42 The new regulations specify that a carrier may collect only that portion of its tariff charges, including charges for accessorital and terminal services, which corresponds to the portion of the shipment actually delivered.43 These regulations will eliminate many of the hardships experienced by individual

41. 49 C.F.R. § 1056.26 (a), (b), (c) and (d) (1976).
42. 126 M.C.C. at 266.
43. Id. at 278.
householders when carriers attempt to collect charges to which they are not entitled because they have failed to fulfill their promise to carry the shipper’s goods intact to destination.

Steps have also been taken to eliminate unnecessary regulation. The regulations governing the weighing of household goods shipments were modified to provide that the shipper may waive the requirement that a driver’s weight certificate be completed for shipments moving on government bills of lading.\textsuperscript{44} Permitting such a waiver will eliminate documentation which serves no useful purpose for the shipper, the carrier, or the Commission. The Commission also reviewed its requirement that each carrier must compile and distribute to prospective shippers an annual performance report.\textsuperscript{45} The performance reports were found to continue to serve a useful purpose, because they include relatively complete information on a carrier’s ability to provide satisfactory moving service, and they offer the shipper an opportunity to evaluate the risks inherent in using any one of the available household goods carriers.\textsuperscript{46} The performance reporting regulations were modified to give carriers additional time within which to compile those reports and to clarify some of the information carriers are required to furnish to prospective shippers.\textsuperscript{47}

The Commission took steps to control abusive and deceptive advertising by motor common carriers of household goods and their agents. Regulations were adopted which require carriers to specify in each advertisement they place the name and certificate number of the carrier which will originate the shipments which are being solicited through the advertisement in question.\textsuperscript{48} This regulation will protect shippers from unscrupulous carriers who offer to perform interstate transportation services without appropriate authority from the Commission, will ensure that potential shippers are made aware of the identity of the carrier soliciting their business, and will protect those shippers from carriers who offer to perform services which they cannot or will not perform or for which they will not ultimately be responsible.

The Commission’s regulations governing the filing of household goods carrier tariffs were also modified to provide for an extended period of time within which administrative action on proposals to change household goods transportation tariffs which are filed on not less than forty-five days notice of

\textsuperscript{44} 49 C.F.R. § 1056.6 (1976) was reviewed in Ex Parte No. MC-19 (Sub-No. 26), Practices of Motor Common Carriers of Household Goods (ICC order, Nov. 9, 1976).
\textsuperscript{45} 49 C.F.R. § 1056.7 (1976) was reviewed in Ex Parte No. MC-19 (Sub-No. 29), Practices of Motor Common Carriers of Household Goods, 125 M.C.C. 766 (1976).
\textsuperscript{46} Id. at 773.
\textsuperscript{47} Id. at 775.
their effective date must be completed. It is expected that this modified time frame will aid in the orderly processing of tariffs and will, ultimately, benefit the individual shipper by providing additional notice of any impending rate changes.

Finally, new rules were also proposed which would permit household goods carriers to sell insurance to shippers of so-called "third proviso household goods." The Commission indicated in its notice of proposed rulemaking that regulations permitting the sale of insurance only to shippers of third proviso household goods would permit carriers to sell insurance covering loss and damage to shipments to commercial shippers who would best be able to understand the terms of any insurance policy offered. Meanwhile, it would also continue to protect individual householders from the frustration and confusion which arose in the past from their inability to comprehend fully the extent to which their shipments were actually covered under the policies being offered.

V. PASSENGERS

The Commission concluded three significant rulemaking proceedings affecting motor passenger carriers. The first, and most significant proceeding in this area, dealt with the adequacy of services provided by regular-route operators. The proposed rules would have (1) required more responsive information to passengers concerning tickets, fares, schedules, baggage, and other service, (2) provided for improvements in baggage handling and claims settlements, (3) required terminals at each city or community having a population of greater than 15,000 served by a carrier and set minimum requirements for those terminals and other accommodations for passenger comfort and safety, (4) required certain standards for buses relating to temperature control and safety, and (5) required special facilities for handicapped and elderly passengers. In adopting regulations the Commission balanced the benefits from adoption of the proposed regulations against the cost of their implementation and the possibility that adoption would result in increased ticket prices. The resulting rules (1) exempt

50. Third proviso household goods are "articles, including objects of art, displays and exhibits, which because of their unusual nature or value require the specialized handling and equipment usually employed in moving household goods." 49 C.F.R. § 1056.1(a)(3) (1976).
"special operations" from the regulations, (2) delete all recordkeeping requirements, (3) delete requirements for the establishment of 24-hour toll-free information services, baggage checking services, and terminal and reservation systems, and (4) adopt specific standards for making terminals accessible to handicapped passengers.

In the second proceeding, Regulations, Special or Chartered Party Service, the Commission amended its regulations to permit the transportation of a charter party made up of different individuals to be transported on the return movement of what would otherwise be a one-way charter service, so long as the transportation was performed under a single "round trip" charter contract with a particular third party. It is expected that this change will result in a decrease in deadhead mileage, fuel savings, decreases in air and noise pollution, and increased overall energy efficiency. These changes apply to carriers operating under incidental charter rights and to those operating under specific grants of charter authority.

In the third rulemaking proceeding, the Commission enlarged the separate seating section on buses where smoking is permitted from 20% to 30% of available seating capacity to accommodate the average number of bus passengers who intend to smoke on buses.

In one particularly significant motorbus application proceeding, a travel agency sought authority to operate its own limousine in door-to-door service between its customers' residences or businesses and various airports and piers. It was first determined that this transportation service was a for-hire service, and not the activity of a private carrier. Inasmuch as no exemption in the Interstate Commerce Act covered the scope of the operations proposed, it was necessary that applicant receive operating authority in order to conduct these operations. In determining whether the operations would be those of a contract carrier or a common carrier, it was pointed out that, despite the fact that the limousine service would be offered only to customers of the applicant's other travel agency services, these other services were, in turn, held out to the general public. Accordingly, the proposed operation was found to be that of a common carrier. Finally, since the nature of the service proposed included some aspects of both charter and special operations, the grant of authority was framed to include both types of service.

In Dufour Brothers, Inc., Declaratory Order, the meaning of the

55. 125 M.C.C. 10 (1976).
58. Id. at 247.
59. Id. at 248.
60. 126 M.C.C. 1 (1976).
"school-bus" exemption of section 203(b)(1) of the Act was interpreted. The question presented was whether the transportation of school children to and from boarding schools at vacation periods is within the scope of the exemption. It was determined that this transportation service was exempt, because it clearly was transportation "to and from school." Prior decisions involving the interpretation of this exemption had found that a school field trip qualified for the exemption only if it was sponsored by school authorities as an official school function for educational purposes. This requirement was found not to limit the application of the exemption to transportation of school children between home and school.

VI. INTERMODALISM

The Commission has continued to implement its explicit policy of coordinating and fostering the growth of efficient and economical intermodal transportation services. During the past year a number of motor carrier operating authority applications involving ex-water traffic have been considered favorably by the Commission.

In Rogers Transfer, Inc., Declaratory Order, the Commission concluded that a restriction imposed upon a grant of petitioner's operating authority limiting the performance of transportation services to traffic having a "prior movement by water", is analogous to a restriction which requires that the involved traffic have an "immediately prior movement by water." This proceeding involved the motor carrier movement of imported frozen meats from maritime vessels docked at the port facilities of various harbors to the inland facilities of consignees. Occasionally, a portion of the imported traffic would be temporarily stored in a freezer warehouse, and subsequently transported by petitioner's motor vehicles to the ultimate consignee. Petitioner sought a determination as to whether the temporary storage of the involved lading in a warehouse before its subsequent inland movement destroyed its character as traffic having an immediately prior movement by water. The Commission construed the warehouse storage to be of an inci-

61. 49 U.S.C. § 303(b)(1) (1970). This section states: "Nothing in this chapter... shall be construed to include (1) motor vehicles employed solely in transporting school children and teachers to and from school..."
62. Id. at 6.
63. Id. at 3-4.
67. Id. at 452.
dental nature, serving to facilitate the orderly, uncontaminated and convenient transfer of commodities to the motor mode of transportation. It was found that such storage did not constitute a break in the continuity of the through movement of the traffic, and that, therefore, the subsequent motor carrier transportation services performed by petitioner comported with the aforementioned restriction upon its operating authority.\textsuperscript{68}

In another case, \textit{Allen-Investigation of Operations and Practices},\textsuperscript{69} the Commission considered the issue of whether the movement of commodities between two points located within a single State, preceded by a maritime movement in private carriage, was subject to economic regulation under the Interstate Commerce Act. The commodities, bananas, were harvested in Latin America, and were transported by ocean vessel across the Gulf of Mexico to Galveston, Texas. The maritime movement was performed in private carriage. Upon arrival at Galveston, the bananas were immediately transported by motor carrier to Fort Worth, Texas. The Commission applied the rule of the fixed and persisting intent of the shipper at the time of shipment, and concluded that the shipper's intent was that the involved commodities move beyond Galveston. This subsequent single state movement was considered to be one performed in continuous foreign commerce.\textsuperscript{70} The remaining issue was then resolved: whether or not the transportation was subject to economic regulation because the single state motor carrier transportation was performed subsequent to a private carriage movement. The Commission emphasized that the essential issue was not whether the involved transportation was a movement in foreign commerce, but whether it was a form of commerce subject to economic regulation under the Interstate Commerce Act. Because the prior maritime movement was performed in private carriage, the subsequent single state motor carrier transportation was found not subject to economic regulation under Part II of the Interstate Commerce Act.\textsuperscript{71}

With respect to the participation of a motor carrier in through air-surface transportation, section 203(b)(7a) of the Act\textsuperscript{72} establishes a terminal area exemption for motor carriage operations when performed incidental to transportation by aircraft. To be subject to the exemption, the motor carrier segment of the through intermodal movement must be limited to a bona fide collection, delivery, or transfer service of shipments received from or delivered to an air carrier as a part of a continuous movement under a through air bill of lading, within a reasonable terminal area of the area car-

\textsuperscript{68} \textit{ld.} at 454-55.
\textsuperscript{69} 126 M.C.C. 336 (1977).
\textsuperscript{70} \textit{ld.} at 344.
\textsuperscript{71} \textit{ld.} at 349.
rier. If the air carrier is subject to the Federal Aviation Act, the terminal area is that defined by the air carrier's tariff as filed with the Civil Aeronautics Board. If, however, the air carrier is not subject to these filing requirements, the motor carrier operations must be limited to a bona fide collection, delivery or transfer service within a 25-mile radius of the involved airport. The Commission is presently considering regulations which would redefine the air terminal area to embrace a zone within a 100-mile radius of each airport.

Containerization has frequently been recognized as a progressive and innovative means of facilitating the development of intermodal operations. A number of proceedings have involved grants of authority for the intermodal movement of commodities in containers.

VII. DORMANCY

Section 5(2) of the Interstate Commerce Act provides that it shall be lawful for a carrier to purchase the properties of another carrier provided the Commission finds that the transaction will be consistent with the public interest. In determining whether a transaction under section 5(2) is consistent with the public interest, the Commission has been concerned with, among other factors, whether the authority sought to be acquired has been actively used. If not, the authority was found to be dormant. That finding is often fatal to a transfer application, the theory being that the position of competing carriers would be jeopardized by allowing a strong vendee to create a new competitive service with dormant operating rights without a showing of a public need for such service. In deciding when the transfer of dormant operating rights would be in the public interest, the Commission developed two lines of cases: that applicant must show a "public need" before the dormant authority may be transferred or that the transfer will be allowed unless protesting carriers show that they will be harmed.

74. Id.
75. Id.
76. See No. MC-C-3437 and No. MC-C-4000. These proceedings were instituted by notice published in 42 Fed. Reg. 26,667 (1977).
80. See, e.g., Wright Trucking — Purchase (Portion)— Bonded Trucking, 116 M.C.C. 382 (1972).
82. Id.
83. Id.
problem arose as to which side had the burden of proof in the determination of the dormancy issue.

In a recent and very significant decision, Central Transport, Inc.—Purchase—Piedmont Petroleum, the Commission stated that resolution of the dormancy question in an individual case can best be handled through use of a three step test incorporating a shifting burden of going forward with the evidence. Initially, applicants will have to show that the transaction and the sale of the dormant rights, if applicable, will be consistent with the public interest. This would involve a demonstration that the public would receive a benefit from the reactivation of the dormant rights. Then the burden of going forward shifts to protesters who must show that "there is a probability that they will be significantly harmed by the proposed transfer." A mere abstract of shipments and contentions of diverted traffic would be insufficient but a reasonable, substantiated projection of the amount of traffic to be lost coupled with the effect that the loss will have on protesters' overall operations and the effect of such loss on protesters' ability to perform service to the public in the involved communities would be required. If that burden is met, then applicants would be required to present evidence that the transfer should be allowed despite the probability of harm to the protestant. This will ordinarily involve a showing of shipper need for the service similar to that required under section 207 of the Act. Under this tripartite test, the transfer of dormant authority will be allowed whenever applicants make a showing that the transfer will benefit the public, and the protesters, if there are any, fail to prove that it is probable that they will be significantly harmed.

VIII. BROKERS

The most important decision in the area of brokers is Entry Control of Brokers. In that proceeding the Commission considered the present licensing requirements for brokers of property and passengers, operating in interstate or foreign commerce, and the possible formulation of legislation which would amend section 211 of the Interstate Commerce Act. After considering comments on the issues from numerous parties, regulations were adopted substantially restructuring the procedures presently used by the Commission in considering applications for brokers' licenses. These rules

84. 127 M.C.C. 1 (1977).
85. Id at 11.
86. Possible benefits would be elimination of a backhaul, authority meshes with existing operations, and opportunities to make better use of equipment. Id. at 11-12.
87. Id at 12.
88. Id
90. 127 M.C.C. at 13.
eliminate the fee for filing an application for a broker’s license, with the exception of applications for a household goods broker’s license,92 raise the required amount of bonding to $10,000,93 and make a general finding that operation by qualified applicants, as brokers, in interstate or foreign commerce, of passengers and property (except household goods), between all points in the United States (including Alaska and Hawaii), will be consistent with the public interest and the national transportation policy.94 This general finding and issuance of a master license was the basis for a modification of the procedures employed for the licensing of brokers in several respects. Generally, the new procedures, because of the general finding, limit the examination of an application for a broker’s license to the issue of the applicant’s fitness. This will permit the expedited handling of broker applications and offer greater ease of entry into the broker industry for qualified applicants. The brokerage of transportation of household goods was excluded from the new procedures, since the Commission wished to maintain the existing agency-carrier relation in the household goods industry in its present form in order fully to protect the consumer.95 Therefore, applications for a license as a broker of transportation of household goods will continue to be handled under prior procedures.

IX. CONCLUSION

The thrust of recent Commission action, both in the area of adjudicative decisionmaking and in its internal process of reform accompanied by recent rulemakings, indicates a liberalizing trend. Commission regulation is evolving to reflect the present and to be ready for the future. If the law is a living thing, it must grow to adapt to a changing society. This process of change has been accelerating in recent years. Perhaps that is what many people find so upsetting: the rate of change rather than change itself.

In every area that this article has examined, the principle of improving the regulatory process and lessening the burden of outdated policies has been of major importance. The recent staff task force report on improving motor carrier entry regulation has brought about a wide-ranging reexamination of Commission policy and internal decisionmaking. That process will continue. What is essential to the success of that process is that the Commission receive constructive suggestions and criticisms so that we may reach that proper balance between economic regulation and freedom so important to the continued vitality of the American economy.

92. Id at 507.
93. Id at 500.
94. Id at 504-05.
95. Id at 514-24.
An Economic Analysis of Airline Fare Deregulation: The Civil Aeronautics Board's Proposal

JAMES C. MILLER III*

I. INTRODUCTION

This article will summarize the salient features of the costs of and the demand for air service and comment on the proposal issued by the Civil Aeronautics Board on April 13, 1978, which makes interim changes in the ratemaking policies developed in the Domestic Passenger Fare Investigative...

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This article is adapted from a statement the author prepared on behalf of the Federal Trade Commission (FTC) under contract with the Public Interest Economics Center (PIE-C). It does not necessarily reflect the views of the AEI, FTC or PIE-C.
tion (DPFI). In this proposal, the Board outlines modifications in its approach to ratemaking that would cause significant changes in the character of airline competition.

The major features of the Board’s proposal are:

1. "Zone of reasonableness." Within an explicitly-defined zone, air carriers would be free to establish fares with little fear that they would be suspended. Starting from a formula which defines the rate "standard" as a function of distance (a modified version of the present DPFI methodology), the zone "ceiling" would be set equal to the standard, and the zone "floor" would be set at one-half the standard.

2. Market-by-market variation. For a given carrier, the fare charged in markets of equal distance would not have to be the same. Also, by implication, the fare in a market of given distance could be higher than the fare in a market of longer distance.

3. Discount fares and the profit impact test. Discount fares would no longer have to meet the "profit impact test," which requires proof that the proposed discount would increase industry profits.

4. First-class/coach differential. Carriers would no longer have to maintain a fixed, percentage relationship between the fare charged to first-class passengers and that charged to coach passengers.

5. Preference, prejudice and discrimination. The Board’s proposal addresses the "reasonableness" of air fares. It does not alter the prevailing standards with respect to preference, prejudice, and discrimination. Thus, these would not only be grounds for finding a fare unlawful, but suspending it as well.

6. Suspension versus lawfulness. The Board’s proposal is not clear on whether the policy developed with respect to suspension of fares would also apply to ultimate determinations of lawfulness.

This article will first outline salient characteristics of the costs of air service, as broken down into passenger servicing costs, capacity costs, overhead costs, and costs of passenger delay. These cost concepts are highly relevant to issues of setting rate ceilings or floors. Next, the major determinants of the demand for air service will be addressed, with the focus on the concept of demand elasticity. An analysis of the Board’s proposed zone of reasonableness, several fare structure issues, and the ultimate grounds for suspension and lawfulness will follow.

II. Cost Characteristics of Scheduled Air Passenger Service

In analyzing the overall costs of producing air service, it is useful to distinguish among the following components: (a) passenger servicing costs,

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2. Preference, prejudice, and discrimination would still be grounds for suspending a fare. See the discussion of the Board’s proposal infra, "Grounds for Suspension and Ultimate Lawfulness."
(b) capacity costs, (c) overhead costs, and (d) passenger delay costs. The first three components appear directly in the carriers’ cost reports, as shown in Table 1. On the other hand, passenger delay costs appear only indirectly, as a function of the type of service offered.\(^3\)

Simplifying only slightly, the air carrier can be viewed as undertaking two distinct operations in providing air service to passengers. First, there is the "processing" of the passenger. Costs associated with this activity include all of the direct expenses incurred while the passenger is on the ground or in the air, plus expenses of sales and promotion.

| TABLE 1 |
| Operating Costs of Domestic Trunk |
| Air Carriers, Year Ending June 30, 1977 |
| Cost Category | Total Cost (millions of dollars) | Percent of total | Cost per available seat-mile (cents) | Cost per passenger-mile (cents) |
| Passenger Servicing Costs | | | | |
| Passenger service | 1,220 | 10.1 | | |
| Promotion and sales | 1,398 | 11.5 | | |
| Subtotal | 2,618 | 21.6 | 1.03 | 1.85 |
| Capacity Costs | | | | |
| Flying operations | 4,111 | 33.9 | | |
| Maintenance | 1,614 | 13.3 | | |
| Aircraft and traffic servicing | 2,114 | 17.5 | | |
| Depreciation, flight equipment | 688 | 5.7 | | |
| Subtotal | 8,527 | 70.4 | 3.38 | 6.04 |
| Overhead | | | | |
| General and administrative | 497 | 4.1 | | |
| Transport related | 306 | 2.5 | | |
| Amortization | 29 | 0.2 | | |
| Depreciation, other than flight equipment | 134 | 1.1 | | |
| Subtotal | 966 | 8.0 | 38 | 68 |
| Total | 12,111 | 100.0 | 4.80 | 8.57 |


Most of these costs are incurred without respect to the given length of the trip.\(^4\) Thus, they decrease on a passenger-mile basis for a type of service: although total passenger servicing cost is higher for longer trips than for shorter trips, the cost per passenger-mile diminishes with increasing distance. Passenger servicing costs also depend upon the type of service.

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3. See text accompanying note 8 infra.

provided. A "no-frills" service will cost less per passenger or per passenger-mile (for a given trip distance) than will normal coach service. But opportunities for significant savings in fares by reducing passenger servicing costs are somewhat limited, since, as shown in Table 1, they account for less than 22% of the total.

By far, the major portion of the cost of airline service is connected with the providing of capacity: that is, the actual conveyance of passengers. Included here are the salaries paid to flight crews (not including flight attendants), the costs of maintenance and aircraft servicing, fuel expenses, and depreciation of flight equipment.\(^5\) As shown in Table 1, these costs account for a little over 70% of total costs.

It is important to understand that capacity costs—for convenience usually expressed in terms of cost per seat-mile—can vary markedly. First, the turbine (all-jet) aircraft has a much lower operating cost per seat-mile than has propeller driven aircraft. Second, capacity costs (per seat-mile) tend to be lower as aircraft size is increased. This is simply a technical phenomenon; the cost of operating a 300-passenger jet over a given distance will not be 300 times the cost of operating a single-passenger jet (presuming one exists). Third, capacity costs increase with the length of the trip, but at a decreasing rate of increase. Thus, capacity cost per seat-mile tends to be lower the greater the trip distance. There are several reasons for this. For example, a certain amount of expense is incurred in taxiing to and from the runway and this does not vary with the distance traveled. In addition, a certain amount of time and cost is incurred in climbing to cruising altitude and descending to landing altitude; moreover, jet engines operate less efficiently at altitudes lower than cruising altitude. Finally, the per-passenger capacity cost is very much a function of the average load factor.\(^6\) If we assume that capacity costs are not increased when the average load factor increases (a minor simplification), then an increase in average load factor from the present average of around 55% to 65% would reduce the average cost per passenger almost 11%.\(^7\) It should be noted that capacity costs are very much dependent upon average aircraft utilization. Since maintenance and operations costs vary less than in proportion to the number of hours per day the aircraft is in the air, one way of "spreading" capacity costs is to keep the aircraft in operation more hours per day.

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\(^5\) Not included in Table 1 is the cost of capital, most of which would be included under capacity costs.

\(^6\) Load factor is the percentage of seats filled. For example, if on a given flight an aircraft with 100 (passenger) seats carries 60 passengers it has a load factor of 60%.

\(^7\) That is, with a 65% load factor capacity, cost per passenger-mile would decrease to 5.11¢ from 6.04¢, reducing total cost per passenger mile to 7.64¢ from 8.57¢; \([8.57 - 7.64] / 8.57 = 0.109\), or nearly 11%.
The third cost category is overhead. As shown in Table 1, these costs account for approximately 8% of the total. While many of these costs may properly be "allocated" to the passenger-servicing and capacity cost categories, it is notable that they do not represent a significant portion of the total cost of providing air service.

The final cost element is the delay the passenger experiences in obtaining a flight. As used here, delay is a measure of the inconvenience the passenger experiences from not having a flight scheduled at the most convenient time of departure. This is related to the frequency of scheduling and the average load factor, the former being a surrogate measure of the time between flights and the latter being a surrogate measure of the probability of having to catch a different flight because the most conveniently scheduled flight is booked.\(^8\)

As shown in Figure 1, the actual (full) cost facing the passenger is the sum of the four kinds of costs: passenger servicing cost, capacity cost, overhead cost, the waiting time (delay) cost. Since the sum of the former three decreases as average load factor increases, whereas the latter increases (at an increasing rate), there appears to be an optimal load factor for a given market (provided we assume that the nature of costs is given, all passengers receive the same service et cetera).

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\(^8\) G. Douglas & J. Miller, supra note 4, ch. 6.
ing with the optimal average load factor) than the value of the reduction in waiting time.9

Finally, we should note that for a given average load factor, waiting time is inversely related to the density (the number of passengers carried per unit of time) of the market. That is true because, everything else equal, a denser market characterized by a given load factor will have more frequent departures, and thus less time between them.

Another issue to address with respect to costs is that of scale economies. As the Board notes,10 the preponderance of analytical studies conclude that the industry is characterized by reasonably constant returns to scale.11 That is, for reasonable ranges of output, a large carrier will produce air service of a given character at about the same cost per passenger as that of a small carrier. In addition, from the standpoint of the individual firm, the extra or "marginal" cost of adding a passenger on a given flight is much lower than the (average) cost per passenger.12 This relates to the point made above concerning the spreading of capacity costs over more passengers.13 However, if the cost of service as perceived by the passenger is the sum of the costs experienced by the firm and delay costs, then, at the optimal price/service combination, marginal cost equals average cost. The full cost of service is at a minimum and thus, in this dimension as well, the airlines would appear to be characterized by reasonably constant returns to scale.14

A final point to note about the costs of producing air service is that while Table 1 summarizes total and average costs on an industry-wide basis, individual firms may vary significantly with respect to the costs they incur. That is, because of more efficient management, route characteristics, and so forth, one airline may be able to provide air service in a given market at considerably lower cost than another firm.15

The major purpose of this discussion is to emphasize that costs (appropriately measured) may vary markedly from one market to the next and ac-

12. The extra passenger adds only minutely to capacity costs, and thus the cost increase is much less than the average cost per passenger—which includes a proportionate share of capacity costs.
13. See text following note 7 supra.
14. If at the present time, as Douglas and I have alleged, the price/service configuration is that of having an average load factor less than optimal, then it is apparent that for a given flight the passenger's perceived marginal cost is slightly less than the perceived average cost. G. DOUGLAS & J. MILLER, supra note 4.
15. On differences in carrier efficiency, see id. at 141-49.
cording to circumstances. As will be discussed in more detail in Section IV of this article, in certain cases some costs should be considered "sunk" and are not relevant to a determination of efficient fares. This is particularly true of off-peak times of travel. At the other extreme, when there is excess demand for air service, the accounting costs summarized in Table 1 will underestimate the relevant costs of service. In short, the peak periods of service should have allocated to them a much higher proportion of costs than off-peak periods. Also, densely-traveled markets which can be served by larger, more efficient aircraft, will naturally cost less per passenger-mile than lower-density markets which may be more appropriately served by smaller, less efficient equipment. Finally, a very efficient carrier may be able to serve a given market at a cost considerably below that of a less efficient rival. All these cost variations should be taken into account when evaluating the reasonableness of fare proposals.

III. THE DEMAND FOR SCHEDULED AIR SERVICE

The nature of the demand for scheduled air service has been of considerable concern to the Board and the subject of scholarly research. It is also pertinent to the Board's proposal for increasing price competition in airline markets.

For at least a decade, CAB rate proceedings have grappled with the price elasticity of the demand for air travel. This has flowed in part from the "Rule of Ratemaking" requirement that the Board take into consideration, among other factors, "the effect of . . . rates upon the movement of traffic." It has also stemmed from a perception that demand elasticity is very important in determining the effects of rate changes on carrier profits.

Over the past several years there have been a number of econometric studies of the demand for air service. In most of these studies, total

16. Costs are "sunk" if they are incurred no matter what action is taken in the short run.
18. The price elasticity of air travel demand is the percentage change in traffic (passengers per time period) divided by the percentage change in price (fare). For example, if a 10% increase in price led to a 20% reduction in traffic, the price elasticity of demand is -2.0 (in other words, -20% / +10% = -2.0). But if a 10% fare increase leads to only a 5% reduction in traffic, demand price elasticity is -0.5 (that is, -5% / +10% = -0.5). In short, demand price elasticity is a quantitative measure of the relative effect on traffic of a given change in fare. If elasticity is greater than unity in absolute value terms, demand is said to be elastic; if it is less than unity in absolute value terms, it is inelastic.
traffic between points A and B is hypothesized to be a function of the populations of points A and B, the distance between them, the average incomes of the people living at A and B, the price of air service between A and B, and other variables. Then, utilizing regression analysis and actual data, researchers estimate the hypothesized relationship.

The results of this econometric work have varied widely, with many of the differences depending upon the data sets used and the researchers' judgments as to what constitutes an appropriate model. Generally, however, most have concluded that, overall, air service tends to be price-elastic. The percentage change in traffic is greater than the percentage change in price. This finding is of considerable importance, for it means that lower fares overall would not only mean more traffic, but greater carrier revenue. While greater traffic would also mean somewhat greater cost, it appears likely that the increase in revenue would more than offset the increase in cost and thus the carriers as a whole would experience no diminution in profits during the transition period.\(^{20}\)

While there is a general consensus that the demand for scheduled air service is price-elastic, there is also a strong recognition that different markets may be characterized by different demand elasticities. Interestingly, there seems to be no strong conclusion as to whether in short-haul markets price elasticity is greater or less than average. For example, De Vany hypothesizes that because price is a larger component of the full price of service in short-haul markets (counting travel time as a component cost of service), these will be less price elastic than the average. He finds some evidence of this,\(^ {21}\) as does Verleger.\(^ {22}\) On the other hand, Brown and Watkins hypothesize that since there is more competition from other modes of transportation in short-haul markets, these modes will be relatively more price elastic than average. However, they conclude, "[t]here appears to be no tendency for fare-elasticities to decrease (numerically) with the length of trip."\(^ {23}\)

A significant problem with the data used in all these studies is that the differences in air fares for similar markets are very small.\(^ {24}\) Because of the DPFI formula (and for other reasons prior to this formula's promulgation), air fares for similar distances are about the same. This means that cross-sectional analyses\(^ {25}\) have had to focus on very minor fare differences.


\(^{21}\) De Vany, \textit{supra} note 19, at 80.

\(^{22}\) Verleger, \textit{supra} note 19, at 455-56.


\(^{24}\) See Miller, \textit{supra} note 20, at 187-88.

\(^{25}\) These analyses utilized data from many markets for a given time period. An example would be data from the "Top-100" for the year 1976.
The time series analyses are hampered by the fact that, largely due to regulation, air fares have been rather stable (in real terms) and changes typically come in small increments at frequent intervals. The significant exceptions are the intrastate fares in California and Texas, which are significantly lower than comparable CAB-regulated fares. In California, between 1965 and 1971, traffic on the intrastate carriers increased at an average annual rate of 23.3%, as contrasted with a growth rate of 4.7% in all domestic markets less than 500 miles in length. Also, as the Board noted, traffic increased dramatically in the Dallas-Houston and Dallas-San Antonio intrastate markets as a result of the low fares charged by Southwest Airlines beginning in 1971. One tentative conclusion that can be drawn from the Texas experience is that while the demand for short-haul air transportation may be only barely price elastic (or even price inelastic) for small changes in fares, it may have significantly greater price elasticity for large fare changes, at least in the downward direction.

Finally, on this issue of demand price elasticity, a few observations about the Board's conclusion in the DPFI that the price elasticity of the demand for domestic air transportation is -0.7 are appropriate. First, one cannot expect board members to be experts on all facets of airline economics; thus, with all due respect, one should not take this opinion as being final authority on this matter. Second, the Board's decision was the outcome of an adversary process—where the carriers argued strongly that demand is inelastic (-0.5 or less in absolute value terms) and the Board's staff argued that it was elastic (-1.3 or higher in absolute value terms)—and there is the natural tendency for a regulatory commission to compromise somewhere within the range advocated. Third, this elasticity figure was purported to be no more than an average across all markets; of course price elasticity may vary by individual market. Finally, the elasticity finding was not all that important, since in the DPFI the Board departed from its former practice of "cost-plus ratemaking" and adopted instead a methodology basing fares on a reasonable quality of service. The elasticity

26. These analyses utilize data from a single market, covering many years. An example would be the Chicago-Washington market using data from each year 1950-1976.
29. Id. at 43.
31. Prior to the DPFI, the Board's rate-setting methodology was roughly one of determining the costs the carriers incurred in providing service, adding to this a reasonable return on investment, arriving at a rate level and structure that would meet the "revenue need." In the DPFI, the Board recognized that in setting the fare level and structure it was also determining the extent of non-price competition and the quality of service that would be provided. It thus set out to deter-
figure adopted was more a device for adjusting costs than for estimating the reasonable level of fares.

To summarize, it is generally conceded by researchers that, overall, the demand for scheduled air service is price-elastic. This means that if the overall level of fares were lowered traffic would increase by a greater percentage. The result would be an increase in carrier revenue and a sustaining of profits. Individual markets would, however, differ with respect to their response to lower fares; in some markets traffic might increase only slightly, whereas in others the increase might be quite dramatic.

IV. THE CIVIL AERONAUTICS BOARD’S PROPOSAL

In this section portions of the Board’s proposal to enhance price competition in air service will be discussed, drawing on the description of cost and demand just presented.

THE FARE FLOOR

The first question with respect to the proposed fare floor is, “Is it low enough?” That is, will the 50% (of modified DPFI formula) floor allow the kind of price competition the Board envisions and accommodate efficient fares?

As the Board points out, a number of intrastate and interstate fares are at or slightly below the 50% of DPFI levels. While the Board makes clear that rate proposals below the 50% floor would not be suspended if justified, the existence of the floor could be constraining in some instances. For example, in high density, long-haul markets the average optimal fare is quite low in comparison with that assumed in the DPFI formula. In other cases, the optimal fare might reflect very low opportunity costs on aircraft and other resources. Examples would include flights scheduled at the very end of and at the very beginning of the day, flown for the purpose of not only generating traffic but “spotting” equipment. Such off-peak fares would reflect some passenger servicing costs, aircraft operating costs, and maintenance costs, but not much else. Thus, it is easily conceivable that a combination of factors—high-density travel, long-haul market, and low opportunity costs on equipment—would reveal the need for a fare below the 50% DPFI standard.

mine the appropriate service characteristics and to establish the rate level and structure that would bring these about. See G. DOUGLAS & J. MILLER, supra note 4, ch. 8.

32. G. DOUGLAS & J. MILLER, supra note 4, ch. 6.

33. That is, the value of an asset in its best alternative use.

34. For example, placing an aircraft at night where it is needed to begin scheduled service the following morning.
The second question with respect to the proposed fare floor is, "Is it high enough?" The reasons for concern, as the Board notes, is fear of predatory pricing. As various researchers have pointed out, predation is a reasonable profit-maximizing strategy when there are impediments to entry. Thus, for example, on occasion a large firm might drive a smaller firm out of business because once this has happened the larger firm can raise prices and earn sufficient excess profits to offset the losses incurred during the predation period. But the firm can realize this reward only if there are barriers to the entry of new firms. In this context, it is particularly important to note the existence of legal entry barriers into airline service. To enter a new interstate market a carrier must obtain a "certificate of public convenience and necessity" from the Board. Because of this, predation may be a rational strategy, depending on the existence of a viable threat of entry, and this in large measure depends on the Board's policies.

In any event, it should be noted that the pricing flexibility proposed by the Board would represent only an incremental increase in the prospect for predation. The reason is that under the existing regulatory regime predation may take place in the form of service predation rather than price predation. Such a strategy may have made some sense in the past because the Board might have been relied upon to restrain re-entry into the market once a carrier had been forced to exit. In addition, there is some evidence that predation has taken place in isolated instances.

It is quite difficult to establish on a priori grounds an operational rule for policing predatory pricing in airline service. Obviously, some measure of marginal cost is the relevant concept. One problem is that costs are incurred in flight increments whereas the fare is revenue per passenger. The price per passenger established by the carrier depends upon the average load factor achieved or expected to be achieved. For example, one could argue that a fare would be predatory if established on the basis of a 50% load factor but not predatory if the load factor were 80%. Diabolically, one reason for lowering the fare would be to achieve a higher average load factor. A markedly lower fare proposal could thus be based on the carrier's anticipation of being able to realize a substantial increase in average load factor or could be a case of attempted predation. Either case would be difficult to prove.

35. See F. SCHERER, INDUSTRIAL MARKET STRUCTURE AND ECONOMIC PERFORMANCE 198-206 (1970). Of course, a more efficient strategy for the predatory firm would be to buy out (rather than drive out) the rival firm.

There is a need to be concerned about the possibility of predatory price competition but it would be easy to place too much emphasis upon it for the purpose of establishing standards for reasonableness. For one thing, carriers alleging that they are victims of predation could protest not only on grounds of reasonableness but could rely upon Section 411 of the Federal Aviation Act ("methods of competition"). The key, however, would appear to be the Board's willingness to certificate new entry where there is evidence predation has occurred. In this context, there are several strategies the Board may wish to consider. One would be to establish a policy of granting expedited consideration of any proposal to enter a market which had been exited following a round of price reductions. While this might constitute a minor restraint on carrier initiatives to reduce fares (the initiating carrier might be reluctant to have a replacement competitor who received expedited consideration), it would go far in assuring that predatory price action did not occur.

**Fare Ceiling**

The issue with respect to the fare ceiling is balancing the need to constrain monopolistic pricing with the need to avoid constraining certain fares from rising to efficiently high levels. It is possible to identify markets where the efficient fare would be higher than the modified-DPFI standard. For example, while the overall level of fares generally exceed optimal levels, there are instances where the efficient fare exceeds the DPFI standard. This is particularly true of short-haul, low-density markets, which might optimally be operated with smaller equipment and characterized by fairly frequent departures and lower-than-average load factors. Also, a fare ceiling at the DPFI standard level could restrain new, innovative, high-class services which, though higher in cost, might nevertheless be in the consumers' interest. More importantly, there would seem to be a need for increased use of peak-load pricing techniques that would not be fully accommodated by the suggested ceiling. Of course, it is difficult, if not impossible, to establish a priori the appropriate peak fare in any market, but it would seem appropriate to have some dispensation in the Board's program to accommodate this need. Finally, if the ceiling is placed too low, there may be a tendency for carriers to collude implicitly on that rate. That is, it may be tempting in many instances for carriers simply to adopt the DPFI standard because it is the ceiling. If a higher ceiling were established, the probability of having prices set at the ceiling fare would be considerably less.

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38. G. Douglas & J. Miller, supra note 4, ch. 6.
39. An example might be a highly commodious, "luxurious" service in a predominantly business market.
In assessing the need for maximum fares, evidence from markets where fares are not subject to maximum levels is revealing. An example is the commuter market. For distances up to 94 miles, the commuter carriers\(^{40}\) have lower fares on average than the DPFI formula, and for almost any distance they have lower fares than the local service carriers’ allowable standard of 130% of the DPFI level.\(^{41}\) In other words, without maximum fare regulation, the prices charged by commuters were, overall, less than those charged by the carriers subject to maximum rate regulation. This was true despite the use of inherently more costly (on a seat-mile basis) equipment. Similarly, in the California and Texas intrastate markets, where maximum rate control has not been a major issue, fares are significantly lower than the DPFI standard.\(^{42}\)

The Board has requested comments on the suggestion that the ceiling be modified by raising it 5% or by allowing it to be 15% higher on any 52 days of the year of the carrier’s choosing. Both approaches seem reasonable, the latter taking specific recognition of the need for peak-load pricing. However, there are several other suggestions the Board may wish to consider. One is that, since the major concern is for the monopoly markets, the Board may wish to exempt from maximum rate control all competitive markets.\(^{43}\) Another suggestion would be to establish a policy of allowing a maximum percentage rate increase each year for fares above the DPFI standard. In such cases, there would be no suspension, but the burden of proof of lawfulness might be greater than for fares within the zone.

**FARE STRUCTURE ISSUES**

*Market-by-market variations*

The Board notes that within the proposed zone, fares could vary on a market-by-market basis. The DPFI formula and various predecessors all establish the fare as a function of distance. But since the optimal price/quality option is not only a function of distance but of market density, passengers’ opportunity cost on time, opportunity cost on equipment, et cetera, this would mean that the appropriate fares for two markets of equal distance might well not be the same. This proposed policy is also conducive to price competition. The alternative to allowing market-by-market variations is requiring individual carriers to raise or lower all their fares to-

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40. Carriers in interstate scheduled service operating equipment with less than 7,500 lbs. net payload and no more than 30 passengers. They are exempt from federal rate, entry, and exit regulation by the Board.

41. See P. MACAVOY & J. SNOW, supra note 28, at 74-75.

42. See generally W. JORDAN, supra note 27; P. MACAVOY & J. SNOW, supra note 28.

43. Such a policy, incidentally, might have the additional effect of reducing carrier resistance to new entry.
gether; however, this would severely limit the incentive to take price initiatives and would make it easier for carriers to collude.

First-class fare differential

The Board proposes to eliminate established differentials between first-class and coach service. Historically, the role of first-class service has been to give passengers the option of more commodious accommodations and increased attention from flight personnel. It has also served as a means for allowing a passenger expressing a strong preference to be accommodated on a particular flight the option of doing so by paying more than the coach fare. The institution of having the two types of service, the fare differential is important. The optimal differential will vary by market, depending on such factors as the distance of travel, the age and income distribution of the passengers, and personal preferences about service. Thus, it would seem wise in a regime where carriers are allowed to price compete in individual markets also to allow them to adjust the first-class differential in response to market forces.

Discount fares and the profit impact test

Another major departure from historic policy is the Board's proposal to eliminate the "profit impact test" as a necessary condition for the approval of discount fares.

Discount fares have several roles. First, during the 1960's they were the primary means for lowering the average level of fares as the carriers realized the economies of turbine-powered aircraft. Discount fares were also, arguably, the only means available for incipient price competition. A carrier wishing to take competitive price action would usually stand a much better chance of having such an initiative approved by the Board if it were characterized as a discount than if it were viewed as a simple case of price-cutting. Another very useful role of discount fares is to acquaint passengers with a new service. This is similar to advertising in the following sense: in

44. The system thus, in a rough way, approximates the scheme outlined by William Vickery, Vickery, Responsive Pricing of Public Utility Services, 2 BELL J. ECON. & MANAGEMENT SCI. 337 (1971). Notably, load factors in first class average less than load factors in coach service.

45. Another decision variable is how to divide the aircraft space allocated to each section, by moving the bulkhead.

46. This position should not be viewed as inconsistent with the view that a first-class differential should be established on the basis of the average (and marginal) costs of the two types of service. The difference is that under the Board's proposal carriers would be allowed to make changes in the differential unilaterally (that is, compete), whereas heretofore the first-class differential has been established on an industry-wide basis. A similar caveat applies with respect to the discussion of discount fares in the next subsection.

47. One reason for this is the subsequent relative ease of eliminating a discount fare (to raise average yield) as opposed to increasing the level of normal fares.
order to attract newcomers a carrier may advertise the existence of the new service and/or offer a lower, "get acquainted" fare.

Another role of discount fares has been to discriminate among passengers on the basis of price elasticity. An example would be lower fares for (price-sensitive) students than for normal coach passengers. As discussed in the section on cost, the provision of air service is characterized by reasonably constant returns to scale, both in terms of the production of service of a given quality and in terms of variations in quality as perceived by the passenger. Under such circumstances, discount fares, other than those of a "get acquainted" variety, cannot be justified on efficiency grounds.

In the past, carriers appear to have proposed discount fares whenever market circumstances were such that the result would be to increase industry profits. This is the crux of the profit impact test. Superficially, such a proposal would seem to be in the public interest: the carriers would earn higher profits, and at least those consumers taking advantage of the discounts also would be made better off. But over the longer run, the existence of the excess industry profits would lead to their being bid away by increases in scheduling and other amenities. Thus, for a given quality of service, some passengers would pay in excess of the average (and marginal) cost of that service, while others would pay less. In short, there would be ("dead weight") inefficiency losses in both the discount and regular-fare markets.

The Board's proposal, however, would not lead to this type of inefficient outcome. Each carrier would be allowed to make unilateral decisions about which discounts to offer and how much differential is appropriate. Just as one does not find price discrimination in competitive markets, one would not expect to observe widespread instances of inefficient discount fares under the reformed regime outlined by the Board. The result would be discounts for off-peak travel, similar to those in the intrastate markets in Texas and California. These are very desirable. But differential fares for a given service based on perceived groupings of passengers and their demand elasticities would be the exception rather than the rule.

**Grounds for Suspension and Ultimate Lawfulness**

In its proposal, the Board clearly indicates that the new standards for suspension would apply to reasonableness grounds only, and not to preference, prejudice, and discrimination. This raises questions about whether the proposal as outlined would fulfill completely the Board's intent

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48. This is what economists call third degree price discrimination.
49. G. Douglas & J. Miller, supra note 4, at 65, 97-98.
of bringing about a price-competitive market for air service. First, in the past, preference, prejudice, and discrimination have seldom been used as grounds for suspending a tariff, the reason being that it was easier to protest a competitor's lower rate on grounds of reasonableness. If it were made more difficult for carriers to protest on reasonableness grounds, they might be expected to increase their reliance on preference, prejudice, and discrimination arguments. Second, historically, significant rate changes have been of an Ex Parte nature—across-the-board increases or decreases, that preserved the existing rate structure. The Board's proposal for market-by-market variations, plus freedom with respect to the first-class fare differential and discount fares, would undoubtedly raise more significant questions about preference, prejudice, and discrimination. This is not in any way to criticize the Board's proposal to reform the reasonableness test. It is, however, to suggest that the Board may wish to establish a similar, more liberal policy with respect to preference, prejudice, and discrimination to assure the goal of enhancing price competition in air service.

Perhaps more important is the standard for the ultimate lawfulness of fares. Although the Board's proposal is not altogether clear on this issue, it would appear that the zone of reasonableness, the liberal rule with respect to market-by-market variations et cetera, are designed to be standards for suspension only. The question thus arises over the standards for determining whether a fare is lawful once it has been the subject for investigation.\textsuperscript{51} Obviously, if the reasonableness criterion for ultimate lawfulness is the same as that proposed for suspension, the likelihood of a significant increase in the price competitiveness of air service is much greater than if the existing (or even modified) DPFI standard prevails.\textsuperscript{52} The market for air service would be much more efficient if the liberalized standards for suspension were also adopted as the test for lawfulness. If such a per se approach were not feasible, then the adoption of a policy making such fares prima facie reasonable (thus putting the burden of proof that they were not reasonable on the protesting party or parties) would be significantly better than having as the standard some version of the DPFI standard. For if the latter is the case, carriers would have much less incentive to price compete, knowing there is some probability of having to incur litigation costs. Many lower fares would survive only during the investigation phase, and the Board might find its workload increased dramatically because of a need to investigate numerous fare initiatives.

\textsuperscript{51} It also relates to the revised grounds for successfully obtaining suspension outlined in the Proposed Rule, at 16. (The first of three requirements is that "there [is] a high probability that the fare would be found to be unlawful.")

\textsuperscript{52} More competition also would be generated if the standards for preference, prejudice, and discrimination were relaxed.
V. CONCLUSION

The Board's proposal represents a timely and significant initiative, one that is very much in the public interest. As the Board notes, the airline industry is characterized by cost and demand conditions which make relying on market forces to determine fares and services an efficient approach. There is not only evidence of the efficiency of price competition in intrastate air markets, but such evidence is also available from numerous markets having similar characteristics. For example, restaurants, movie theaters, barber shops, and many other service industries are characterized by fluctuating, "unstable" demands and "perishable" outputs—two phenomena often cited in differentiating the airline industry and justifying for it special treatment. Yet, these other industries operate very efficiently, and few could propose price controls as a means of improving their performance. In short, the Board's reasoning is sound in finding that the public interest would be served by increasing carriers' freedom to compete on the basis of price.

Within a broader context, the Board's initiative should be viewed in terms of its importance in changing the competitive "rules of the game." Since in the airlines, as in many industries, decisions made today affect service years from now, it is important that carrier management have firmly in mind the circumstances that will govern competition in the coming years. In this connection, the force of the Board's resolve to implement new rules is laudable. But more important is the need for the Congress to change the basic regulatory statute.53 For a Board that can use its discretion under the Act to change policy so much for the better might under different circumstances discharge its responsibilities in a way which was not consistent with the public interest.

Collective Ratemaking by Motor Common Carriers: Economic and Public Policy Considerations*

JESSE J. FRIEDMAN**

I. INTRODUCTION

The justification for collective ratemaking in trucking and for the antitrust exemption that makes it possible must in the last analysis turn upon how the public interest is affected. The public interest necessarily embraces the interests of all groups affected by trucking service—carriers, shippers, communities, consumers. Each is relevant and important, but not to the exclusion of the others, and it is elementary that to achieve equitableness among all a balancing process is unavoidable.

Shippers are entitled to minimize transportation costs, but not by exacting favored treatment over competitors, and the shipper’s interest in the transportation he buys extends not only to the quality and the cost of the service but to a reasonable degree of stability in the rates he pays. Rates must not exploit the users of trucking service and place an unjust burden on

* Based upon testimony presented to United States Senate Judiciary Committee, Subcommittee on Antitrust and Monopoly, May 22, 1978. For a review of the historical background and basic aspects of the same general subject, see the author’s COLLECTIVE Ratemaking in Trucking: The Public-Interest Rationale (1977).

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ultimate consumers, but still must be high enough to permit carriers to finance the amount and kind of service the public wants and needs. Carriers should be motivated to vie for the traffic of customers, but not by undermining competition among the enterprises they serve or the communities in which those enterprises are situated. Communities have a right to expect that rates to resident industries will reflect any natural advantages of location, but they have no claim to preferential rates having nothing to do with superior location. Clearly, the interest of the public as a whole demands not simply the lowest possible rates, but the lowest possible rates consistent with economic soundness in the broadest sense of that term.

Collective ratemaking, by definition, involves a limitation on motor-carrier price competition and, when carried on under procedures required by statute or prescribed by the Interstate Commerce Commission, is exempt from the antitrust laws.\(^1\) Some critics choose to refer to rate bureaus as "cartels" and to collective ratemaking as "price-fixing" or "collusion" that "would be a felony in most American industries."\(^2\) Colorful as such phrasing may be, it is merely a pejorative and inflammatory expression of the simple, prosaic, straightforward fact that with respect to the pricing of common carriers in surface transportation, including trucking, Congress has authorized a limited departure from usual antitrust policy considerations where collective ratemaking furthers national transportation policy.

Competition has a deservedly high place in the roster of public policies that help to promote the economic interest of the nation. As a matter of common observation and experience, the prod of competition can be, and frequently is, the most reliable means of assuring good economic performance in the public interest. In general, there is a public policy presumption in favor of competition. But there is no iron law of public policy that competition must, without exception, play exactly the same role and take exactly the same form in every type of economic activity in the country. In special situations, where Congress recognizes that rigid application of antitrust strictures would defeat rather than promote the public interest, it modifies the basic policy of competition and implements that modification by means of an antitrust exemption. No opprobrium attaches to the resulting moderation of competition. The exemption is merely a formal recognition by Congress that unusual circumstances are involved.

A congressional decision regarding an antitrust exemption always reflects a choice between alternative impacts on the public interest. When Congress confers antitrust immunity upon farmers to permit them to price

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and market their crops or livestock collectively, it is making a public policy decision that in this area of the economy collective selling of output can be more beneficial to the public interest as a whole than unrestrained competition or, stated in reverse, that unrestrained competition would be more harmful to the public interest than collective pricing would be. In the case of motor freight transport, the policy of Congress for the past thirty years has been that the public interest as a whole is better served by permitting carriers a carefully controlled freedom to price their services collectively than by insisting on conventional price competition.

Good public policy requires that whenever an area of economic activity is freed from the operation of the antitrust laws, the procedures under which prices are established and the prices themselves should be subject to stringent public control to make sure that the interests of affected groups in the economy are properly protected. The controls exercised over Interstate Commerce Act rate bureaus meet this requirement. These controls are unquestionably far more strict than the controls applied to other areas of antitrust exemption.

For example, ocean shipping rate conferences enjoying antitrust immunity are permitted to operate under agreements that contain dual-rate provisions designed to penalize shippers who patronize non-conference carriers, and conference members have no right of independent pricing action. Insurance companies subject to state regulation are exempt from antitrust no matter how weak or inadequate that regulation may be. The prices charged by antitrust-exempt agricultural marketing associations apply not only to the products of their own members but to those of nonmembers which they may handle in substantial volume, and those prices, as well as the procedures under which those associations operate, are for all practical purposes completely unregulated.

The situation is quite different with respect to motor carrier rate bureaus. Every provision of every agreement under which a rate bureau operates must be approved by the Interstate Commerce Commission standing as the guardian of the public interest, and no agreement may be approved except on a specific finding of the Commission that national transportation policy considerations justify an exemption from the antitrust laws. Each carrier belonging to a rate bureau is assured the "free and

8. Id. § 5b(2), (9).
unrestrained right to act independently with respect to any rate at any time without sacrificing the eligibility to remain a bureau member and act on other rates. Regardless of size, all members have an equal vote. Shippers are free, without suffering any economic penalty, to give any portion of their traffic at any time to carriers that are not members of the rate bureau. Rates established through a rate bureau govern only the traffic of its members. All rate actions of a rate bureau are subject to the closest regulatory review:

1. Changes in the general rate level or rate structure must meet regulatory standards of reasonableness and must be supported by extensive data specified by the Commission.

2. The relationships of rates to each other must meet stiff legal tests concerning discrimination and preference and prejudice affecting shippers, industries, communities, points, or any particular description of traffic, and these tests are the same for rates established by a rate bureau as for rates established by an individual carrier (whether or not a bureau member) acting alone.

3. The Commission is authorized to suspend or investigate any rate proposal.

4. Every shipper or other interested party, individually or through an organization, has the right to file with the Commission an official complaint challenging any rate bureau action as unjust or unreasonable or otherwise unlawful.

5. Any complainant dissatisfied with a Commission ruling may appeal to the courts.

Compare this thorough system and degree of regulatory control with the kind of control which exists concerning prices established by agricultural marketing associations, which sell collectively on behalf of agricultural producers about $40 billion of farm products annually. Under the Capper-Volstead Act of 1922, which exempts agricultural marketing associations from antitrust, an association is not limited to handling the products of its own members; up to half of its business volume may consist of the products of nonmember producers. A Capper-Volstead marketing association, by itself or by agreement with another such association, may control up to 100% of the market for any farm product it handles. No association is required to notify a government agency of its prices, and no agency has

9. Id. § 5(b).
10. Id. § 316(a), (g).
11. Id. § 316(d).
12. Id. § 316(g).
13. Id. § 316(e).
14. Id. § 316(f).
authority to act in advance to prevent such prices from going into effect. In some associations, voting power is not the same for each member but is in proportion to the amount of capital stock or membership capital owned. The Secretary of Agriculture is empowered to institute proceedings at any time to determine whether the practices of any marketing association have unduly enhanced prices and to issue a cease and desist order, enforceable in the courts, to restrain the offending practices. No other government agency is authorized to proceed against a marketing association on account of unduly high prices. No private party has a right to bring such a suit. Only the Secretary of Agriculture has the power to act against unduly enhanced prices, but in the 56 years since the antitrust exemption and the accompanying investigatory and enforcement power have been on the statute books no proceeding has ever been held.

II. RATE BUREAUS AND CARRIER COMPETITION

Although collective ratemaking operates to limit price competition among motor freight carriers, competition is far from eliminated. The competition that remains is substantial and vigorous, and takes a variety of forms.

There is first the basic right, reserved by law, for every carrier belonging to a rate bureau to act independently of any bureau action concerning rates or other tariff matters. While restrictions upon price competition are inherent in the very nature of collective ratemaking, it is a mistake to downplay, as some critics are wont to do, the moderating influence of independent action, both actual and potential, upon those restrictions.

Membership in a rate bureau is optional on the part of carriers serving the bureau territory, but every carrier becoming a member has this statutory right of independent action. As a result, no carrier may be bound against its will. The right of independent action is an unqualified one; it may be exercised by a carrier’s declining to go along with a rate change concurred in by others or by establishing a rate change unilaterally, and it may be taken before, during, or after any rate-bureau decision. Congress, in providing for antitrust exemption for collective ratemaking in 1948, recognized the crucial importance of assuring such a right of independent action, and made it an absolute condition of any approval of a rate bureau agreement by the Interstate Commerce Commission. The railroad rate bureau agreements struck down by the Supreme Court fifty years earlier as violative of the Sherman Act contained no such unequivocal right of independ-

18. Id.
ent action.\textsuperscript{19}

The Commission has placed tight safeguards around the right of independent action and it represents an important source of competitive pressure upon rates. Both large and small carriers have invoked the right of independent action when their interests, or the interests of shippers they serve, have required it. Most of the independent actions taken by carriers involve rate reductions.

The role of the right of independent action in the collective ratemaking system is an interesting one. The right itself is an important part of the statutory and regulatory design for antitrust exemption, and the timely and judicious employment of that right is an essential means of safeguarding the public interest in motor carrier rates by making sure that no carrier may be committed, merely by the operation of majority rule, to any rate to which he objects, either on his own behalf or on behalf of a shipper he serves. At the same time, it is evident that if invoked indiscriminately so that, contrary to congressional intention, independent actions became more the rule than the exception the public purposes served by collective ratemaking would be undermined.

There is no way of judging the effectiveness of collective ratemaking or of the right of independent action from the numbers of such actions alone. The numbers themselves depend upon the technical definition of independent action. More importantly, the competitive significance of the right of carriers to establish rates independently cannot be measured simply by the independent actions officially taken. Students of antitrust are familiar with the role that potential, as well as actual, competition can play in affecting business behavior, and the impact of potential competition is seen in the processes of motor carrier ratemaking as in other fields of the economy. Even when not actually pressed to the point of formal unilateral rate publication, the power of any carrier to price independently can and frequently does exert a decisive competitive influence on the rate actions of other bureau members.

From time to time one hears it alleged that the competitive significance of independent action is of little consequence because it may be assumed that the more powerful members of a rate bureau will succeed in coercing the less powerful. Evidence of such coercion is lacking and there is no reason to give any weight to that assumption without some substantiation of its validity. Interference with the "free and unrestrained right of independent action" would, of course, be clearly unlawful.

Aside from the actual and potential competitive pressures arising from the right of independent pricing action, competition among bureau mem-

\textsuperscript{19} United States v. Trans-Missouri Freight Association, 166 U.S. 290 (1897); United States v. Joint-Traffic Assn., 171 U.S. 505 (1898).
bers for traffic on the basis of the quality of the service provided is marked by the same kind of intensive struggle for business as occurs in many other industries on the basis of product or service quality. It is unrealistic to regard competition in factors other than price as a substitute for price competition, but it is equally unrealistic from a public-interest standpoint to ignore the competitive importance of rivaling for the favor of shippers by means of modern equipment, expeditiousness and reliability of service, adaptation of service to specific transportation needs, and similar factors which can be of crucial importance to shippers. And nothing in the collective ratemaking process interferes with the vigor of these forms of competition.

On any given traffic lane, competition among carriers within a bureau embraces both the services offered by carriers with single-line authority on that lane and the multiplicity of interline services available via joint routings of two or more carriers operating through various points of traffic interchange. Less direct but nonetheless important competition among bureau members occurs between carriers hauling a commodity between one pair of points and carriers of the same commodity to or from a competing point.

Competitive pressures from motor carriers outside the rate bureau membership also affect the level of rates and the struggle for traffic. Such pressures come from the large numbers of carriers in each territory that are not members of any of the major rate bureaus—common carriers that choose to belong to other bureaus or to no bureau at all, contract carriers dedicated to the traffic of one or more shippers under negotiated rates, and, pervasively, shipper-owned private carriers operating truck fleets of varying sizes and, by means of both actual and potential competition, continually exerting a strong downward force on common carrier rates. United Parcel Service, freight forwarders, air cargo, and of course rail transport, including piggyback service, are also, in varying degrees, competitively significant.

On the heavy-traffic lane between Boston and New York, there are 92 member carriers of the New England Motor Rate Bureau offering single-line service. These carriers also provide Boston-New York service in combination with other member carriers via various interchange points, including Providence, Springfield, New Haven, and Hartford. Via Providence alone, for example, all 92 carriers offer joint-line service between Boston and New York in combination with 55 other carriers.

Between Boston and Richmond, there are at least 15 member carriers of the Middle Atlantic Conference operating single-line service. In addition there are 30 joint-line combinations of member carriers operating between these cities via Baltimore, 16 such joint-line combinations via New York, and 10 such joint-line combinations via Philadelphia. Other interchange points include Albany, Hagerstown, Harrisburg, Hartford, New Haven, Prov-
idence, Roanoke, Washington, and Wilmington, and there are still other joint-line routes. Some joint-line routes involve more than two carriers. There are also at least 6 nonmember common carriers, 4 contract carriers, 4 freight forwarders, and UPS actively competing for traffic on the Boston-Richmond route.

Between Philadelphia and New York, a relatively short haul, there are 117 Middle Atlantic Conference members competing for traffic with single-line service. In addition, there are about 20 nonmember common carriers, 11 contract carriers, 4 freight forwarders maintaining class rates, and UPS.

Elsewhere in the country, the pattern is much the same. Between Chicago and Omaha, for example, 25 member carriers of Midwest Motor Freight Bureau compete for traffic alongside at least 30 nonmember common carriers, 8 contract carriers, 2 major freight forwarders, and UPS, to say nothing of 5 major railroads.

On these routes as on innumerable others, the competition from private carriers is ever-present and extensive. The Census of Transportation for 1972, the latest year for which such data are available, shows, for example, that there were 30 major categories of manufactured goods in which private motor carriers hauled one-fourth or more of the freight tonnage moving by all forms of transportation. In these categories, the share of the total motor carrier traffic tonnage hauled by private fleets ranged from 28% to 78%.

III. JUSTIFICATION FOR COLLECTIVE RATEMAKING

Special factors make collective ratemaking in trucking indispensable to the public well-being. They all are rooted in considerations of a practical nature. Where there are thousands of carriers providing service, thousands of commodities being moved, tens of thousands of geographic points to be served, millions or more of point-to-point combinations, countless carrier interline routes and connections, a staggering number of individual rates, and awesome complications of competing origins, destinations, and products, practical considerations in ratemaking can not be either wished away or lightly dismissed as matters of mere convenience which can be overcome with a little technological ingenuity. These considerations are:

1. There is no other practical way by which the level of motor carrier rates and the relationship of rates to each other can be effectively regulated as the public interest demands.

2. There is no other practical way to prevent, or at least minimize, the damaging effects upon the economy of serious discrimination in the prices paid for motor carrier service by large and small shippers who are in competition with each other.
(3) There is no other practical way to preserve a well-coordinated network of motor carrier service required for efficient and expeditious distribution of the vast variety of goods which move to and from every corner of the economy by truck.

(4) There is no other practical way to assure the degree of rate stability and certainty producers and distributors must have in order to plan current and projected production and marketing operations efficiently.

(5) There is no other practical way in which the highly desirable involvement of shippers in monitoring and influencing the ratemaking process can be systematically provided.

A. Effectiveness of Rate Regulation

It is assumed here that the continued regulation of rates to protect the public is regarded as desirable. In the absence of collective ratemaking, effective regulation would literally be impossible.

Under existing regulation, rate levels on traffic in each rate-bureau territory are controlled by Commission actions applicable to all of the carriers belonging to that bureau. While the Commission is armed with extensive financial and traffic data of the bureau member carriers, individually as well as on a group basis, its determinations that rate levels are sufficient, but no more than sufficient, to meet reasonable revenue and income needs, are made for the carriers as a whole. This process makes it possible to keep within manageable proportions the task, that would otherwise be necessary, of reviewing mountains of detailed historical and pro forma information on the revenues, expenses, profitability, and traffic of thousands of individual motor carriers and determining the reasonableness of rate levels, structures, and relationships on a carrier-by-carrier basis.

If carriers were barred from establishing rates in common and rates were established individually, each carrier would propose its own rates. The Commission would have to determine the revenue and income needs of each carrier separately in order to rule on the reasonableness of its individual rate level. It would also have to rule on the reasonableness of the rate structures and the reasonableness of individual rates in relation to each other for each individual carrier. The enormity of such a regulatory burden and the scale of the regulatory machinery which would be necessary to cope with it at all, much less satisfactorily, defy description. And these towering difficulties would be compounded by gigantic problems of enforcement.
B. Discrimination, Preference, Prejudice

In a system of individually-established rather than collectively-established rates, flagrant discrimination, preference, and prejudice, with serious impacts upon shippers and localities, would be inevitable, not only because of the breakdown of regulation but because of the inherent nature of a system of individually-established rates.

If regulation of rate levels, rate structures, and rate relationships of carriers on the basis of individual costs and individual revenue and income needs produced significant differences in rates among carriers, the result would be severe competitive inequities to affected shippers and localities served by different carriers. If it is argued that as a result of competitive pressures such rate differences would be eliminated, a question might well be asked as to what purpose would be served by following a circuitous and disruptive course to rate uniformity already prevailing under collective ratemaking. But there is in fact the strongest likelihood that competitive forces would in many cases produce serious sustained rate disparities, and that discrimination, preference, and prejudice would be rampant.

The most common and most difficult problems of discrimination, preference, and prejudice arise not in terms of disparities in rates charged by the same carrier providing trucking service to two shippers of the same commodity under the same conditions between the same origin and destination points, but in connection with the rates charged by different carriers to competing shippers located at the same or different points of origin or destination or both. Where the same carrier charges different rates to shippers of the same commodity under the same conditions between the same points, the practice is on its face unlawful, and in the absence of a regulatory failure, enforcement could presumably be relied on for a remedy. Where different carriers and the same shipper are involved, the problem is one of competition and is not normally a matter for public concern. The more serious problem, however, arises in connection with a more subtle and vexatious, but potentially decisive, form of rate favoritism. That problem derives from the ability of an economically powerful shipper in one locality to gain from the carrier or carriers serving him rates that are more favorable than those a less powerful rival, located there or elsewhere in the territory but competing for the same markets—or located at the same point but receiving similar raw materials or components from the same or different origins—is able to obtain from a different carrier or carriers on whom he must rely for service.

Rate favoritism of this kind toward giant shippers controlling large volumes of traffic would surely be unavoidable under a system of rates established by individual carriers without collective action. Each carrier in its own traffic market would be responding in accordance with normal com-
mercial principles and motivations, and no single carrier could legitimately be accused of itself engaging in discrimination. The plain reality of the situation is that it is not a sufficient protection to the public interest in fostering healthy competition either among carriers or in the industries dependent upon motor transportation that any one carrier abstain from rate discrimina-
tion. To achieve the parity of rates among competing shippers that good public policy requires it is necessary that the rates charged by carriers as a group be non-discriminatory. That result can be achieved only by collective ratemaking. The vital principle of equitableness of rate relationships achieved by the collective ratemaking system is that, apart from extraordi-
nary circumstances, the rate charged by a member carrier of a rate bureau for moving any class of goods under given conditions between any pair of points is the same as that charged by any other member carrier, not only between that pair of points but, mile for mile, between any other pair of points in the territory—regardless of the size or power of the shipper.

C. **COORDINATED SERVICE**

Its growth has been made possible by, and requires for its continua-
tion, a highly developed national transportation system. The National Transportation Policy speaks wisely of the national need for a coordi-
nated transportation system. A coordinated network of trucking service is a natural and vital part of such a system. No carrier, no matter how large, has or can have single-line access to and from each and every point in the country requiring trucking service. Total coverage requires the integration of all common carrier services in a Nationwide network of single-line and joint-line operations which together make it possible to reach every part of the country from every other part by common carrier service.

Coordination in terms of a national policy designed to promote the public interest as a whole means more than the physical hookup of the carriers. It means establishing a system that permits taking advantage of opportunities for service efficiencies, increases the competitive service alter-
 natives available to shippers, and assures that every region, community, or locality requiring service will receive it at the same rate regardless of the single-carrier or combined-carrier routings by which it is reached.

Traffic patterns and densities and the imperatives of efficient operation can favor the choice of an interline over a single-line route. Interlining can serve the cause of carrier operating efficiency by routing freight over inter-
change points where loads can be broken down for consolidation with other shipments consigned to the same ultimate destinations. It contributes to shipper efficiency by making available routings that fit in with a desired

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distribution pattern. It permits carriers lacking single-line authority to join with others to compete with the single-line services of other carriers. And it protects the competitive position of shippers and communities at those points which are reached only by joint-line service by holding down the rate for any particular movement to that which would be charged on a mile-for-mile basis if single-line service were available; in the absence of such a "through" rate, a substantially higher charge, representing the combination of applicable local rates, would be incurred.

The collective ratemaking system makes it possible to maintain a complete interlock of interline arrangements among all the carriers serving the territory, with the same rate applicable over all joint routes regardless of the innumerable combinations and permutations of interchange points and participating carriers involved, with all through rates equalized with the applicable single-line rates, and with a uniform basis of divisions of the through rates among the interlining carriers. Such total interlacing of trucking service across the nation is inconceivable without the machinery of collective rate action by all the carriers concerned and the antitrust immunity which makes it possible. It is not simply a matter of one carrier entering into a joint rate and service arrangement with a non-competing connecting line, raising limited if any questions of antitrust. What is involved is a total pattern of service interconnections among all the carriers in a territory, including carriers in direct competition with each other, and the establishment of a vast profusion of joint carrier routings competitive with each other and with the single-line carriers participating in the joint routings. And what is also involved is an equalization of rates via all such services for a given movement. Clearly, this could only be accomplished by the process of collective ratemaking.

In the absence of collective ratemaking, the advantages of the present total interline network of motor carrier service joint routes and through rates would be lost or drastically impaired. The scope of the problems and the likely course of events in the absence of collective ratemaking need to be fully appreciated.

There are about 3,500 member carriers of the major rate bureaus. Many individual carriers have joint-line arrangements with literally hundreds of other carriers. One major carrier interlines with more than 1,200 carriers. An interline arrangement ordinarily covers all the points at which the interlining carriers have terminals where freight can be interchanged, and each joint-line arrangement applies to the rates applicable to each of the large number of commodities moving over the multitude of routes concerned. Were rates to be established individually instead of by collective carrier action, the sheer magnitude of the task of negotiating the innumerable complicated terms of the many interline agreements required would deter many
carriers from establishing joint routes and through rates with others, except where advantageous from the standpoint of their own operations.

Interline service is generally more costly than single-line service. Revenue divisions of carriers participating in through rates on interline service are frequently substantially lower than the single-line revenues earned over the same route to or from the point of interchange. Under these circumstances, carriers could be expected to rely to a much greater extent than at present upon their own single-line services in lieu of interline routings. The spread between lower charges in single-line service and higher charges in interline service as a result of combining local rates would inevitably lead to a curtailment of interline service save for those routes where no single-line alternative was available or the maintenance of a joint routing happened to serve the individual interest of the carrier controlling the traffic. Many carriers, especially smaller ones, are highly dependent upon the revenues they derive from sharing in interline traffic. They would be severely damaged by the loss of interline traffic, shippers and communities dependent upon interline service would be saddled with a rate handicap, the efficiency of trucking service as a whole would suffer, and an important aspect of the national policy of a truly coordinated transportation system would be undermined.

D. Rate Stability

In addition to the reasonableness of rate levels, structures, and relationships, shippers must be able to rely upon a fair amount of stability in the transportation charges they pay. Stability of rates is not a substitute for reasonable rates, but there is no doubt that in many commercial activities, including transportation, the purchaser regards the need for a reasonable degree of price stability as inseparable from the need for a reasonable price itself. Under present inflationary conditions costs are continually rising, but there is a marked difference between cost uncertainties resulting from inability to predict the future, an inability shared by all, and cost uncertainties generated by confusion and discrimination. Businessmen do not prize cost stability as a security blanket to insure a "quiet life" in the competitive world but because universally, one of the most disruptive forces in business planning—of plant expansions, distribution programs, marketing strategies—is uncertainty as to costs, including, and sometimes especially, transportation costs, and when that uncertainty extends to the transportation costs paid by competitors the disruption is multiplied.

Collective ratemaking insures a high degree of rate stability for shippers. A system of individually-established rates would be at the opposite pole in this respect in important ways such as lack of ready ascertainability of prevailing charges and tariff conditions under the welter of alternative rates and routes available. The burdens would fall most heavily on small
shippers with limited resources and sophistication for dealing with the intricacies of transport tariffs.

E. SHIPPER INVOLVEMENT

One of the most useful aspects of the collective ratemaking system is the opportunity it provides for active involvement of shippers in the discussion and debate of carrier rate proposals before they are acted on, and in the submission of proposals of their own. The rate bureau machinery affords the shipper the unusual means of simultaneously proposing desired rate changes to all of the carriers serving him in a given territory, and of simultaneously responding to rate changes proposed by one or more of the carriers. Whether the rates proposed affect the rates of a shipper or his competitor, each has an opportunity to be heard on equities and impacts of the proposal, to come forth with alternative approaches, or, without waiting for a carrier proposal, to suggest needed changes and improvements in the rates to correct inequities or meet problems created by special market or supply situations. If rates were established by individual carrier actions rather than collectively, a shipper would not only be forced to negotiate with each carrier or combination of carriers separately, but would have no opportunity to air, challenge, and reconcile diverse views of different carriers serving him and his competitors at the same or different points.

The system assures the shipper of a timely and ample opportunity of a hearing; it does not guarantee that he will get what he wants. There is, after all, no more reason to assume that all shipper proposals are meritorious than that all carrier proposals merit approval. No sensible system could be based on either one assumption or the other. Under the collective ratemaking system, the important safety feature is that a federal regulatory body, not an organization of carriers, has the last word as to the reasonableness of carrier rates that are charged.

Given the enormous administrative apparatus inherent in the establishment of rates however accomplished, the collective ratemaking system—with its strong emphasis upon shipper participation in discussions with carriers and upon the opportunity for hammering out differences before formal rate proposals are placed before the Commission—has the distinct advantage of tending to minimize protests and the concomitant burdens of litigation. The right to protest formal rate actions filed with the Commission is not affected but there is a chance for objections that might otherwise result in protests to be ironed out in advance. In the case of general rate increases or major rate restructurings by weight brackets, actions which have a broad effect upon shippers generally, protests by shipper organizations and suspensions and investigations by the Commission in the exercise of it its powers are an indication not that the collective ratemaking system is
not working but that the results of collective action are being subjected to
the close regulatory scrutiny which good public policy contemplates.

IV. PRICES AND PROFITS

Collective ratemaking produces important public benefits and the various forms of competition for traffic exert a restraining influence upon the prices charged the public for motor carrier service. But the ultimate protection of the public interest lies in the all-embracing array of powers with which Congress has equipped the Interstate Commerce Commission for the purpose of regulating rates. Armed with these powers, the Commission is in a position to make certain that the level of rates established by collective pricing is no higher than economically necessary to provide good service, that rate structures are reasonably related to costs, that individual rates are equitably related to each other, and that industry profits are not excessive.

So long as rates as a whole are held to levels that are not unreasonably high in relation to the total costs of service, the public's interest in assuring that collective pricing is not producing inordinate returns for the carriers as a whole is protected. It is not essential from a public-interest standpoint that the profitability of each carrier should be identical. Differences among carriers with regard to route structures, traffic composition, operating efficiency, marketing or administrative skill, or managerial effectiveness generally, will inevitably result in differences reflected in the profit and loss statement. Variations in carrier profitability are not a cause for public concern. Where carriers experience different costs, uniform profitability could only be achieved if the rates charged by the various carriers were also different. Such rate differences would be neither competitively viable nor publicly desirable.

It is fallacious to assume, as some commentators seem to do, that cost variations among individual carriers are necessarily attributable to variations in operating efficiency. Carrier differences with respect to such factors as traffic density, length of haul, route congestion, size and handling characteristics of shipments, and quality of service can produce differences in unit cost having nothing to do with efficiency as such. Nor are such cost differences necessarily correlated with profitability. Some of the most profitable—and reputedly most efficient—carriers have relatively high unit costs that merely reflect their manner of operations.

Another fallacy which has received wide currency is that the effect of general uniformity of rate levels established under collective ratemaking is to protect inefficient carriers and stultify incentives for improving efficiency. It is true that under collective ratemaking the general uniformity of rate levels established are geared to the weighted average costs of handling the
traffic in the ratemaking territory so as to produce a degree of profit which is reasonable for the carriers as a whole. But this is a far cry from gearing rates to the costs of the least efficient carriers. As noted, profitability will vary under the uniform rate levels established. But the system reinforces rather than undermines incentives for efficiency improvement. Carriers whose costs are high because of inefficiency will suffer low profits, or losses; carriers whose costs are held down by efficient operation will be rewarded with higher profits. And every carrier, regardless of its relative efficiency at present, will be motivated to operate with increased efficiency in the future in order to maximize its profits.

Aside from rate levels as a whole, it is essential to establish a structure of rates applicable to major shipment-weight categories. The collective ratemaking process seeks to establish rates for the various weight categories in relation to relevant costs, with rates scaling downward as shipment weight increases. The costing techniques used are those either established or approved by the Commission. Cost allocation is far from scientific, and it is not surprising that efforts to structure rates by weight categories in relation to costs should be disputed by shipper groups facing increased rates. Such disputes are for the Commission to decide on the basis of the best evidence which can be applied. But the basic effort to structure rates in relation to costs for different shipment-weight categories must be regarded as economically sound and equitable.

Carrier profitability is frequently measured in terms of return on investment. The return on the capital dedicated to a transportation enterprise is a significant, though not the only, indication of whether or not a reasonable profit is being earned. It is capital that is at risk in a business and the relation of profit to that capital must be adequate to preserve the capital from impairment, reward investors, and induce new investment in modernization and expansion to enable the carrier to serve the public well.

To the extent that rate of return is used as a measure of adequacy of earnings and thus of revenues, however, it is essential to calculate the return in a way that makes proper allowance for the impact of sustained inflation upon the economic cost of supplying transportation service. And it becomes absolutely mandatory to do so before any valid comparisons can be made between the profitability of one carrier with that of another or between the profitability of motor carriers as a group with that of other industries or of industry generally.

There is perhaps no more fundamental proposition in modern economics than that the economic cost of any resource, including capital, consumed in producing a product or service is the "opportunity cost" of the resource. That is economists' shorthand for the basic concept that a company's real cost of capital, for example, is the return that could be earned on that capital in some other use. In order to express return on investment
in sound economic terms, it is fundamental that asset values included in the investment base must be expressed in terms of current replacement cost, not in terms of historic cost as reported in conventional financial statements. In economic terms, the capital invested in an enterprise must be valued not by the original acquisition cost of the physical assets of the firm but by the cost of re-creating the equivalent productive capability of those assets at today's market prices. Similarly, the allowance for depreciation, which reflects the consumption of the capital tied up in fixed assets, must be based upon their current replacement cost rather than their historic or original cost. The necessity to view return on investment in these economic terms has become imperative because of the heavy inflation which the economy has undergone and which has introduced such distortions in asset valuations and in depreciation allowances based on these valuations that conventional accounting measures both of profit and of investment are out of touch with reality.

As the Department of Transportation said in a recent filing with the Interstate Commerce Commission: "'In an inflationary period, reliance on historical asset cost misrepresents the asset's value, and, indeed, the entire financial posture of the firm, because the historical cost bears little relationship to the actual, current value of that asset.'" 21

The growing spread in the economy at large between depreciation based upon current replacement costs and depreciation based on historic costs has become so significant in the eyes of responsible government economists concerned with the validity of basic national economic measures that corporate profits based upon historic-cost depreciation are no longer regarded as valid. The corporate profit figures now used in the official National Income and Product Accounts (NIPA) published by the Department of Commerce have been restated to reflect depreciation allowances based upon current replacement costs. As is well known, the NIPA measures of national economic activity and its various components provide the statistical underpinning for basic national economic policymaking by the Council of Economic Advisers, other executive departments, and the Congress.

Two years ago, the Securities and Exchange Commission determined that the inadequacies of conventional financial statements with regard to data on asset investment and profits of corporations required that such data be supplemented by data based upon current replacement costs. Present SEC rules require corporations to show in regular financial statements filed with it the current replacement costs of fixed assets (and inventories) and the amount of depreciation expense based on such costs "to enable inves-

tors to obtain more relevant information about the current economics of a business enterprise in an inflationary economy than that provided solely on the basis of historical cost."\(^{22}\)

Attention has been called to the fact that some motor carriers have earned higher rates of return on equity capital than some corporations in other industries. The inference is that the favorable profit rates of these carriers are the result of insulation from price competition under the collective ratemaking system. The data used in making these comparisons are taken, without any adjustment, from financial statements in which both the asset values included in equity capital and the depreciation expense reflected in profits are based upon original or historic costs rather than current replacement costs.

Accounting data are meaningful for accounting purposes. But it can be stated unequivocally that measures of return on equity drawn from conventional financial statements reflecting original or historic costs can not provide a valid basis for comparing the profitability of one enterprise or industry with another or with industry generally. It can be stated unequivocally that no valid inference concerning competition or monopoly power (the economist's term for insulation from competition) can be drawn from profitability comparisons unless such comparisons are based on economic, as opposed to accounting, concepts of profit and investment.

The irrelevance of an accounting measure of return on equity in determining whether an enterprise is excessively profitable or in evaluating questions of competition or monopoly power is well understood and accepted by economists. As Professor Bain stated many years ago: "The unadjusted accounting rate of profit as computed by the usual methods from balance sheets and income statements, is *prima facie* an absolutely unreliable indicator of the presence or absence either of monopoly power or of excess profits. . . ."\(^{23}\) Or as Professor Machlup later expressed it: "[T]here are several fundamental pitfalls in the idea that the accounting rate of profit can show the degree to which monopoly power is exercised . . . . But we know for certain that . . . unadjusted accounting rates of profit . . . cannot be accepted as a measurement of the degree of monopoly."\(^{24}\) Similarly, Professors Douglas and Miller have emphasized the "classic distinction between economic costs and accounting costs." "A price which remains low, consistent with a normal return on accounting costs, will result in deteriorating service," they stress, adding that "for efficiency to obtain, prices


must reflect economic costs.\textsuperscript{25} Numerous studies analyzing the accounting and economic profitability of many different companies and industries have been made, not only for regulatory purposes but also for internal management use. These studies show that the effect of adjusting rates of return to reflect the effects of inflation upon true economic profitability can vary widely not only from one industry to another but also for enterprises within the same industry. Such variations can occur even for the same enterprise at different periods. A recent study of the profit position of the intercity bus industry analyzed for that industry the difference between return on equity capital on the basis of conventional accounting data and the return on equity when adjusted for inflation to reflect current replacement costs of equipment and facilities. That analysis showed that for the year ending June 30, 1977, adjustment for the effect of inflation upon current replacement costs of depreciable property reduced the bus industry’s return on equity from 8.1% to 1.3%\textsuperscript{26}. The conviction among economists who have studied these matters that accounting measures of return on investment cannot, without substantial adjustment, be used with any assurance of validity to indicate either that profits are excessive or that competition is inadequate can be illustrated by referring to the financial data of one of the largest motor common carriers, Consolidated Freightways, which last year had motor freight revenues of about $650 million and total corporate revenues of $1.1 billion. The accounting financial statements filed with the SEC show that for the corporation as a whole the return on equity capital was 24.4%.\textsuperscript{27} Data on current replacement costs, filed with SEC under the new regulations can be used to adjust the accounting return on equity for the corporation. (Similar data are not reported for the motor carrier subsidiary alone.) While replacement-cost data involve an unavoidable degree of estimating, the data submitted conform to the SEC guidelines. Using the same approach used in making studies of profitability in other industries to adjust reported profits and investment for the effects of inflation, the corporate-wide return on equity for Consolidated Freightways is reduced from 24.4% to 12.8% after adjustment for the current replacement costs of fixed assets, and to 13.6% if adjustment is made for the replacement costs of inventories as well as of fixed assets. Before any significant comparison could be made between the true profitability of the motor carrier business of Consolidated Freightways with the returns earned by corporations in other industries it would be necessary to make adjustments of the profit and investment data both for


\textsuperscript{26} J. Friedman, Revenue and Income Needs of the Intercity Bus Industry (1977).

\textsuperscript{27} Consolidated Freightways, Inc., Annual Report (Form 10K) to Securities and Exchange Commission for fiscal year ended December 31, 1977.
the motor carrier subsidiary and for the corporations with which it is compared.

V. ECONOMIES OF SCALE

Repeal of the antitrust exemption for collective ratemaking in trucking is sometimes urged by advocates of substantial deregulation of both rates and entry in the motor carrier industry. One of the main premises on which proponents of such deregulation rely is the statement that there are few if any economies of scale in trucking operations. This view is so frequently repeated that it deserves at least passing scrutiny. An examination of the published literature dealing with economies of scale in trucking lends support to a number of observations and opinions:

(1) The analytical problems are intrinsically difficult in the extreme and the analyses themselves are of widely varying depth, perceptiveness, representativeness as to carrier size, number of relevant variables covered, and quality of reasoning. There are wide differences as to a proper definition of economies of scale and as to proper approaches for measuring them.

(2) The conclusions vary also. Some investigators believe that there are significant economies of scale in trucking, some believe that there are not, and some are undecided or have mixed judgments on the matter.

(3) The cost data relied upon are limited to what is available. The quality of the available data is poor for the purpose in hand. Statistical techniques applied range from low to high degrees of sophistication. None of the analyses has succeeded in filtering out extraneous factors, nor is there agreement as to what factors are extraneous.

(4) All of the cost information is of an accounting nature. None of the data has been converted into economic costs. As in the case of profitability analysis, only economic costs would be valid in reaching conclusions as to relative economic efficiencies.

(5) No allowance has been made for the influence of quality of service on cost.

Noteworthy in this connection is the significant comment contained in a recent report of the Council of Wage and Price Stability dealing with carrier purchases of operating authority. Practically every such purchase increases the size or scope of the acquiring carrier’s operations. The Council expresses the opinion that a purchase of operating authority “is in almost all cases likely to increase the efficiency of trucking.”

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VI. CONCLUSION

How is the public interest, as reflected in the National Transportation Policy, affected by collective ratemaking in trucking? The brief answer is that the public gains advantages that are obtainable only through collective carrier action and, while foregoing some of the possible benefits of rate competition among carriers, avoids the damage and inequities that unrestricted competition would bring.

In the absence of collective ratemaking, the regulatory process, which affords the ultimate protection to the public interest, could not function effectively. It would be impossible to control rate levels, prevent excessive profits, assure reasonable and equitable rate structures and relationships, or forestall flagrant discrimination, preference, and prejudice. The present system, by contrast, makes it possible to achieve these goals while subjecting all collectively made carrier actions to the closest scrutiny of the Interstate Commerce Commission for its approval or disapproval.

The present system is not perfect, neither is any other human institution. As has been said in another connection, some dissatisfaction with a system of this kind would be inevitable even if the process were presided over by the Archangel Gabriel himself. Whatever may be regarded as the drawbacks of the present system, the best justification for its continuation is the widespread economic disruption which its discontinuation could cause. From the standpoint of the public interest, which must be the paramount consideration, the system is better than any alternative which has thus far been suggested.
Inedible Tallow, The Maximum Charges Rule, And Other Fables: Motor Carrier Regulation By The ICC

JOE SIMS

INTRODUCTION

There seems to be constant confusion about the interest and role of the Department of Justice in motor carrier regulation. We do have both an interest and a role, although I could probably get unanimous agreement only on the first of those. I will try in this article to explain why we are interested and what we see as our appropriate role.

You will undoubtedly be relieved to find no discussion of the Yak Fat case. But I have a more recent substitute—a story about beer and wine. Some years ago, the Interstate Commerce Commission decided that wine was a "grocery product" and therefore could be transported by those trucking firms that hold Commission licenses to carry grocery products or "prepared food products." Wine, according to the ICC, was "little more than fermented fruit juice, a potable liquid ... classified as a grocery." 1

Recently, a trucking firm tried to get the Commission to extend this

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rationale from wine to beer. This firm, which already held a license to carry grocery products and prepared food products, also wanted to carry beer. It argued that beer has greater nutritional value than wine, that it is frequently consumed as part of a meal by many people, and that it is used as a cooking ingredient. In any event, it argued, beer is clearly no less a foodstuff than wine.

But the ICC was not about to allow itself to get trapped in a seamless web of simple logic. The Commission held that beer, unlike wine, is not a foodstuff because what various commodities really are does not depend on the "academic or literal definitions found in dictionaries." The Commission pointed out that those trucking firms that already hauled beer might be injured if other trucking firms that currently haul foodstuffs were also allowed to haul beer. On the other hand, the Commission said, those companies who would like to haul beer, but cannot, would not be injured by a refusal to permit expansion of their operations. Therefore, since one side might have been hurt by declaring beer to be food, and the other side would not have suffered by refusing to declare beer to be food, beer was found not to be food.

If you had trouble following that reasoning process, consider a case reported recently in the Washington Star. Trucker A filed an application for a license. Trucker B opposed it and asked for his own license covering the same route. The ICC granted trucker A's request. Trucker B then petitioned for reconsideration. The ICC, until it could make a final ruling, postponed the issuance of the license to Trucker A. Meanwhile, Trucker B won his license. The ICC ultimately ruled that because there was already a trucker on the route—Trucker B—and there was not enough business to support a competitor, the original ruling that awarded the license to Trucker A had to be reversed.

Stories like this circulate about every government agency, but there seem to be a lot of them about the ICC. In addition, this type of "reasoning," if you'll pardon the expression, encourages a lot of otherwise capable ICC practitioners to write very silly things. For example, the Department of Justice was involved in a proceeding before the Commission in which a carrier was attempting to obtain new operating authority to transport inedible tallow. In a reply brief, one of the protesters argued:

The evidence shows the principal shipper's "tallow" is in fact not tallow at all but in all cases a mixture of pork fat. As demonstrated by any dictionary, tallow

3. Id. at 237.
4. Id. at 239.
is derived from cattle; pork fat from pigs; and this Commission has consistently over the years held that a "petroleum" product cannot be transported on "petroleum" authority; a "molasses product" on "molasses" authority; "vegetable oil" on "vegetable oil product" authority or "chemical" authority. . . .

This poor fellow was obviously not familiar with the beer and wine cases, and did not realize that the dictionary carries no weight in ICC analyses.

Recently, the DOJ has attempted to have the Commission further protect the right of independent action. We received a lot of interesting comments in that proceeding, but the most amusing one was contained in the reply statement of the New England Motor Rate Bureau. Among other comments on our position and analysis, the New England Motor Rate Bureau took the position that we did not know how to read a tariff sheet, and it went on to point out inaccuracies in our description and analysis of various rate bureau documents. As clear evidence of our ignorance, the brief pointed out:

Ms. Hurdle [a government economist] then states that under item 860, a fifteen hundred pound shipment from Massachusetts to Staten Island, New York was rated at 376¢ per cwt., when in fact, by virtue of supplement 38 to tariff 204-R, the proper rate was 410¢ per cwt. She then states that under item 950 of tariff 204-S, the rate would move to 510¢ per cwt., but completely overlooked the application of the maximum charges rule whereby the 1500 lb. shipment would be billed as 2,000 lbs. at a rate of 336¢ per cwt. resulting in an effective rate of 448¢ per cwt.

We hereby plead guilty to not understanding those kinds of documents, and anyone who does, or claims that he does, ought to be immediately placed under a doctor's supervision.

These examples give you half the reason why the Department of Justice is interested in regulation of the motor carrier industry. Any regulatory scheme that produces this kind of analysis must inherently result in economic waste. But there is more than mere humor, as exemplified in another contribution by an ICC practitioner in the independent action rule-making proceeding: "Additionally, we have found the collective rate-making process a healthy, upward influence on prices which allows many small carriers to get rate adjustments they need to stay in business." The reason for our interest here is much less humorous because it involves the approximately $4 billion that comprises investment value in operating rights of Class 1 common carriers, and the 13% per year capital gain on the value of that

9. Id.
"ticket." 12 The American Trucking Association correctly describes operating rights as a trucker's "single most important asset." This $4 billion is the added cost to shippers, and ultimately to consumers, that results from the current regulatory system which protects the inefficient, preserves historical patterns of operating rights, and requires a participant in the industry to be not only a businessman, but also a gladiator in the literal sense of that word. He must fight his way through the halls of the Interstate Commerce Commission in order to get the opportunity to make and implement a business decision—adding the cost of that effort to his prices.

The rate bureau system of price fixing is another reason for DOJ concern. This method of determining prices allows carriers to agree collectively on the rates they will file with the ICC, or, to put it bluntly, allows truckers to fix the prices they want to set as opposed to having the prices set for them by the marketplace. Those prices might not always be too high but they are almost certainly not the prices the market would set. Government agencies are not qualified to set prices, and the least qualified institution to set prices in the trucking industry in this country is the ICC. There is no reason to assume that the ICC is ever able to set a price which, even at a particular moment in time, not to mention the next day or week or month, reflects a true market price.

It is the rigidity of regulation and its attendant waste, perhaps most simply illustrated by the gateway problem and its close companion, the empty backhaul problem, which costs consumers well over a hundred million gallons of fuel per year according to a recent study commissioned by the Federal Energy Administration. 13 Finally, the inequity of a system that perpetuates economic and social discrimination is disturbing. Its high barriers to new entry and the enormous costs of entry do not permit potential truckers who were previously denied access to the marketplace, because of racial or economic discrimination, an opportunity to rectify that denial. Instead, discrimination on the basis of race is replaced by discrimination on the basis of time because those lucky enough to get entry "tickets" are then perpetually protected from new competition.

These problem areas are the other half of the reason why the Department of Justice is interested in ICC regulation. We have tried over the years to be relatively clear about our interests and the underlying rationale. We think ICC regulation is wasteful, is in large part unnecessary, and is probably unjustifiable on any rational basis. To the extent it can be justified only

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as protecting the interests of the "ins" against the "outs," or as perpetuating hidden cross-subsidies, either geographic or product, which the public might not vote to continue if they knew such subsidies existed, or as giving the industry a convenient tool by which it can "rationalize" its internal competitive structure—there is no excuse for continuing this regulatory system.

DEPARTMENT OF JUSTICE ROLE

Given our interest, and our perspective, what do we see as our appropriate role? To answer that, it is necessary to give you a basic understanding of what the Antitrust Division is and what it does.

The Antitrust Division is primarily a law enforcement agency. Its central mission is to punish hard-core restraints of trade, and try to ensure that a reasonable range of competitive choice exists within markets. But we have a second and equally important mission: to serve as an advocate for competitive policies before regulatory agencies, Congress, and within the Executive Branch. This effort does not include arguing for more competition regardless of its consequences, but it does include encouraging the precise definition of public goals and where possible, pragmatically showing how a more competitive policy can be implemented to enhance consumer choice and/or economic efficiency.

This competition advocacy role occurs on a day-to-day basis, and is sometimes closely related to our antitrust casework, because the courts increasingly look to agency jurisdiction and expertise. At other times, it can involve much broader issues, and perhaps broader relief, in the context of an industry wide rule-making proceeding before a regulatory agency. The benefits of a free enterprise society are widely extolled in the abstract, but frequently shuffled aside in specific situations. It is inevitably the case that those seeking exceptions from the ordinary free enterprise rules, or those seeking to undertake particular anti-competitive activities, are capable and willing to make the case for their proposed course of conduct. Unfortunately, there are rarely advocates of competition policy available with the incentives to make counter-arguments. The Antitrust Division had traditionally tried, within the limits of its resources, to undertake this general role of competition advocate.

Perhaps the most obvious advocacy activity is our participation before the federal economic regulatory agencies. For many years, objective observers, including the Council of Economic Advisers\(^\text{14}\) and both the Neal and Stigler Task Forces,\(^\text{15}\) strongly suggested the need for increased con-

consideration of competitive factors in matters before the regulatory agencies.

The agencies usually receive extensive arguments from industry to the effect that increased competition would be inconsistent with statutory policy and, in some cases, the agency staff is so extended that it cannot critically evaluate a self-serving statement by the regulated parties. Under those circumstances there is often the need for an independent party, experienced in the analysis of economic problems, to bring to the agency’s attention the manner and the extent to which competitive and regulatory policies can be simultaneously pursued in advancement of the public interest.

We have participated in regulatory proceedings requiring an accommodation of the purposes of the antitrust laws and those of regulatory statutes for many years. In fact, the 1969 Stigler Report urged even greater activity by the Antitrust Division, and formalization of its role as ‘‘the effective agent of the Administration in behalf of a policy of competition. . . .’’ Other, such as Senator Kennedy who has reintroduced legislation, originally sponsored in 1977, have also urged a more formal advisory structure which would create a statutory right for the Department to intervene before federal regulatory agencies.

Of course, our advocacy efforts are not limited to agencies. The legislative arena, interagency meetings and conferences are all forums that we use when they seem appropriate. Obviously, some people are a bit uncomfortable with these efforts. They believe that the Antitrust Division should simply enforce the antitrust laws without interfering with agency or legislative matters. The reality is that such lines cannot be drawn so easily.

For example, in 1968, the Division urged the Securities and Exchange Commission to eliminate fixed commission rates on sales of stock on the New York Stock Exchange. We believed that fixed rates, which dated back to the 1700’s, were neither essential to the effective functioning of the regulatory scheme, nor immunized by that scheme from the operation of the antitrust laws. While the SEC considered what action should be taken, a significant amount of private litigation was initiated that challenged fixed commission rates as violations of the antitrust laws. The Antitrust Division intervened as a party in one of those cases. At the same time, fixed commission rates and other competitive issues in the securities industries were receiving a considerable amount of attention in Congress. The Antitrust Division testified on a number of occasions before congressional committees on these issues.

16. *Id.*
18. Comments of Department of Justice, Inquiry into Proposals to Modify the Commission Rate Structure of NYSE (April 1, 1968), 115 Cong. Rec. 15,932 (1968).
Ultimately, fixed commission rates were indeed eliminated, with a resulting savings to the stock buying public of over $680 million thus far, as estimated by the SEC.\textsuperscript{20} But seven years and a combination of legislative, regulatory agency, and law enforcement initiatives were required to accomplish this single objective. Not only would it have been undesirable to our law enforcement interest in this area to avoid participation in forums other than the courts in which the subject was being debated, it simply would have been impossible.

This aspect of the Division’s activities is in many ways illustrative of its special character and responsibilities. It is not just a cop on the beat, nor is it merely a voice in the night, with no authority. The Division is more than just an advocate, and not merely a litigant. It is in many respects a unique institution, and the continuation of these activities brings with them a special responsibility to be open and consistent. Competitive advocacy may occasionally conflict with a particular piece of litigation, but in the long run they are truly complementary.

Placed in this context, our role before the ICC is relatively clear. The ICC is broadly charged with regulating the entry of new firms, their rates and rate-making, and mergers and acquisitions in the motor carrier industry. The ICC has a broad public interest responsibility, and it also has the authority in certain circumstances to immunize transactions from the scope of the antitrust laws. It is quite clear from the underlying statute, case law, and agency decisions that competitive factors are a relevant consideration in almost everything the ICC does. Thus, the Department not only has a particular responsibility to counsel the ICC on competitive impact but it can offer an expertise, in economic analysis generally and competitive analysis in particular, that is highly relevant to the ICC decision-making process.

**DOJ Goals at the Interstate Commerce Commission**

Our principal goals at the ICC have been the elimination of unnecessary restraints on new entry into motor carrier markets and the removal of unnecessary restrictions of competitive motor carrier rate-making. These goals are intertwined. Without the possibility of new entry, rate flexibility simply invites the extraction of monopoly profits by existing carriers and could even lead to predatory pricing. The power to set rates in a market protected from the restraining potential of new entry is obviously subject to abuse. Without rate freedom, eased entry would lead merely to excessive service competition with a continuation of the present inflated rate level, which reflects the average cost of both efficient and inefficient carriers.

We have tried to promote these twin goals in a variety of proceedings at the ICC. For example, our efforts to persuade the Commission to ease entry into motor carrier markets can be described as falling into six categories: (1) relaxation of the "public convenience and necessity standard" for certification of new carriers; (2) prospective licensing of carriers through generalized public convenience and necessity findings; (3) removal of inefficiency-producing restrictions on existing carriers' operations; (4) exemption of traffic from regulation; (5) avoidance of market concentration resulting from mergers; and (6) revision of procedural requirements to facilitate new entry applications.

With respect to competitive rate-making, our efforts have fallen generally into two areas: flexibility to set rates without regulatory review, and restrictions of rate bureau activity. We believe the ICC has authority to permit some rate-making flexibility, and that motor carriers should be given the freedom to decrease rates as they see fit so long as the rates cover out-of-pocket costs. Upward rate flexibility, unfortunately, is another matter. Its feasibility would require the elimination of antitrust immunity for rate bureaus and substantial easing of entry. In this second area involving rate bureau activity, the Division has been active in urging the ICC to exercise its


24. See, e.g., Comment of U.S. Dep't of Justice, Motor Transp. of Property and Passengers Incidental to Transp. by Aircraft, No. MC-C-3437 and MC-C-4000 (filed Sept. 23, 1977); Ex Parte No. MC-37 (Sub-No. 29), Comment of U.S. Dep't of Justice (filed May 24, 1977); Terminal Areas for Express Shipments by Bus, 128 M.C.C. 204 (1977).


authority to restrain anticompetitive rate bureau activities, and we have questioned the Commission's jurisdiction to approve certain classes of rate bureau agreements.

While the Division has some specific interests and goals, our participation before the ICC is largely designed merely to make our views known in a consistent manner with respect to a variety of significant activities that come before the Commission for approval. We have tried, especially in recent years, to maintain a program of regular participation before the Commission. The goals of this program may be stated very simply: (1) to encourage the ICC to undertake a more detailed and reasoned analysis of the anticompetitive agreements and activities that come before it for approval; (2) to bring to the Commission's attention the relevant competitive considerations; and (3) to encourage less anticompetitive solutions and a more competitive market in the motor carrier industry. We think we have been relatively successful, at least in recent years, in meeting these objectives.

Still, the ICC is an old agency, and set in its ways. On any absolute measure, there has been very little recent change despite the efforts made by every administration since President Truman's. In 1948, President Truman vetoed the Reed-Bulwinkle Act, which gave motor carrier rate bureaus immunity from antitrust prosecution. Congress overrode his veto. A Presidential Advisory Committee on Transport Policy under President Eisenhower issued a report concluding that less regulation was needed. President Kennedy described federal transportation regulation as a patchwork of inconsistent and often obsolete legislation and regulation. In 1971, the Transportation Regulatory Modernization Act was proposed, with pricing and entry reforms for both railroads and motor carriers. Hearings were held at that time, but nothing concrete resulted. In 1975, the Ford Administration proposed its comprehensive Motor Carrier Reform Act, which would have resulted in substantial deregulation. The bill received some brief attention in the Senate, but no action was taken. Currently there are several pieces of legislation pending before Congress, and the Carter Administration is examining in some detail the possibilities for legislative change in the motor carrier regulatory system. The outcome of that examination remains

27. See, e.g., Ex Parte No. 297 (Sub-No. 2), Petition of Dep't of Justice for Rulemaking, Proposed Rule to Prelude Automatic Cancellation of Independent Rate by Bureaus (filed May 11, 1977); Reply Statement of U.S. Dep't of Justice, Movers and Warehouseman's Ass'n of America, Section 5a Application No. 4, Amendment No. 4, (filed Dec. 5, 1977).
32. H.R. 7768, 95th Cong., 1st Sess. (1977); H.R. 8973, 95th Cong., 1st Sess. (1977);
unknown, although the reader probably will be able to speculate as to what the Justice Department's position has been and will continue to be.

The key point is there have been few concrete results from all these efforts. Today, of course, the Justice Department is not the only reform advocate in town. The ICC itself has indicated an interest in reform.33 I think it is clear that ICC Chairman, Daniel O'Neal, probably is both one of the most capable and almost surely the most reform-minded chairman in history. I think it is clear that he plans to try to fix some of the more obvious problems. But I think it is equally clear that neither the Chairman nor the Commission can make the kind of permanent changes that are necessary in the system of motor carrier regulation. The ICC Chairmen have limited tenure, as do ICC Commissioners. What may be considered reform today may be considered chaotic and destabilizing tomorrow. The only true reform in a system of government regulation is to remove discretion from the regulators.

**THE POSSIBLE EFFECTS OF DOI INVOLVEMENT**

The DOI can have an impact. Perhaps the best example in recent months is the *Highland Tours* case.34 The petitioner, Scotty Milloy, was a bus operator from Jacksonville, Florida, with a very small business. When he retired as a mechanical engineer a few years ago, he began operating bus tours around Florida which became quite popular. Before long, he received requests to travel interstate so he sought interstate charter bus authority. Greyhound and Trailways Bus Lines protested, as they automatically seem to do for almost every application for competing authority. As a result, Mr. Milloy had to appear a year later at a hearing before an ICC Judge as a supplicant, asking to be allowed into a business of providing interstate charter bus trips. He presented travel agents, school teachers, the Morocco Temple Pilgrimage Committee and the Sons of Scotland Bagpipe Band, among others, as witnesses to testify to their desire for his services on an interstate basis. Greyhound and Trailways, on the other hand, pointed out that Mr. Milloy would be competing with them if he were granted a certificate, and that would divert traffic from them.

Greyhound and Trailways won the case. Five months later, the ICC Judge held that these companies "are entitled to all traffic they can handle economically and efficiently within the scope of their operating authority before a new, competitive service is authorized."35 Mr. Milloy then appealed and the Department of Justice intervened in the case at the recon-

sideration stage. We made every effort to convince the ICC that this was an absolutely silly result, and we attempted to draw public attention to this case as an example of government regulation at its worst. We were reasonably successful since Mr. Milloy and his problem began appearing in newspaper editorials and on television shows. Eighteen months later, the ICC reconsidered, and decided that, in the words of one reporter, "Scotty Milloy and his one-bus bus line aren't likely to bring Greyhound and Trailways to their knees." In the process, and this is the important part from the DOJ perspective, the Commission made some new law when it said:

It is well established that even when the services of existing carriers are not shown to be inadequate, the Commission is not precluded from granting authority based on consideration of other factors, such as the desirability of competition. . . . A carrier first in business has no absolute immunity against further competition. Even though the resulting competition may cause a carrier already providing service to lose revenues, the issuance of new authority may best serve the public convenience and necessity, as we find to be the case here.\(^{36}\)

We view results like these as justification for our participation before the ICC, and we hope to see more opinions with language like that. More importantly, the Department of Justice hopes to see a large number of substantive changes in ICC regulation. While we are not sanguine in the long run about changes effected through Commission decision-making, we are perfectly prepared to accept pro-competitive changes in the short run. The Commission should be supported and encouraged in its efforts to do what it can, within the framework of its statute and within the real world environment of its constituency, to make the system of regulation less onerous, less restrictive and less silly than it has proven to be in years past.

For our part, we will try to continue to support the Commission in its efforts to rationalize the regulatory system. For example, one possible filing we are currently considering would request the Commission to provide for the compilation and organization of information identifying all firms holding common carrier authority between all origin and destination points. We believe such tabulation is essential if the Commission is to meet its statutory responsibilities. In merger and licensing cases, it is necessary that the ICC be able easily to determine the number of carriers and type of service authorized in any market so that it may evaluate the effects of the proposed action on the level of competition. In addition, such a compilation obviously would aid the Commission in enforcing the common carrier obligations of certificated firms. After all, this common carrier obligation is frequently pointed to by advocates for the existing regulatory system as the *quid pro quo* for protective regulation. It seems obvious that the ICC cannot effectively enforce common carrier obligations unless it knows who has them.

\(^{36}\) *Id.* at 603.
Finally, the identification of firms holding authority for particular products in particular markets would be tremendously helpful to shippers seeking the best service available at the lowest cost. There will be other initiatives, and whether they are successful and to what extent depends on how they are received by the Commission. But the DOJ will continue to try before the Commission, within the Administration, and, where appropriate, before Congress, to apply our expertise in competitive analysis to the serious regulatory issues in the trucking industry.

CONCLUSION

Let me caution the reader that he should not think the DOJ had singled out the ICC for our attention or our criticism. Every regulatory agency hears from us, and we usually say things that they don’t want to hear. The ICC has plenty of company. In fact, after a long and arduous search, I finally found an even sillier regulatory episode than Yak Fat. Recently, the District of Columbia Alcoholic Beverage Control Board ruled that restaurants which feature topless and bottomless go-go dancers must allow minors to view the entertainment. Despite the fact that minors were not permitted to purchase or consume alcoholic beverages, the Board said that the City’s human rights law prohibited discrimination by any holder of a restaurant license on the basis of age, with respect to admission. The Board stated that “[we are] not aware of any policy permitting holders of [restaurant licenses] to refuse admittance of minors to a restaurant or to separate them within a restaurant simply because they are minors . . . .” The reader will agree that this holding makes even less sense than the Yak Fat, or the beer and wine cases, or the maximum charges rule, where 1500 lbs. is billed as 2000 lbs. The main difference is that the ICC is regulating a $50 billion industry. How long can the nation afford it?

As MGM’s Sam Goldwyn once observed, 90% of the art of living consists of getting along with people one cannot stand. If that’s true, for an antitrust lawyer at least nine-tenths of the remainder must be learning to cope with a free market that is chock-full of regulatory potholes and fences. We in the Antitrust Division will continue trying to cope.
The Antitrust Aspects of Oil Company Ownership of Deepwater Ports*

CHRISTOPHER A. HART**

The projected United States consumption of petroleum is recognized by most authorities as exceeding by a substantial margin the projected United States production of petroleum for many years to come. In the continuing quest for more efficient methods of transporting foreign source petroleum to the United States, the economies of scale have resulted in the creation of larger and larger oil tankers. There are now in operation very large crude carriers (VLCC's) which are over 1,300 feet long and nearly 250 feet wide.

For the foreseeable future, VLCC's could potentially provide the most efficient means of transporting oil to the United States. However, oil from the Middle East, Africa and Venezuela, which would be delivered to the eastern and Gulf Coast United States' cannot be delivered in a VLCC because the draft (distance from waterline to keel bottom) of a fully loaded VLCC is about 90 feet, and no Eastern or Gulf Coast port now in existence is deep enough to accommodate such a vessel. Thus, the United States

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* The opinions, analysis, and conclusions expressed in this article are solely those of the author and do not necessarily reflect the views of the Department of Transportation.

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1. West Coast ports are not considered in this article because no interest has yet been shown in building a deepwater port on the west coast—perhaps in part because of lack of sufficient refineries and/or transportation facilities (pipelines) to refineries in that area.
cannot now fully enjoy the transportation economies of scale of VLCC's carrying foreign oil.

The inability of the existing U.S. ports to accept VLCC's requires either that the oil be carried the entire distance in smaller vessels, or that it be transferred at some point from a VLCC to smaller vessels. The latter method is presently more cost effective and is used whenever possible, with the transfer occurring either directly, from ship to ship ("lightering"), or indirectly, with an intervening onshore loading and unloading facility, typically in one of the Caribbean or Bahamian Islands ("transshipment"). Deepwater ports would eliminate the need for lightering or transshipment by allowing VLCC's to bring the oil directly to the United States.

A deepwater port is an offshore port facility placed in water deep enough to accommodate VLCC's. The port consists of one or more mooring buoys to which a vessel can secure for the purpose of pumping its oil into a buried submarine pipeline which extends from the buoy to the onshore storage and distribution facilities. In addition to permitting greater realization of the presently available marine transportation economies of VLCC's, deepwater ports offer the opportunity to reduce traffic in many of the congested harbors which now receive large quantities of oil shipments. Moreover, the environmental hazards of shipping petroleum can be reduced by deepwater ports because the number of vessels importing oil is reduced, the total number of transfer operations engaged in by those vessels is also reduced, and the need to navigate near the shores of the locations to which the oil is being shipped is alleviated, resulting in a decreased likelihood of running aground.

In much of the Eastern and Gulf Coast United States, the slope of the continental shelf is so shallow that a port which can accommodate a vessel of 90 foot draft must be many miles offshore. Consequently, the ports in those areas must be constructed beyond the three-mile limit within which the states may exercise jurisdiction. The federal response to the need for deepwater ports, in conjunction with the inability of the states, acting alone, to license or build a deepwater port, was the Deepwater Port Act of 1974 ("Act").2 The Act provides for a "one window" licensing process, by which an applicant submits an application to the Department of Transportation ("Department") for a deepwater port license, whereupon the Secretary of Transportation ("Secretary") is required by the Act to obtain the advice and comment (and for some matters the consent) of other affected federal and state agencies and the public at large, as to the desirability and feasibility of a deepwater port, and is required to decide whether and under what conditions to issue a license.3

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At the time of this writing, two companies have applied for and were offered deepwater port licenses—LOOP, Inc. and Seadock Inc.—both owned primarily by oil companies. LOOP accepted its license to construct a deepwater port off the coast of Louisiana, but Seadock, which would have constructed a port off the coast of Texas, lost its major owners and did not accept a license due to inability to find enough new owners to finance the project. The State of Texas has begun the steps necessary to build a deepwater port at the same location and of comparable size as the port which Seadock would have constructed.

The Act reflects the recognition by Congress that a deepwater port might be owned by oil companies which ship their own oil, and that such owners might operate the port in an anticompetitive manner. This article enumerates the possible anticompetitive effects of oil company ownership of deepwater ports and, in relation to those possible anticompetitive effects, discusses their treatment by the Act, sets forth the recommendations by the Attorney General and the Federal Trade Commission, and analyzes the safeguards incorporated by the Department into the deepwater port license. No attempt is made in this article to analyze the manner in which the antitrust laws could provide a remedy for abuses which may occur in the operation of deepwater ports.

I. Antitrust Problems With Oil Pipelines and Deepwater Ports

Federal economic regulation of transportation common carriers has been precipitated by different circumstances for different modes—it began for the railroads and oil pipelines, for example, because of widespread monopoly abuses, while it began for the airlines to help a fledgling industry develop. Whatever led to economic regulation of such carriers, it was generally implemented with the underlying belief that free competition might not, under the circumstances then existing, produce a system which best serves the public interest.

Most transportation common carriers provide service generally to any eligible member of the public who seeks service. Because this service often

4. "LOOP" is an acronym for Louisiana Offshore Oil Port. It is presently owned by Ashland Oil, Inc. Marathon Oil Company, Murphy Oil Corporation, Shell Oil Company, and Texaco, Inc. Union Oil Company was an owner when the deepwater port license application was filed, but it withdrew before the license offer was accepted. When its application was filed, Seadock was owned by Cities Service Company; Continental Pipe Line Company (a subsidiary of Continental Oil Company); Crown-Seadock Pipeline Corporation (a subsidiary of Crown Central Petroleum Corporation); Dow Chemical Company; Exxon Pipe Line Company (a subsidiary of Exxon Corporation); Gulf Oil Corporation; Mobil Oil Corporation; Phillips Investment Company (a subsidiary of Phillips Petroleum Company); and Shell Oil Company.

involves cooperation among competing carriers, for example, in providing end-to-end joint through service between two points not served by any one carrier—most common carrier statutes permit the economic regulatory agency to exempt from the operation of the antitrust laws various types of agreements between those competitors which might otherwise be unlawful. To assure that each agreement has received scrutiny by the regulators before it goes into effect, the antitrust exemption normally extends only to those agreements which have specific prior approval. Generally the economic regulator can grant the exemption only if it finds that the public benefit which can result from the agreement more than justifies the potential harm to competition.⁶

For oil pipelines, end-to-end intercarrier agreements are not the major source of potential anticompetitive problems. Rather, the potential anticompetitive abuses from oil pipelines derive from a combination of distinct but highly interdependent circumstances unique to the oil industry.⁷ Because deepwater ports are, from an economic and antitrust standpoint, quite similar to oil pipelines, these potential abuses can extend to the ports as well.

A. Owner-Shipper Competitive Advantages

Unlike most transportation common carriers, much of oil transported by oil pipelines is owned by a company which owns or is under common ownership with the company that owns the oil pipeline. Because few other common carriers are owned by industries which have large transportation needs, shippers which own the carriers ("owner-shippers") are rare. One major instance of owner-shiper abuses, that of railroads shipping their own coal, resulted in the addition of the "commodities clause" to the Interstate Commerce Act in 1906.⁸

Conceptually, the most obvious problem created by owner-shippers is that an owner-shipper has every incentive to favor the shipment of its own goods over the shipment of its competitors' goods. This problem has been addressed for oil pipelines by the legislative imposition of the common

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⁶ See, e.g., 49 U.S.C. § 5b (1976) (Interstate Commerce Commission); id. § 1382 (Civil Aeronautics Board). Many of the agreements which have been approved by these agencies have come under considerable attack by the antitrust agencies, among others.


⁸ The "commodities clause" provides, in pertinent part:

It shall be unlawful for any railroad company to transport . . . any commodity manufactured, mined, or produced by it, or under its authority, or which it may own in whole or in part, or in which it may have any interest direct or indirect, except such articles or commodities as may be necessary and intended for its use in the conduct of its business as a common carrier.

carrier requirement to serve the public on a nondiscriminatory basis, and has been addressed in other contexts by other means.

Another undesirable effect of shipper ownership of the carrier is that such ownership eliminates the incentive of the otherwise most interested group, the affected shippers, to press for lower rates before the appropriate economic regulatory agencies. The owner-shippers will not seek lower rates for obvious reasons, and the nonowner-shippers may not seek lower rates for fear of retaliation, however subtle, from the owner-shippers.

The major unresolved problem created by owner-shippers is that both the owner-shipper and the nonowner-shipper pay the same tariff for the same service, as required by the Interstate Commerce Act, but the owner-shipper receives a dividend on its ownership (assuming the pipeline is not a non-profit venture) which effectively offsets part of the rate for the shipment and creates for the owner-shipper a competitive advantage over other shippers. This problem is inherent in oil company ownership of oil pipelines generally, and the deepwater port in particular, without regard to whether the owners are seeking to avoid or to produce an anticompetitive result.

The U.S. government attempted to put an end to the oil pipeline owner-shipper's competitive advantage in the early 1940's when it brought suit against several oil companies and oil pipeline companies, alleging that the dividends of ownership constitute an illegal rebate to owner-shippers under the Interstate Commerce Act and the Elkins Act. With the onset of World War II, the action was settled by Consent Decree. This Consent Decree does not provide that owner-shipper dividends are illegal rebates, but provides that owner-shippers can lawfully receive a dividend which does not exceed 7% of the pipeline "valuation."

On the liability side of a balance sheet, the pipeline company's "valuation" for the purpose of the Consent Decree consists of debt plus equity. Using "throughput and deficiency agreements" as security, many oil pipeline companies are able to obtain debt financing up to 90% of the total original capital input, and the owners must provide only 10% of the original

10. See United States v. Terminal R.R. Assn. of St. Louis, 224 U.S. 383 (1912), relating to railroad-owned corporation which owned both railroad bridges and the only railroad ferry service across the Mississippi River into St. Louis, in which the Court required reformation of various agreements to prohibit discrimination against nonowners.
14. A throughput and deficiency agreement is an agreement either to ship at least a certain amount of oil or to pay for the shipment of that amount of oil even if the oil is not tendered for shipment.
capital input from their own funds as equity. In addition, the ICC has normally allowed debt service to be treated as an expense, to be subtracted from gross income in determining the allowable cost of capital.\textsuperscript{15} The combined effect of the use of throughput and deficiency agreements as security (which facilitates a high debt-to-equity ratio), and the accounting practices which have been allowed by the ICC (which encourage a high debt-to-equity ratio) is that an initial 90/10 debt/equity ratio is common for oil pipeline companies.\textsuperscript{16} As a result, the 7% Consent Decree limit on "valuation" effectively allows a 70% return on equity, initially, and is not in any real sense a limit at all.\textsuperscript{17} Thus, the Consent Decree, in combination with the failure of the ICC to require the inclusion of interest in determining the cost of capital, exacerbates the owner-shippers competitive advantage for oil pipelines.

The recent \textit{Trans Alaska Pipeline System} case may signal a significant change in this situation.\textsuperscript{18} For the first time in many years, the ICC suspended the rate tariffs filed by oil pipeline owners, notwithstanding their "compliance" with the Consent Decree, and indicated that the Consent Decree has served as a measure of lawfulness of dividends under the Elkins Act but has never been used by the ICC as a measure of reasonableness under the Interstate Commerce Act. Moreover, the ICC's calculations of a reasonable \textit{interim} rate included interest within the cost of capital for determining allowable rate of return. If this interim rate standard were adopted as a standard for permanent rates, the allowable return on equity for owner-shippers could be reduced from the present 70% to a more realistic 12-15%, depending on the capital structure of the company. Whether the transfer of ICC regulatory duties to the Federal Energy Regulatory Commission ("FERC")\textsuperscript{19} will alter this ICC trend in the direction of closer scrutiny of oil pipeline rates is not known at this time. However, in view of

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\textsuperscript{15} Most regulatory agencies compute the total cost of capital as the cost of debt (debt service) plus the cost of equity (dividends to stockholders) and compute the allowable total cost of capital as gross income less expenses. In such a context, the company carefully limits its debt-to-equity ratio because an increase in the cost of debt reduces the amount that is available from the total allowable cost of capital for stockholder dividends. The allowance by the ICC of debt service as an expense has the opposite effect. As with any other expense, an increase in the cost of debt which results from an increase in the debt-to-equity ratio provides justification for an increase in the tariff rate to increase gross income, but it does not decrease the amount available for stockholder dividends.

& AD. NEWS 7549.

\textsuperscript{17} This construction of the Consent Decree was affirmed in United States v. Atlantic Refining Co., 360 U.S. 19 (1959).

\textsuperscript{18} \textit{Trans Alaska Pipeline System, ICC Investigation and Suspension Docket No. 9164 (June 28, 1977).} The ICC’s authority to suspend these rate tariffs was recently upheld in \textit{Trans Alaska Pipeline Rate Cases}, 46 U.S.L.W. 4587 (U.S. June 6, 1978).

\textsuperscript{19} The transfer of ICC functions to the FERC occurred under the Department of Energy Organization Act, P.L. 95-51, 91 Stat. 565, §§ 306, 402(b) (codified at 42 U.S.C. §§ 7155,
several recent legislative and administrative efforts to make regulatory agencies more responsive to the broad public interest and less protective of the industries they regulate, a continuation by FERC of this trend is likely, at least in the near future.

B. VERTICAL INTEGRATION

Another aspect of oil pipelines which makes them unique as a common carrier is the extensive vertical integration of the oil industry of which they are a part. Not only do the companies that own the oil also own the oil pipeline, but many also own the oil tankers, the tank farms, the refineries, the refined product distribution systems and in some instances, the retail outlets.\footnote{7172(b)(1976). The transfer occurred without any changes in the statutory provisions relating to oil pipeline economic regulation.}

If an oil pipeline or the port is part of a vertically integrated structure, the port owners will want the port capacity to be that needed by their vertically integrated operation, rather than that desired by all users of the port. Thus, there is no incentive for vertically integrated oil company port owners either to make the port large enough for nonowners originally or to expand the port to meet the needs of nonowners.

With respect to rates for use of the port, vertical integration facilitates the spreading of profits and losses across the total structure. In general, this permits individual segments of the structure to operate at lower prices with cross subsidy from the other segments, to the detriment of non-integrated competitors of the lower-priced segment. In particular, if one segment is regulated, as many oil pipelines are and deepwater ports will be, the profits which could otherwise be realized in the regulated segment can be realized in other segments, resulting in effective circumvention of the regulatory rate constraints. Moreover, if any link of a vertically integrated structure is a monopoly, the monopoly characteristics are extended to a degree throughout the structure. The effect would be that non-integrated competitors would be forced either to pay the higher prices charged in the monopolized segment of the industry or to use less cost-effective alternatives to that segment, both to the detriment of the non-integrated competitors. Oil pipelines and deepwater ports would fall into this category if not regulated because they are a monopoly, as discussed below. Thus, vertically integrated oil companies are more able to manipulate the total system to maximize the advantages of port ownership and to maximize the extent to which port ownership can be leveraged to produce advantages in the total system.

This vertical integration of the oil industry has not escaped the attention of Congress, and bills have been introduced which would require various degrees of divestiture.\(^2\)

C. Monopoly

Oil pipelines generally are a natural monopoly.\(^2\) They are a natural monopoly because of their "geographically fixed facilities designed to serve customers in close proximity to such facilities and almost entirely useless for any other purpose."\(^3\) They are a natural monopoly because it is generally more efficient, due to the economies of scale, for one pipeline to be utilized between the same two points. In practice, of course, many other factors could result in multiple pipelines, such as a need for phased growth which makes it desirable to add other pipelines when needed, rather than to commence with an oversized pipeline or to replace the original pipeline with a larger pipeline, the need to be able to carry more than one substance simultaneously, or limitations in the size of readily available pipeline.\(^4\)

For the same physical reasons that an oil pipeline is a natural monopoly, a seaport is a natural monopoly. Thus, a deepwater port is a natural monopoly both in its role as an oil pipeline and in its role as a seaport.

In addition to the naturally monopolistic character inherent in oil pipelines and seaports, deepwater ports are also, in effect, a statutory monopoly because the Act precludes the construction of more than one port within an "application area."\(^5\) This prohibition provides a port investment in-


\(^2\) See, e.g., NAT. BUREAU ECON. RESEARCH, PRICE RESEARCH IN THE STEEL AND PETROLEUM INDUSTRIES (1939).

\(^3\) W.K. JONES, CASES AND MATERIALS ON REGULATED INDUSTRIES 51 (2d ed. 1976).

\(^4\) See L. COOKENBOC, supra note 7.

\(^5\) Sections 5(d)(1) and (2) of the Act provide:

(d)(1) At the time notice of an application is published pursuant to subsection (c) of this section, the Secretary shall publish a description in the Federal Register of an application area encompassing the deepwater port site proposed by such application and within which construction of the proposed deepwater port would eliminate at the time such application was submitted, the need for any other deepwater port within that application area.

(2) As used in this section, "application area" means any reasonable geographical area within which a deepwater port may be constructed and operated. Such application area shall not exceed a circular zone, and center of which is the principal point of loading and unloading at the high water mark of the nearest adjacent coastal State.


Upon receiving application for a deepwater port, the Secretary is required by § 5(d)(3) of the Act to publish notice of the application in the Federal Register (after having determined pursuant to § 5(c)(1) that the application contains all information required by § 5(c)(2)), and to publish therewith pursuant to § 5(d)(1) a description of the application area. Id. § 1504(d)(3). Within 60 days after such Federal Register publication, any applicant intending to submit an application for a deepwater port within the application area is required by § 5(d)(3) to submit notice of intent to file an applica-
centive by eliminating the possibility of a diminution in the value of the investment by a competing port.

The absence of competition in a monopoly leaves the monopoly holder free of the constraints which in a competitive market would help cause supply to be responsive to demand. In a competitive context, the supply-demand relationship helps to assure that the price of goods or services is a reflection of their real value to society and that the quantity of goods or services provided is the quantity desired by society. Due to the absence of the market constraints which result from the supply-demand relationship, possibilities for pricing and other market abuses are inherent in a monopoly.

There are both economic and legal constraints in relation to monopoly abuses. As an economic matter, the alternative means of importing oil would establish the limits beyond which additional monopoly abuses would provide no additional benefits to the monopolist because nonowner-shippers would turn to those alternatives. In decreasing order of present economic attractiveness, these alternatives are lightering, transshipment, and nonuse of VLCC's. However, because lightering is encountering increased environmental opposition, and many transshipment facilities are not available for public use, the only certain limiting alternative is nonuse of VLCC's. With nonuse of the VLCC's as the limiting alternative, it is apparent that monopoly abuses could eliminate almost entirely the economic advantages which deepwater ports can enjoy over existing methods of importing oil, for the nonowner-shipper.

As a legal matter, the license provides no antitrust immunity, and the issuance of a license is not admissible as a defense to any civil or criminal antitrust action. Thus, aside from the prospective standards which the Department can incorporate in the deepwater port license, as discussed below, monopoly abuses generally would be subject to the antitrust laws. The analysis of the manner in which the antitrust laws could be relied upon to remedy abuses by deepwater port licensees, if they should occur, is not presented here—such analysis would in itself be sufficiently complex to justify an entire article, and would be more meaningful if undertaken after operational experience had been acquired with the ports. For purposes of this article, it is necessary only to note that Sections 1 and 2 of the Sherman Act among other antitrust statutes such as Section 5 of the Federal Trade

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27. Section 1 of the Sherman Act, 15 U.S.C. § 1 (1976) provides, in pertinent part: "Every contract, combination in the form of trust or otherwise, or conspiracy, in restraint of trade or commerce among the several States, or with foreign nations, is declared to be illegal . . . ." This could be applied in relation to agreements between the port and third parties, and could conceiva-
Commission Act, would be applicable both in relation to the acts of the port itself and in relation to agreements between the port and third parties such as connecting downstream pipeline companies.

Natural monopolies and "statutory" monopolies result from situational and legal circumstances, respectively, which are beyond the control of the monopoly holder. To assure that such a monopoly holder does not unduly benefit therefrom, most natural transportation monopolies in this country are common carriers which are required to serve the public without discrimination and are regulated as to the rates they may charge for their natural monopoly service. Likewise, the natural monopoly advantages inherent in seaports normally inure to the public benefit ultimately, because they are public or quasi-public facilities which, by that fact, operate in the public interest.

D. Oligopoly

The concept of oligopolistic behavior in a given market relates in its most common usage to a situation in which that market is dominated by a few large competitors. Their status as competitors and their large size result in the likelihood of a commonality of interest. This commonality of interest, combined with the small number of participants which helps generally to facilitate similarity of action, can result in market behavior which resembles the behavior of one very large and dominant joint-venture competitor.

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29. The economic regulation of seaports is a matter of local concern. Thus, the public interest is defined by a local authority. See generally S. Rep. No. 1217, 93d Cong., 2d Sess. 23 reprinted in [1974] U.S. Code Cong. & Ad. News 7550.
30. C. KAYSER & D. TURNER, ANTITRUST POLICY 27 (1959)
The ownership structure and operation of a deepwater port will determine whether there is potential for oligopolistic abuse, stemming from the marine transportation of oil, which might be felt throughout the petroleum industry. As a general matter, greater similarity of the interests of each participant to the interests of the other participants and the interests of the whole results in greater potential for oligopolistic behavior. There is nothing inherent in a deepwater port which favors either the number, type, or size of participants from which oligopolistic abuses might be expected. With respect to the number of participants, the magnitude of the necessary capital commitment to the port favors a large number of owners; on the other hand, the desire of each owner not to see its large financial commitment directed against its wishes favors a small number of owners. With respect to the nature of participants, the ability of oil companies to ship their oil through a common carrier deepwater port without incurring any ownership risk would seem to discourage oil company ownership; on the other hand, the owner-shippers competitive advantage, in conjunction with the relative inability of any investor other than an oil company to provide or obtain adequate capital, favors oil company ownership.\textsuperscript{31} With respect to the size of the participants, the larger companies are more able to use the port to derive benefit over the entirety of a vertically integrated structure, and are financially probably more capable of acquiring an ownership interest; on the other hand, the smaller companies are less able than the larger companies to obtain or provide alternative means of transporting their oil.

Inasmuch as oil company owners of an oil pipeline are joint owners rather than competitors in that pipeline, a pipeline fits squarely within the classical oligopoly concept of a dominant joint venture. The oil company owners are often vertically integrated competitors in the oil industry at large, within which oil pipelines are obviously an important element. Therefore, in addition to the opportunities provided by this joint participation for competitors to share information they would not otherwise share and to act in accordance with their mutual interest, the potential for abuse lies in the joint participation by competitors in an important segment of the total industry, a type of joint participation that is not common in any unregulated portion of the American economy, and that generally occurs only with the oversight or prior approval of a regulatory agency in regulated enterprises.

Thus, the potential for oligopolistic abuse would be greatest in relation to oil pipelines, including deepwater ports, if the owners were large oil companies, few in number, of comparable nature in the oil industry at large, and in combination, a vertically integrated dominant portion of that industry. In

\textsuperscript{31} As noted above, few investors can command the 90% debt financing which oil companies can obtain with throughput and deficiency agreements as security. See note 15 and text accompanying notes 15 & 16 supra.
such a situation, each owner’s individual interest would be similar to the collective interest of the whole. The small number of owners would increase the likelihood of their pursuing similar courses of action in general by decreasing the likelihood of a diversity of interests. The large size and similar nature of owners would also increase the likelihood of a similarity of owner interest in the deepwater port because, for example, large oil companies have many similar needs in terms of market structure, corporate structure, financial structure, and equipment, to name a few, all of which may be different than those needs for medium or small oil companies. By the same token, vertically integrated oil companies would have many needs that are similar to the needs of other vertically integrated oil companies but dissimilar from the needs of companies that are not vertically integrated. The similarity of interests would narrow the scope of considerations which must be taken into account in relation to business decisions and would thereby decrease the likelihood that decisions of the port owners will affect positively the public interest. The combined vertically integrated dominance of the owners in the oil industry at large would increase their incentive and ability to manipulate the total system to increase the leverage which port ownership could provide over the total system. With diverse owners, on the other hand, the collective interest of the whole is an amalgamation of differing individual interests, such that the collective interest is less like the interest of any individual but more like the broader public interest.

In sum, the unique nature of oil pipelines as compared with other common carriers combines with the nature of the oil industry to result in a combination of potential abuses which is not susceptible to easy remedy. If any one of the problems were eliminated, the severity of the others would be mitigated. Some of the potential abuses would not be expected unless the port owners chose to operate the port in an anticompetitive manner, while other potential abuses are inherent in the nature of oil company ownership of deepwater ports irrespective of the manner in which the port owners choose to operate the port.

All of the potential problems are greatly exacerbated by the vertically integrated oil industry structure and the 1941 Consent Decree, discussed above, which effectively allows the port owners to establish rates that permit as much as 70% return on equity.
II. Treatment of Competitive Concerns by the Deepwater Port Act of 1974

The legislative history of the Act indicates that considerable attention was given to the possibility of competitive abuses from oil company owned deepwater ports.\(^{32}\) Indeed, this concern resulted in recommendations by the Senate Commerce Committee and the Justice Department that the Act prohibit port ownership by oil companies.\(^{33}\)

A. Ownership Priorities

These recommendations were not incorporated in the Act because of the countervailing concern that oil companies which use the port might be the only entities which would be willing and able to acquire or provide the estimated $600-900 million needed to construct a deepwater port.\(^{34}\) However, as a compromise between the desire for deepwater ports and the concern that oil company owners might abuse their ownership privilege, the Act permits oil company ownership only if no other prospective owners apply, and it imposes certain mandatory and discretionary safeguards.

To encourage deepwater port ownership by non-oil companies, the Act establishes a priority of ownership. If more than one eligible application is submitted for an "application area,"\(^{35}\) section 5(i)(2) of the Act provides:

(2) In the event more than one application is submitted for an application area, the Secretary, unless one of the proposed deepwater ports clearly best serves the national interest, shall issue a license according to the following order of priorities:

(A) to an adjacent coastal State (or combination of States), any political subdivision thereof, or agency or instrumentality, including a wholly owned corporation of any such government;

(B) to a person who is neither (i) engaged in producing, refining, or marketing oil, nor (ii) an affiliate of any person who is engaged in producing, refining, or marketing oil or an affiliate of any such affiliate;

(C) to any other person.\(^{36}\)

As forecast by many of the legislators involved in framing the Act, most of the serious initial interest shown in seeking a deepwater port license has


\(^{35}\) See note 25 supra.

been from companies desiring to ship their own oil. However, at the time of this writing, legislation had recently been introduced in Delaware which would permit it to apply for a deepwater port license, and as noted above, the State of Texas had begun to show serious interest in applying for a license to build a port similar to that which Seadock had applied to build.

B. COMMON CARRIER STATUS

Another provision in the Act which helps reduce the likelihood of abuses is section 8, which provides that the deepwater port and affiliated storage facilities are subject to regulation as a common carrier under the Interstate Commerce Act, and requires a deepwater port licensee to convey without discrimination all oil tendered to the port. This provision applies to all deepwater ports, but its benefit is most apparent in relation to ports owned by oil companies.

C. CONSULTATION WITH DOJ, FTC

Finally, the Act contains a provision which provides the licensing flexibility that the Secretary needs to respond to the wide variety of situations which could occur. The Secretary cannot issue, transfer, or renew any license without first obtaining the opinions of the Attorney General and the Federal Trade Commission as to whether the issuance, transfer, or renewal "would adversely affect competition, restrain trade, promote monopolization, or otherwise create a situation in contravention of the antitrust laws." In contrast to the ownership priority and common carrier provisions, this consultation requirement facilitates examination by the antitrust agencies of each license issuance, transfer, or renewal situation that is presented, and allows the Secretary to tailor safeguards to the needs of each situation.

The extent to which each of these provisions is necessary or desirable can only be determined from experience with the actual operation of the deepwater ports.

III. RECOMMENDATIONS BY THE DEPARTMENT OF JUSTICE AND THE FEDERAL TRADE COMMISSION

After the LOOP and Seadock deepwater port license applications were submitted, the Secretary requested the views of the Justice Department

39. See text accompanying note 5 supra.
and the Federal Trade Commission pursuant to Sections 4(c)(7) and 7 of the Act. The Justice Department and the Federal Trade Commission each submitted their report on these applications to the Secretary on November 5, 1976 ("DOJ Report" and "FTC Report," respectively). A brief summary of the views of both agencies is presented here.

As a general matter, because the Act does not prohibit oil company ownership of the ports and because no one else had then applied for a license, neither the DOJ Report nor the FTC Report recommends against issuance of the licenses to the oil company applicants. However, both Reports express concern that the vertically integrated oil company port owners will earn excessive profit. They also express concern about the incentive for such port owners to discriminate against nonowners, both as to the port itself and as to pipelines owned by the port owners which connect the port to inland common carrier distribution pipelines, and about the lack of incentive for such port owners to expand the port when demand exceeds capacity.

More particularly, the DOJ Report notes the following:

The major conclusion to be drawn from our antitrust analysis is that the integrated oil company owners of the proposed ports have attempted to maximize their profits through various overt and subtle requirements which will have the effect of restricting port throughput by limiting port capacity and access, thus enhancing the owners' profits in downstream product markets. Our economic analysis indicated that the port owners have the incentive to act in this manner, since port profitability is limited by rate regulation. We believe that the evidence demonstrates that the owners propose to operate the ports in a restrictive and anticompetitive manner, and that this will result in a misallocation of our nation's resources.

In order to address these concerns, the DOJ Report lists four competitive rules which are recommended for adoption by the Secretary as conditions in any deepwater port license issued to the oil company applicants. The four competitive rules are:

1. Deepwater ports must provide open and nondiscriminatory access to all shippers, owner and nonowner alike.
2. Any deepwater port owner or shipper providing adequate throughput guarantees at the standard tariff can unilaterally request and obtain expansion of capacity.
3. Deepwater ports must provide open ownership to all shippers at a price equivalent to replacement cost less economic depreciation.
4. The ownership shares of the deepwater ports' owners must be revised frequently (annually) so that each owner's share equals his share of aver-

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42. Id.
44. Id. app. B-7.
With these competitive rules as a core, the DOJ Report enumerates 18 specific implementing recommendations, along with five additional recommendations relating to the port financing, tariffs, and other matters.\textsuperscript{46}

The DOJ Report provides the following explanation concerning the competitive rules:

The competitive rules have the potential to eliminate most of these excess port and downstream profits. The rules achieve this result by prohibiting integrated oil companies from unreasonably or discriminatorily restricting access to and the capacity of the port, so that the owners will not be able to restrict use of the port. Rule 3, by permitting any non-owner to become an owner, serves as an expansion incentive by making the excessive port profits available to all shippers. Rule 4 completes the process of giving a shipper the ability to ship at the true economic cost of shipping. As an owner he will receive dividends to offset the excessive tariffs which are charged.

But rules 1, 3 and 4 alone are insufficient, since the owners old and new could restrict port capacity and achieve the same result—excess downstream profits—although they are now shared by all shippers. To forestall this type of restriction, first, an owner or a shipper must be able to force port expansion unilaterally, as long as that shipper is willing to guarantee the expansion by executing a throughput agreement and is willing to pay the going tariff for the expanded shipments.

It is likewise important to note that all four rules must be allowed to work together, for paradoxically, reliance on some of them and omission of the others may lead to a worse result than no rules at all. For example, if Rules 1, 3 and 4 were implemented and Rule 2 omitted, we would in effect be sanctioning a cartel with the power to veto the capacity decisions of each member firm in the industry.

The rules are designed to achieve the most competition possible short of nonintegration.\textsuperscript{47}

The FTC Report likewise enumerates several rules and recommendations which are intended, solely or in combination with other recommendations, to address competitive problems similar to those isolated in the DOJ Report.\textsuperscript{48} In broad terms, the recommendations in the Reports can be classified into three major categories: port design/ownership, port operation and rate tariffs.

A. PORT DESIGN AND OWNERSHIP

First, with respect to major port design and planning decisions, the primary concern relates to the lack of incentive for vertically integrated oil company port owners either to make the port large enough originally to

\textsuperscript{45} Id. app. B-10.
\textsuperscript{46} Id. app. B-14 to B-21.
\textsuperscript{47} Id. app. B-11 to B-12.
\textsuperscript{48} Id. at C-1 to C-2 (rules), C-2 to C-6 (recommendations)
allow capacity in excess of expected owner demand for expected non-owner demand, or to expand the port when total demand exceeds capacity, especially when the "excess" demand is nonowner demand. The theory is that as a general matter, in addition to the lack of incentive for oil company port owners to expand when an expansion would help their competitors at least as much as it would help them, vertically integrated oil companies have incentive only to make the port large enough to support their vertically integrated structure without regard to the needs of nonowners, because the port can provide a bottleneck which can restrict supply and thus support higher prices at the end of the vertically integrated structure.

The most direct remedy proposed by the Reports is a license requirement to permit nonowners to buy ownership shares in the port at a price based upon replacement cost less economic depreciation of the port facilities.49 This would create an incentive for the owners to consider the expansion requests of nonowners seriously because those nonowners would have the leverage of their right to become an owner if the existing port owners ignored their expansion requests. In broader terms, it would also help deter any anticompetitive abuses which enhance port profitability because the greater the profit from the port, the higher the incentive for outsiders to become owners. A second remedy is a requirement in the license that any shipper (owner or nonowner) which is willing to guarantee the throughput can unilaterally compel an expansion.50 To be effective, this remedy would require the license to provide the means by which the debt of the port could be increased to finance the necessary expansion. Finally, the backstop remedy which the FTC Report recommends, if all else fails, is that the Secretary retain in the license the authority to compel an expansion as he deems necessary.51

As part of the total capacity problem, the Reports also address the throughput demands of the owners in relation to each other. As long as dividends are in the same proportion as owner throughput, each owner receives the same percentage offset on its shipping rates. If ownership percentages remain fixed while owner throughput varies, any owner shipping more than its initial ownership percentage would receive a lower percentage offset. To assure that ownership percentages are periodically adjusted to equal owner throughput percentages, and to eliminate the disincentive to expansion caused by dividends which are proportionately less than throughput, the Reports propose a license requirement for periodic readjustment of share percentages.52

49. Id. app. B-18 to B-19 (DOJ), C-3 (FTC).
50. Id. app. B-18 (DOJ), C-3 (FTC).
51. Id. app. C-3.
52. The DOJ Report recommends annual readjustments, id. app. B-20; the FTC Report recommends "periodic" readjustments, without specifying the period, id. app. C-3.
B. PORT OPERATION

With respect to day-to-day physical operations of the port, the primary concern is the lack of incentives for the port owners to assure and facilitate access to the port by nonowners. The remedies proposed for this problem fall into two major categories. First, the Reports recommend license conditions either specifying or requiring prior approval by the Secretary of various port access conditions, for example, size of minimum tender, segregation capability, and other factors affecting the practical utility of the port to nonowners.53 Second, the Reports recommend that the license contain various provisions to assure that nonowner-shippers can transport their oil from the port to the inland oil distribution pipeline system.54 The intent is to avoid the frustration of protective measures at the port itself by more restrictive conditions in connecting downstream pipelines, especially as to downstream pipelines which are owned or controlled by owners of the port.

C. RATE TARIFFS

Both Reports express concern with respect to the day-to-day financial operations of the port. The ability of the port owners to charge rates which provide up to 70% return on equity could discourage use of the port by nonowners, and would in any event frustrate a basic purpose of the Act—to pass the transportation economies of deepwater ports to the consumer. The Reports recommend that the Secretary not allow tariff rates which provide more than the "true costs of capital" (DOJ Report)55 or "a reasonable rate of return on total investment in light of the risks involved and in light of the types of financial commitments made by the owners" (FTC Report).56

IV. COMPETITIVE SAFEGUARDS INCORPORATED IN THE LICENSES

Section 4(c) of the Act provides that the Secretary may issue a deepwater port license if, among other things, "he determines that the construction and operation of the deepwater port will be in the national interest and consistent with national security and other national policy goals and objectives, including energy sufficiency and environmental quality."57

Likewise, Section 4(e)(1) of the Act gives the Secretary the authority to impose conditions in the license in order to help assure that a deepwater port will be in the national interest:

54. Id. app. B-16 (DOJ), C-5 to C-6 (FTC).
55. Id. app. B-20.
56. Id. app. C-2.
In issuing a license for the ownership, construction, and operation of a deepwater port, the Secretary shall prescribe any conditions which he deems necessary to carry out the provisions of this [Act], or which are otherwise required by any Federal department or agency pursuant to the terms of this [Act].

On December 17, 1976, then Secretary of Transportation William T. Coleman, Jr. issued "The Secretary's Decision on the Deepwater Port License Application of LOOP, Inc." and "The Secretary's Decision on the Deepwater Port License Application of Seadock, Inc." These documents announced his decision to offer nearly identical licenses to the two applicants. Because LOOP has accepted its license, the LOOP Decision will be the reference document for this article.

A. Analytical Framework

In deciding which recommendations from the DOJ and FTC Reports to incorporate as conditions in the license, the Secretary was faced with a complex and unprecedented combination of factors, both with respect to the antitrust analysis itself and with respect to the role which that analysis should play in deciding whether and with what conditions to issue a license.

1. Antitrust Factors

The first step in the antitrust analysis is the selection of the appropriate analytical framework. A classical free market analysis of problems such as shipper-ownership and vertical integration cannot by itself yield realistic results in a regulated context because the economic regulation of the port results in various structural controls and constraints which destroy the validity of several fundamental assumptions of a free market analysis. On the other hand, a regulated industries antitrust analysis is not entirely appropriate because, although a deepwater port itself will be a regulated common carrier, the vertical integration of the oil company owners necessitates an analysis which goes beyond the port itself to the oil industry at large. As the analysis broadens to the oil industry at large, it is confronted with an industry which is regulated in some segments, narrowly "regulated" by price "controls" (ceilings) in other segments, and unregulated in still other segments. In addition, the vast diversity of end products which results from crude oil creates a flexible and dynamic industry the shape and mixture of which at any point in time is partly a reflection of the mixture of regulation, price controls, and nonregulation which forms the legal and economic environment in which the industry exists. Given this dynamic mixture of vertically linked regulated, semi-regulated, and unregulated segments of an

58. Id. § 1503(e)(1).
59. See, e.g., Decision, supra note 43. Appendix A of each decision is the license itself. In order to clarify certain ambiguities in the two licenses, they were modified slightly and reissued on January 17, 1977.
industry, the threshold task of determining the appropriate antitrust analytical framework is in itself a difficult matter as to which knowledgeable analysts vary widely.\textsuperscript{60}

An added complexity which must be factored into the analysis derives from the possibility that oil company owned and publicly owned ports may someday be operating contemporaneously. Although it is unlikely that there will ever be two or more geographically proximate "competing" ports, it is clear in the broader view of the oil industry at large that the extent to which a deepwater port could engage in anticompetitive activities would in a very real sense be limited by the existence, or even the possibility, of a publicly owned deepwater port somewhere else in the system. This potential for parallel operation of private and public "competing" facilities presents a situation which is rare to antitrust analysts. By the same token, as noted above,\textsuperscript{61} the extent to which transshipment and lightering will provide viable alternative methods of transportation depends upon legal and environmental constraints which may change drastically in the future.

Finally, perhaps the most fundamental problem presented in the antitrust analysis is that deepwater ports are an unknown entity in this country. Thus, in addition to all of the other uncertainties which are inherently presented to an analysis of this kind, such as the impact of Alaskan oil, the reliability of Middle East supply, the nation's future energy consumption patterns, and the rate regulation of oil pipelines, all anticompetitive safeguards imposed in deepwater port licenses must be based upon an educated guess as to what owner-shippers and nonowner-shippers, as well as possible public owners and investors generally, \textit{might} do in future years in relation to deepwater ports. Most of the competitive safeguards are preventive, rather than after-the-fact remedies. As with any prospective safeguard, and more so in relation to a situation such as the deepwater ports which has never existed before, these prospective safeguards must be very carefully constructed in order to provide complete coverage without overkill; they must retain the flexibility to respond to future situational changes; and they must avoid creating obstacles which merely redirect future behavior into less efficient mode without eliminating the abuses.

2. \textit{Transportation Factors}

Added to these difficulties of developing a reliable antitrust analysis and solutions is the problem ultimately placed by the Act upon the Secretary in determining the extent to which the antitrust problems should be


\textsuperscript{61} See introductory discussion at the beginning of this article supra.
incorporated in order to assure the development of a transportation project which is "in the national interest," as required by the Act.62

B. LICENSE SAFEGUARDS

Most of the safeguards recommended in the DOJ Report and the FTC Report were incorporated in the licenses. In determining which safeguards to apply, the Decision notes:

In general, the findings of the Attorney General and the FTC are consistent, and both agencies express similar concerns . . . . Although I do not agree with every statement made in the analysis of either the Attorney General or the FTC, I have found their conceptual framework and specific recommendations generally reasonable, sound and constructive. I have accepted and incorporated into the license almost all their recommendations for conditions.

Where I have not followed their specific advice, I have adopted an alternative course, explained below, that, in my judgment, will work more effectively. Where I have chosen an alternative, it has been primarily because another Federal agency has the statutory authority and operating responsibility, and the statute permits the regulatory agency to do exactly what the Attorney General and the FTC request. Thus, I am reluctant to assert my conditioning authority in a way that duplicates or conflicts with the proper exercise of another agency’s authority.63

The Decision continues by indicating the basic policy guidelines which were applied in deciding which anticompetitive safeguards to incorporate:

In my judgment (and the Attorney General apparently agrees), the proper construction and operation of a deepwater port offers certain environmental, economic and transportation benefits. We must ensure, therefore, that in furtherance of antitrust objectives, we do not defeat important transportation objectives by creating unnecessary impediments to construction of the port. Accordingly, I am applying the following policy guidelines in reconciling the antitrust recommendations with other important transportation objectives:

(a) Consistent with our stated policy, we will encourage the action of competitive forces to the maximum extent feasible.

(b) In the interest of rational delineation of Federal agency responsibility, we will avoid exercising jurisdiction that duplicates that of other agencies, instead seeking reform of ineffective agency practices through intervention in that agency’s proceedings and, if necessary, by proposing legislation to amend its statutory charter.

(c) We will exercise our authority in conditioning the license and regulating the port to the extent necessary to fill the gaps in the regulatory framework in order to prevent discrimination and anticompetitive practices in an effective manner.

(d) In constructing or advocating any regulatory scheme, we will follow the advice of the Supreme Court in American Trucking Association v. Atchi-

63. Decision, supra note 43, at 45.
son, T. S.F.R.R. "flexibility and adaptability of changing needs and patterns of transportation is an essential part of the office of a regulatory agency." We will attempt to avoid regulating "...the present and the future within the inflexible limits of yesterday," by devising a regulatory and enforcement mechanism, rather than fixing rigid conditions.

(e) We will seek to ensure that the applicant is both motivated and required to comply with the traditional obligations of a common carrier "clothed with public interest."64

Finally, the Decision reviews the four major areas of concern expressed in the DOJ and FTC Reports—discrimination to nonowners, capacity, rate regulation, and inland transportation—and indicates why the recommendations with respect to each area of concern were or were not accepted.

1. Use by Nonowners

The Decision expresses agreement that oil company owners of a deepwater port would have incentive to discourage the use of the port by nonowners by designing and operating the port in a fashion that favors owners. The Decision notes that despite this incentive, the shareholders of the port "must recognize that possession and control of the deepwater port brings with it certain obligations to furnish service to all shippers, even competitors of the shareholders."65 To help assure that the port design and operation do not discriminate against nonowners, the Decision establishes the following license conditions, consistent with the recommendations in the DOJ and FTC Reports:

In the license, we utilize the mechanism of review and approval of the Operations Manual to control the imposition of conditions of service by the licensee. DOT, and in particular, the Coast Guard, which will have primary responsibility for the Operations Manual, will consult and cooperate with the Department of Justice and the FTC on all matters of the Operations Manual which relate to conditions of service and limitations imposed on vessels calling and cargoes tendered.

The proration policy of the port, applicable when cargoes tendered exceed capacity, shall be included in the Operations Manual and similarly reviewed. We also will conduct public hearings, as suggested by the FTC, if after examination of any proposed limitations, the FTC deems such hearings necessary to explore the reasonableness of such limitations.

To provide guidance on the reasonableness of any conditions imposed by the licensee, and to be generally responsive to the particular recommendations of the Attorney General, we have included in the license specific requirements ensuring nondiscrimination in vessel handling, and acceptance of cargoes and storage segregations.

64. Id. at 46 (footnotes omitted).
65. Id. at 47.
We have made an explicit condition of the license a general prohibition against
discrimination, prohibiting either a licensee or owner from discriminating
against shippers or owners of oil in the facilities furnished, services rendered,
or rates charged, so as to make available the remedies of the Deepwater Port
Act for discriminatory behavior.\textsuperscript{66}

Prior approval requirements such as these create tremendous uncen-
tainty for potential owners because there have never been any deepwater
ports. By the time the Operations Manual is ready for approval, the port
owners will already have invested tens and perhaps hundreds of millions of
dollars into the port. At that point in time, when the Department of Trans-
portation can require that the Manual be modified in a certain fashion, the
owners have little bargaining leverage, short of political pressure beyond
the scope of the license process itself. On the other hand, if an offer of the
license itself had to await approval of the operating details which will be in
the Operating Manual, the cost of proceeding to the point where a license
could be offered would be so high, given the risk that an offer might not be
made, so as to discourage most or all potential investors. Thus, imposition
of these prior approval requirements reflects the decision to require those
approvals after, not before, the license is offered. As in many areas of
government regulation, this decision is the result of a situation in which ei-
ther the government must assume that private enterprise will act in the pub-
lic interest (in which case there would be no prior approval requirements), or
private enterprise must assume that the government officials will act respon-
sibly (in which case prior approval would be denied only upon good
cause)—and the government, with the "upper hand" (the licensing author-
ity), elects to proceed along the latter course because responsible govern-
ment is institutionally more likely in our society than publicly-minded private
enterprise.

2. \textit{Capacity}

The DOJ and FTC Reports indicate that the demand estimates
presented by the applicants are conservative, and that oil company port
owners have little incentive to expand, especially if the expansion is desired
only by nonowners.\textsuperscript{67} In response to these concerns, the Decision notes
that three steps will be taken. The first step is simply that the port must be
expanded at least as large as contemplated in the license application if
shippers willing to make throughput commitments so desire. The second
requirement is that "the Secretary can compel expansion of capacity an
additional 25\% in a situation where demand is evidenced by commitments
of shippers for throughput, and he finds that expansion is technically practi-
cal, economically reasonable, financially feasible and environmentally

\textsuperscript{66} Id. at 48 (references to license articles omitted).
\textsuperscript{67} Id. app. B-18 (DOJ), C-3 (FTC).
sound.  

In conjunction with such a mandated expansion, the Decision notes that:

In any action to compel expansion, the Secretary must observe the tenets of due process by affording opportunity for hearing, and will be bound by standards of reasonableness and consistency with regulatory principles. In view of the extra capacity which is possible in the design approach taken by LOOP, we do not foresee that this requirement will impose undue hardship.

Finally, the Decision notes that the DOJ and FTC recommendations which are intended to induce expansion will be adopted as license conditions. The Decision indicates that:

Proration policies will require review and approval of DOT, in like manner as the conditions of service. The FTC advises that effective proration policies can create incentives to expand (or at least reduce incentives to restrict the size of the Port).

Any shareholder or group must be able to authorize the corporation to expand the facilities. As LOOP explains, additional shareholder action is not now required for expansion to the limit of the application, but without this provision in the license, shareholders holding, in the aggregate, more than 25% of the shares could block expansion.

Preferential rights of shareholders to the shares of other owners, offered for sale, will be prohibited.

Shares must be made available at times of expansion, when new financing is required. The Attorney General has recommended that shares be available during the life of the project, on a continuous basis. We believe that such availability would diminish incentives for investment, in the early, higher risk stages of construction. Accordingly, we will require LOOP to hold ownership open until the closing of the initial financing, which will be for six months after the effective date of the license. We also will require that ownership be reopened upon subsequent financing for expansion. This will give outside shippers an opportunity to join in the benefits (and risks) of new facilities, but minimize the potential dilution of profits arising out of the original investment.

Shareholders must have the option to purchase additional shares to adjust ownership interests to conform to throughput percentages. The Attorney General recommends annual adjustments of ownership shares; the FTC does not specify a period (but prefers a short period) and LOOP has suggested five-year adjustments. We think that three-year intervals for adjustment of ownership shares, the interval selected by the LOOP shareholders for the initial share redistribution (after a two-year “start-up” period), should be the maximum interval, and we have so provided in [the license]. The concern of LOOP about the threat of future antitrust litigation on this point should be put to rest by the offer of a “Business Review Letter” by the Department of Justice.

68. Id. at 49.
69. Id. at 50 (footnotes omitted).
70. Id. at 50-51 (footnotes and references to license articles omitted).
As intended, these conditions have two advantages. They help reduce the incentive to owners to maintain their original throughput, as discussed above, and they help to provide the authority and incentive for anyone who desires to obtain an expansion of the port. One disadvantage is that, unlike most other oil pipelines, the original owners have no control over who the subsequent owners may be. Perhaps a more fundamental disadvantage is that the imposition of conditions on the sale of shares requires federal oversight in relation to the internal corporate documents of the licensee, which is generally unprecedented except as to federally chartered entities such as banks.

The extent to which these license conditions are necessary or desirable to achieve their intended purpose, and the effect of this detailed federal oversight, will be viewed with great interest by many. This type of federal "regulation" is a concept which may appear more frequently in years to come with respect to a variety of joint quasi-public projects that can benefit the nation but are too large to interest any significant number of non-federal public entities, or with respect to private projects that are too large for any private firm to undertake alone.

3. Rate Regulation

To keep the competitive advantage of the owner-shipper from being exacerbated by the potential 70% return on equity allowed by the Consent Decree, both the DOJ and FTC Reports recommend that the Secretary exercise indirect control over port tariff rates by making determinations as to the reasonableness of the port rate of return. In declining to accept this recommendation, the Decision notes:

Since this problem is common to oil-company owned deepwater ports and oil-company pipelines, the solution should also be common. Any remedy imposed by DOT to control deepwater port rates ignores the larger problem of pipeline rates. The correct approach is broader, including pipelines as well as deepwater ports. As I read the Interstate Commerce Act, the ICC [now FERC] now has the authority to handle the rate issue in the manner that the Attorney General suggests that I do by imposing conditions. Thus, DOT will urge, by participation in regulatory proceedings, that the [FERC] reassess the methods used to compute the proper rate of return, and to give full consideration to the fact of ownership by principal customers in determining the reasonableness of the return itself. The Attorney General, no doubt, will join in such proceed-

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71. See text accompanying note 52 supra.
72. For national banks, for example, see 12 U.S.C. §§ 21-42 (1976) (organization and other general matters); id. §§ 51-67 (capital, stock, and stockholders); and id. §§ 71-76 (directors).
73. See text accompanying notes 16-17 supra.
ings. If the [FERC] considers itself bound by statute or precedent, DOT will seek remedial legislation, and the Attorney General can join in such request. A solution developed for oil-company owned petroleum pipelines would also be applicable to the LOOP project.\textsuperscript{75}

The argument that the Department will not interfere with the establishment of rates because it is within the domain of the FERC could, of course, be applied with equal vigor to the conditions of service, over which the Department has retained authority in the license to exercise control. Although there is sound basis for exercise of control by the Department over certain matters of port design because the FERC has no statutory authority to do so, nothing in the Deepwater Port Act or in the Interstate Commerce Act would support including conditions of service within the Department's control while excluding ratemaking. Apparently, the basis for the distinction is that the conditions of service are essential to assure that the ports are operated in the manner contemplated by Congress in creating the Act, especially in assuring that nonowners have access to the port. Thus, waiting to see if the FERC will impose such conditions after experience has shown a need for them, rather than imposing them in advance in the license, could jeopardize the viability of the entire deepwater port concept. With respect to rates, on the other hand, there is no reason to believe that nonowners would not at least have access to the ports, as contemplated by Congress, even if the ports operated under the existing rate regulation formula. In this sense, it is apparent that the decision to retain authority in the license was based in some instances on the need for safeguards where the ICC has no authority under the Interstate Commerce Act, and was based in other instances on the need for safeguards where the ICC has the authority but simply has not acted. This dichotomy illustrates that two policy guidelines enumerated in the Decision can be inconsistent to a certain extent, because in attempting to "fill the gaps in the regulatory framework in order to prevent discrimination and anticompetitive practices," it is not always possible to "avoid exercising jurisdiction that duplicates that of other agencies."\textsuperscript{76}

4. Inland Transportation

In response to the concern noted in the DOJ and FTC Reports that the ability of nonowners to use the port would be meaningless unless they could be assured of receiving equally nondiscriminatory treatment in the connecting downstream pipelines, the Decision notes:

The Secretary has a special obligation to ensure that the oil imported through the deepwater port by a non-owner can be delivered to a common carrier pipeline for further transportation without discrimination. Consequently, DOT will exercise such regulatory responsibilities as are necessary to ensure that ship-
pers through the port have access to common carrier pipelines and that the policies applicable to the port are not frustrated downstream.77

This obligation will be fulfilled in the following manner:

The license . . . provides for review of joint arrangements by DOT, including proration policies, and [as] an additional incentive, we have included a requirement for storage until accepted by connecting carriers. [The license] also requires provision of facilities for delivery to connecting carriers, which are not now required by the Interstate Commerce Act, but are clearly part of the duties of a common carrier of this kind.78

The implementing provision in the license divides the connecting pipelines into three categories—existing pipelines owned or controlled by the port owners, new pipelines owned or controlled by the port owners, and pipelines not owned or controlled by the port owners—and specifies requirements which vary in accordance with the ability of the owners to implement them, which in turn varies with the degree of ownership of the port owners over such pipelines.79

77. Id. at 55.
78. Id. at 56 (references to license articles omitted).
79. Article 16 of the LOOP license provides:
The License shall establish with such common carrier pipelines as are owned or controlled by the Owners of the Licensee and their affiliates, or any of them, fair and adequate arrangements as may be reasonably required for the transportation of oil from the Port Complex to inland points served by such pipelines. Any requirements in such arrangements for minimum tender, shipment specification, or other conditions of shipment shall not be more restrictive than the conditions of shipment for the Port Complex, except such requirements that may be justified by pre-existing physical limitations of connecting facilities which cannot be readily corrected without substantial investment. The arrangements shall include a requirement that policies and practices concerning acceptance of cargoes when tenders exceed capacity shall be consistent with the policies and practices of the Port Complex. If any such common carrier pipeline fails or refuses to accept a shipment of any part thereof when properly tendered, the Licensee shall store such shipment or part without penalty until it shall have been accepted by such carrier.

Any pipeline constructed or extended after the date of issuance hereof, owned or controlled by the Owners or affiliates, or any of them, which will or reasonably could provide a connection between the Port Complex and any common carrier pipeline, shall (a) be owned by a single entity which shall operate such pipeline as a common carrier under the Interstate Commerce Act; (b) provide for terminal tankage on a common warehouse basis; and (c) participate in joint arrangements and conduct operations in a manner consistent with the provisions of the preceding paragraph.

The Licensee shall use its best efforts to establish similar arrangements with common carrier pipelines, not owned or controlled by Owners or affiliates, which will or reasonably could provide a connection with the Port Complex.

As used in this Article, the term "ownership" shall include, but not be limited to, ownership of any corporation owning pipeline facilities and any joint interest in pipeline facilities. The term "control" shall mean actual or legal control, contractual control, control by ownership of the majority of the voting stock in a corporation owning pipeline facilities or ownership of the majority of joint interests in pipeline facilities. The term "affiliate" shall include any corporation or business entity, controlled by, controlling, or under common control with the Licensee or any Owner.

Id. app. A-10 to A-11.
Thus, the Decision notes that although the Interstate Commerce Act and the antitrust laws are the most suitable vehicles by which the basic abuses of shipper-ownership are to be cured, the Department will exercise oversight in relation to joint arrangements between the port and connecting downstream pipelines. The unavoidable difficulty in this approach, of course, is the impossibility of specifying in advance the connecting downstream pipelines to which this oversight could or should apply. In theory, this could extend the Department's reach to a large portion of the nation's total oil pipeline system. In practice, the Department's reach via this provision would probably remain within the immediate geographical area of the port, given the strong suggestions in the Decision of a desire to avoid the use of a deepwater port license to involve the Department in oil pipeline economic regulation generally.80

One recommendation not accepted in the Decision is that each shareholder, rather than only the licensee, be liable to fulfill the joint tariff conditions of the license.81 The license does impose individual shareholder liability for certain matters,82 and the rationale for rejecting the recommendation in relation to joint tariffs is not clear. On one hand, direct shareholder liability for nondiscriminatory license conditions such as nondiscriminatory joint tariffs may not be effective because each shareholder could plead that it did not individually have complete control over the port's end of a joint tariff. On the other hand, the absence of direct shareholder liability may eliminate the Department's ability to oversee joint tariffs because the port as an entity had no control over the other end of a joint tariff. Thus, both shareholder and licensee responsibility for joint tariffs would be necessary for effective enforcement.

C. PORT OWNERSHIP BY NON-SHIPPERS

As noted above,83 the Act establishes a priority of ownership for deepwater ports—first to adjacent coastal states, second to entities other than oil companies, and finally, to oil companies. Nonetheless, the Decision mentions only the possibility of port ownership partially or entirely by oil companies shipping their own oil. The Decision is probably silent about the ownership by non-shippers because no non-shippers joined in the license applications.84 However, it is possible that the port could in time become an attractive investment to one of the relatively few independent oil pipeline companies or to other types of public and private investors. As a general matter, the presence of other investors would help to reduce the

80. Id. at 55.
81. See note 79 supra.
82. See Decision, supra note 43, app. A-7 to A-8 (Article II: Nondiscrimination).
83. See text accompanying note 36 supra.
84. See Decision, supra note 43, at 3.
possibility of anticompetitive behavior because a vertically integrated owner may have different motives for a port than an investor whose sole purpose is to reap the best return on the port investment itself. Without delving into the theoretical possibilities which may flow from partial or entire ownership by non-shippers, it is noted at this point that such ownership of the ports could fundamentally affect the basic assumptions underlying this analysis.

V. Conclusion

In the process of analyzing the two deepwater port applications submitted by the oil companies, the Department of Justice and the Federal Trade Commission have made clear their considerable suspicion as to the motives of the oil company applicants. Those agencies are, of course, acutely aware of the difficulty of relying solely upon the antitrust laws to remedy problems after they have developed; thus, they recommended the implementation of an ounce of prevention at the outset as being considerably more desirable than a pound of cure.

The Secretary of Transportation, on the other hand, while acknowledging the concerns of the antitrust experts, added the countervailing concern that an overabundance of prospective safeguards in relation to perceived potential abuses which have not yet ripened and may never ripen could discourage potential owners from constructing a port. Thus, the Secretary, who is required by the Act to have a broader view of the problem than merely attempting to curtail anticompetitive practices within the oil industry, noted that some of the preventive measures proposed by the DOJ and FTC Reports were aimed at problems which are far broader in scope than just the deepwater ports. To that end, the Secretary refused to jeopardize the deepwater ports by allowing them to be used by the antitrust agencies to cure a much broader problem, the responsibility for which rests with another agency. Moreover, there are inherent social and economic inefficiencies in attempting to solve broader problems with remedies which are aimed in a piecemeal or patchwork fashion at individual narrow aspects of the broader problems.

Most of the prospective safeguards recommended in the DOJ and FTC Reports were incorporated into the licenses. Only time will tell whether those safeguards will reduce the potential for harm, or merely shift an undiminished burden from enforcement after-the-fact to policing during-the-fact.

Many elements in the equation are as yet uncertain—oil demand, oil supply, oil pipeline rate regulations, and the number of deepwater ports, to name a few—and it remains to be seen how these elements will affect the ultimate outcome. As the situation progresses, the deepwater ports will be viewed with avid interest by many—the Department itself, the antitrust agencies, several other government agencies, the oil industry, antitrust law-
yers everywhere, and the American consumer who, if all goes well, will be the ultimate beneficiary of the ports.
Recent Developments in the Transportation of Hazardous Materials

RUSSELL S. FRYE*

I. INTRODUCTION

Since the fall of 1976 there has been a rapidly growing interest in the protection of workers, the public, and the environment from the dangers of hazardous materials.¹ Alarmed by accidents involving tank cars filled with toxic gases, incidents of massive environmental contamination by pollutants such as mercury and kepone, and the discovery of carcinogenic substances in workplaces and public water supplies, environmental, labor, and consumer protection groups have strengthened their demands for federal regulatory activity. President Carter, in his Environmental Message to Congress in May, 1977, stressed the high priority his Administration places on the control of hazardous chemicals.²

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1. Although the Clean Air Act, 42 U.S.C. §§ 7601-7626 (1976), the Federal Water Pollution Control Act, 33 U.S.C. §§ 1251-1376 (1976) and the Safe Drinking Water Act, 21 U.S.C. § 349, 42 U.S.C. §§ 201, 300f to 300j-9 (1976), all had provisions dealing with hazardous or toxic pollutants, and regulations under the Occupational Safety and Health Act, 29 U.S.C. §§ 651-678 (1976), providing for protection of employees from certain hazardous substances have been in existence for several years, real concern over hazardous substances, particularly those with subtle or chronic health effects, has been steadily increasing in recent years.

Not surprisingly, this concern has resulted in federal legislative and regulatory activity, including new federal regulations concerning hazardous materials which will have a significant impact on the transportation industry. Prior to these recent developments, federal control over the transportation of hazardous materials was vested exclusively in the Secretary of Transportation under the Hazardous Materials Transportation Act (HMTA). In 1976, through the enactment of the Resource Conservation and Recovery Act of 1976 and the Toxic Substances Control Act, the Environmental Protection Agency was given new regulatory authority concerning hazardous wastes and toxic chemical substances and mixtures, to which carriers of these substances will frequently be subject. Regulations under the authority of these two statutes will first be promulgated in 1978. EPA has already promulgated regulations prohibiting spills of hazardous substances under the Federal Water Pollution Control Act. Meanwhile, the Occupational Safety and Health Administration is developing regulations under the authority of the Occupational Safety and Health Act of 1970 dealing with three areas: employee exposure to carcinogens; labeling and data availability for hazardous substances; and training and health monitoring for employees who handle hazardous substances. The applicability of these impending regulations to the transportation industry, the interaction of these statutes with each other and with other federal and state legislation, and the potential effects of these new developments on the transportation industry will be examined.

II. HAZARDOUS WASTE TRANSPORTATION

The Resource Conservation and Recovery Act of 1976 is the environmental legislation most clearly applicable to the transportation industry. Congress had previously addressed the problem of solid waste management in the Solid Waste Disposal Act of 1965 and the Resource Recovery Act of 1970. The earlier laws provided federal assistance to state and local governments for the planning and development of resource recovery and solid waste disposal programs and authorized the promulgation of

3. 49 U.S.C. §§ 1471, 1655, 1761-1762, 1801, 1812 (1976). The Secretary is directed to "protect the Nation adequately against the risks to life and property which are inherent in the transportation of hazardous materials in commerce." Id. § 1801. The Materials Transportation Bureau within the Department of Transportation (DOT) is responsible for the enforcement of a large number of regulations governing container manufacturers, shippers, and carriers of materials determined by DOT to be hazardous when transported in interstate commerce. 49 C.F.R. ch. 1 (1976).
waste management guidelines. Under this federal encouragement, all of the states had issued some kind of solid waste disposal regulations by 1975.\textsuperscript{9} These state programs did little, however, to curb the growing dangers to health and the environment from hazardous wastes.\textsuperscript{10} This was one of the major concerns behind the enactment of the Resource Conservation and Recovery Act of 1976.

\section*{A. Statutory Provisions}

The Act addresses three areas of solid waste problems: municipal waste disposal, including open dumping; government procurement of recovered materials; and hazardous wastes. Subtitle C of the Act, "Hazardous Waste Management,"\textsuperscript{11} provides the EPA with direct regulatory authority over transporters of hazardous waste.\textsuperscript{12} A hazardous waste is defined in the Act as any solid waste,\textsuperscript{13} or combination of solid wastes, which may:

\begin{itemize}
  \item[(A)] cause, or significantly contribute to an increase in mortality or an increase in serious irreversible, or incapacitating reversible, illness; or
  \item[(B)] pose a substantial present or potential hazard to human health or the environment when improperly treated, stored, transported, or disposed of, or otherwise managed.\textsuperscript{14}
\end{itemize}

Many types of wastes which are frequently transported in large quantities could fall within this definition.\textsuperscript{15} The EPA Administrator is directed to

\textsuperscript{9} Savas, Evaluating the Organization of Service Delivery: Solid Waste Collection and Disposal, ch. 14 at 33 (1975).


\textsuperscript{12} A different provision of the Act may eventually have a greater, though less direct, impact on the transportation industry. Section 8002(j), 42 U.S.C. § 6982(j) (1976), established a Resource Conservation Committee directed to study and report to Congress and the President on, \textit{inter alia}, "the effect of existing public policies . . . upon resource conservation, and the likely effect of the modification or elimination of such incentives and disincentives upon resource conservation." One of the subjects being considered by the committee is the effect of freight rates and regulations on resource conservation. \textit{Cf.} Ex Parte No. 319, Investigation of Freight Rates for the Transportation of Recyclable or Recycled Commodities (ICC investigation into the rate structure for rail transportation of recycled materials). For a detailed examination of the legislative history and the various provisions of the Act, \textit{see} Kovacs & Kluczynski, The New Federal Role in Solid Waste Management: The Resource Conservation and Recovery Act of 1976, 3 Colum. J. Envl. L. 205-61 (1977).

\textsuperscript{13} "Solid waste" here need not necessarily be in solid form; any solid, liquid, semisolid, or contained gaseous wastes which are not regulated under the Federal Water Pollution Control Act or the Atomic Energy Act of 1954, 42 U.S.C. §§ 2011-2254 (1976), are within the definition of "solid waste" provided in § 1004(27) of the Act, 42 U.S.C. § 6903(27).


\textsuperscript{15} A 1976 report by the House Interstate and Foreign Commerce Committee estimated that 30-35 million tons of hazardous wastes are placed in open dumps each year. H.R. Rep. No. 1491, supra note 10, at 11.
promulgate regulations identifying characteristics of hazardous wastes and listing particular hazardous wastes subject to the provisions of the Act. Following identification of hazardous wastes, EPA must promulgate standards for those persons who generate, transport, store, treat, or dispose of such wastes.

EPA can set strict performance standards and will have to issue permits for approved hazardous waste treatment and disposal facilities, but its regulatory authority over generators and transporters of hazardous wastes is much more limited. The primary goal of the provisions of the Act dealing with generators and transporters is the institution of a "cradle to grave" recordkeeping system which allows EPA to monitor all hazardous wastes from creation to final disposal, thereby ensuring that all of these wastes eventually reach authorized disposal facilities. Although there is no authority in the Act to directly regulate the generation of wastes, generators will be required to keep transportation records showing the carrier to whom the wastes were given and the intended destination of the wastes. The generator will also be responsible for the use of appropriate containers and for labeling in accordance with EPA standards.

Section 3003 of the Act requires the EPA Administrator to establish such standards applicable to transporters of hazardous wastes identified or listed by EPA as may be necessary to protect human health and the environment. These standards shall include requirements for:

1. recordkeeping concerning such hazardous waste transported, and their [sic] source and delivery points;
2. transportation of such waste only if properly labeled;
3. compliance with the manifest system . . . ; and
4. transportation of all such hazardous waste only to the hazardous waste treatment, storage, or disposal facilities which the shipper designates on the manifest form . . .

For any hazardous waste which is subject to the Hazardous Materials Transportation Act, the regulations promulgated by EPA for hazardous waste transporters must be consistent with DOT regulations under the HMTA. Violation of any standard promulgated under the Act could result in imposition of a civil penalty of not more that $25,000 per day of noncom-

22. Section 3003(b), 42 U.S.C. § 6923(b) (1976). Since regulations requiring compliance with the manifest system, for example, were obviously intended to be different from DOT regulations requiring a shipper's certification before acceptance of a shipment of hazardous materials, 49 C.F.R. § 177.817 (1976), it seems that EPA requirements can be different from and additional to DOT regulations without being "inconsistent" within the meaning of this section.
Any person who knowingly transports hazardous waste to a facility which does not have an EPA permit or makes a false statement in any manifest, record, or report is subject to a criminal penalty of a fine of not more than $25,000 for each day of violation or imprisonment for not more than one year.\textsuperscript{24}

Two other provisions of the Resource Conservation and Recovery Act could affect transporters of hazardous waste. First, regardless of any other provisions of the Act or regulations promulgated thereunder, the Administrator, whenever he finds that the handling, storage, treatment, transportation, or disposal of any solid waste or hazardous waste "is presenting an imminent and substantial endangerment to health or the environment," may bring suit in federal district court to restrain such handling or to take such other action as may be necessary.\textsuperscript{25} Second, § 3006 of the Act\textsuperscript{26} provides for EPA authorization of state hazardous waste programs which meet certain criteria. After EPA authorization, enforcement of hazardous waste regulations would be handled by the state agency. While such state programs are being developed, the EPA Administrator may grant two-year interim authorization to states which have existing hazardous waste programs.\textsuperscript{27} Because no more than $25 million was authorized for grants to assist states in development and implementation of authorized state hazardous waste programs,\textsuperscript{28} it is unlikely that most states will wish to take on the responsibilities of administering hazardous waste programs under the Act without further incentives.

\textbf{B. Proposed Regulations}

Although regulations for waste generators and transporters were statutorily required to be promulgated by April 1, 1978, EPA did not publish proposed regulations for transporters until April 28, 1978,\textsuperscript{29} with comments on these proposed regulations to be submitted by early fall and final regulations expected sometime in late 1978.\textsuperscript{30} Proposed Subpart C of 40 C.F.R. Part 250 sets out the requirements for recordkeeping, compliance

\begin{footnotesize}
\begin{enumerate}
\item Section 3008(a), 42 U.S.C. § 6928(a) (1976). Note that this is considerably more than the $10,000 civil penalty provided in the HMTA, 49 U.S.C. § 1809 (1976).
\item Section 3008(d), 42 U.S.C. § 6928(d) (1976).
\item Section 7003, 42 U.S.C. § 6973 (1976).
\item Section 3006(c), 42 U.S.C. § 6926(c) (1976).
\item Section 3011(a), 42 U.S.C. § 6931(a) (1976).
\item 43 Fed. Reg. 18,506 (1978). Four environmental groups have notified EPA, pursuant to § 7002 (c) of the Act, of their intention to commence legal actions against the agency for failing to promulgate certain regulations within the statutory deadlines. 43 Fed. Reg. 36, 323 (1978).
\item The comment period will not close until 60 days after all regulations under §§ 3001-3005 (42 U.S.C. §§ 6921-6925) have been proposed, which is expected to be late in the summer of 1978. Final regulations will be effective six months after publication.
\end{enumerate}
\end{footnotesize}
with the manifest system, loading, storage, delivery, emergency procedures, and marking and placarding of vehicles for transporters of hazardous wastes, as identified or listed by EPA.\textsuperscript{31} To comply with the above-mentioned requirement that hazardous waste transportation regulations must be "consistent with" DOT regulations under the HMTA,\textsuperscript{32} the proposed regulations do not set up separate standards for containers and procedures used in the transportation of hazardous wastes, but rather incorporate the DOT regulations by a general requirement that any hazardous waste which meets the DOT criteria for a hazardous material must be handled in accordance with the provisions of the DOT hazardous materials regulations in addition to EPA regulations.\textsuperscript{33} At the same time, DOT is revising its regulations under the HMTA to include on the Hazardous Materials Table\textsuperscript{34} all listed hazardous materials when transported as wastes and all materials subject to EPA hazardous waste regulations, to address the problem of mixtures of several types of wastes, and to make several other revisions to ensure consistency with EPA hazardous waste regulations and to adequately protect the public from the dangers of the transportation of hazardous wastes.\textsuperscript{35} Publication of final DOT regulations is planned to coincide with that of final EPA regulations for hazardous waste transporters in late 1978.

\textsuperscript{31} There is some question whether a waste which meets EPA criteria for a hazardous waste, e.g., flammability, but has not been specifically listed by the Administrator as a hazardous waste is subject to hazardous waste regulations promulgated under the Act. In a cover letter circulated with draft proposed regulations on identifying hazardous wastes, EPA indicated a belief that wastes need not be specifically listed to be subject to regulation: "Several options for lists include waste types, process types, industry categories, substances, or a combination. In addition, whether the list is an example of wastes that are potentially dangerous, a definitive enforceable list of those defined to be hazardous, or some other approach is still under discussion." Although §§ 3002-3004 of the Act (42 U.S.C. §§ 6922-6924 (1976), refer to "hazardous wastes identified or listed under this subtitle," the House Committee Report, H.R. REP. No. 1491 supra note 10, at 25, stated: "the criteria for determining what should be considered hazardous should not be confused with an actual hazardous waste. . . . Only after the criteria for determining what is hazardous has [sic] been developed can the Administrator determine which specific wastes are hazardous."

\textsuperscript{32} See note 22 supra.

\textsuperscript{33} Proposed 40 C.F.R. § 250.30(c), 43 Fed. Reg. 18,510 (1978). DOT regulations incorporated into EPA hazardous waste regulations would, however, be applicable to both interstate and intrastate transportation of hazardous waste. See also note 35 infra.

\textsuperscript{34} 49 C.F.R. § 172.101 (1976).

\textsuperscript{35} 43 Fed. Reg. 22,626 (1978). In a largely unanticipated development, DOT has suggested that the fact that the Resource Conservation and Recovery Act applied to both interstate and intrastate transportation of hazardous wastes amounts to a congressional finding that intrastate transportation of hazardous wastes affects interstate commerce, so DOT proposed regulations would be applicable to both interstate and intrastate transportation of hazardous wastes by all modes. Id. at 22,626-27. EPA is also considering recommending that DOT develop a new placard for wastes which are toxic, bioaccumulative, carcinogenic, or mutagenic. 43 Fed. Reg. 18,507-09 (1978).
An analysis of the statement on applicability in the proposed regulations gives rise to several questions. The statement indicates that the regulations "do not apply to persons . . . that transport hazardous waste(s) on the site of a hazardous waste generator or a permitted hazardous waste management facility."36 Although § 3002 of the Act37 does not require the use of the manifest system for transportation of hazardous wastes on the premises of the waste generator, there is no definition of "transport" or "transporter of hazardous waste" and no other provision in the Act which would limit the application of hazardous waste transportation standards to off-site transportation. Thus this limitation in EPA and DOT regulations may be subject to challenge by environmentalists.

A question of greater significance to the transportation industry is whether the carrier is obligated to determine the hazardous nature of any waste he accepts for transport. Will the carrier be subject to the standards established by these proposed regulations whenever he transports a waste which has been identified or listed as hazardous by EPA, or only when the waste generator has identified the waste as hazardous through compliance with labeling or manifest requirements? The plain language of § 3003 of the Act38 makes hazardous waste transportation standards "applicable to transporters of hazardous waste identified or listed under this subtitle . . ." and gives no indication that notification of the hazardous nature of the waste by the generator is required. However, the Report of the House Committee on Interstate and Foreign Commerce stated that, under the Act, the waste generator "will bear the burden of . . . providing information and warning to the transporter of the waste," while "the duties of the transporter are to accept only those hazardous wastes properly labeled and in compliance with the manifest system. . . ."39 The ambiguity of these and similar provisions40 makes it uncertain to what extent transporters of hazardous waste may be held liable for transportation of a waste material

38. Id. § 6923.
39. H.R. Rep. No. 1491 supra note 10, at 26-27. A similar conflict may be found in the proposed regulations for hazardous waste transporters. Although the preamble to the proposed regulations states that preparation of the manifest, labeling, and packaging for hazardous wastes is the responsibility of the waste generator (43 Fed. Reg. 18,508 (1978)), several sections of the proposed regulations seem to indicate that transporters are required to comply with these proposed standards regardless of whether a hazardous waste has been so designated by the generator. For example, § 205.34(a) provides that: "A transporter shall not accept from a generator a shipment of hazardous waste without a manifest . . . signed by the generator . . . and § 205.34(b) forbids the transporter to "transport a shipment of hazardous waste in containers not properly labeled or marked in accordance with the provisions of § 250.26." See also preamble to proposed DOT regulations, 43 Fed. Reg. 22,626-28 (1978).
40. See note 39 supra.
which qualifies as a hazardous waste under criteria promulgated by EPA, but which was not so identified by the waste generator prior to shipment.

The manifest system is the cornerstone of the EPA program for the management of hazardous waste. Under the proposed regulations, the transporter may not accept a shipment of hazardous waste without a manifest issued by the generator indicating the nature of the waste and designating a permitted hazardous waste storage, treatment, or disposal facility to which the waste is to be delivered. The transporter will be required to sign the manifest acknowledging acceptance of the hazardous waste, have a copy of the manifest with the shipment at all times, deliver the manifest to the designated facility, and keep a copy of the manifest for at least three years from the date of certification of delivery to the permitted hazardous waste management facility.41 The transporter must deliver the entire quantity of hazardous waste or wastes accepted from the generator to the permitted hazardous waste management facility which has been designated on the manifest. Through the use of this system, EPA can ensure that all hazardous wastes are handled by facilities which have obtained an EPA permit and could trace the origin or the final disposition of any hazardous waste at a later date.

The proposed EPA regulations are considerably more stringent than existing DOT regulations with regard to emergency incidents involving hazardous waste. Proposed § 250.37(b) requires notification of the United States Coast Guard National Response Center and submission of written reports to EPA and DOT "in the event of any spill of hazardous waste during transportation," regardless of whether such an event presents a hazard to health or the environment. In contrast, DOT hazardous materials transportation regulations permit repair or temporary storage of a leaking package or container when safe and practicable.42 It is questionable whether it is necessary for the EPA proposed regulation to be so strict in order to protect public health and the environment.

Within 90 days after promulgation of regulations identifying or listing any substance as a hazardous waste, any person transporting such substance is required to file with the EPA Administrator a notification stating the location and description of such activity and the identified or listed hazardous waste handled by such person.43 Under proposed regulations, hazardous waste transporters would be required to submit a notification for each terminal the transporter owns and utilizes for vehicles transporting hazardous wastes. The transporter would also have to identify the types of hazard-

43. Section 3010(a), 42 U.S.C. § 6930(a) (1976).
ous waste handled and estimate the annual amount of such waste handled based on 1977 volume. Neither the Act nor the proposed regulations are clear about whether a new or additional notification will be required whenever a transporter begins handling a new type of hazardous waste; however, this interpretation, which could be burdensome for many carriers, could be implied from the statement in § 3010(a) of the Act that: "No identified or listed hazardous waste subject to this subtitle may be transported, treated, stored or disposed of unless notification has been given as required under this subsection."  

C. Potential Impacts

Since transporters of hazardous materials are already required to comply with DOT standards for packaging, labeling, and handling of hazardous materials as well as requirements for obtaining shipper’s certification on shipping papers for hazardous materials, EPA regulations for hazardous waste transporters are unlikely to impose many new affirmative obligations on such carriers. However, many waste materials, which have not until this time been treated as hazardous materials requiring compliance with DOT standards, will now be subject to such requirements after identification and listing of hazardous wastes is completed by EPA and after DOT regulations for hazardous materials transportation are amended to conform with hazardous waste regulations. On the other hand, requirements of the Resource Conservation and Recovery Act that hazardous waste treatment, storage, and disposal facilities must obtain EPA approval and meet certain performance standards will mean that, in the future, there will be considerably fewer facilities in the United States capable of receiving hazardous waste. Therefore, the need for transportation of hazardous wastes over longer distances will increase. Increased awareness of the environmental effects of solid waste disposal facilities will create greater public demand for transportation of solid wastes.

45. Section 3010(a), 42 U.S.C. § 6930(a) (1976). The preamble to the draft proposed notification regulations contributes to this ambiguity: "Revised Section 3001 [hazardous waste identification] regulations will become effective in 180 days after promulgation and all persons who generate, transport, treat, store, or dispose of such hazardous wastes will be required to notify EPA . . . . No additional notification is required from those persons unaffected by the Section 3001 regulations revisions."
46. The provision of proposed DOT revisions of hazardous materials regulations which may be most troublesome for waste transporters is proposed 49 C.F.R. § 173.510(5), 43 Fed. Reg. 22,626 and 22,633 (1978), which would prohibit the use of open-top or tarp-covered vehicles for bulk shipments of hazardous wastes or any other hazardous materials.
47. For example, an EPA study suggests that, in order to protect groundwater supplies, land disposal of solid waste "is not environmentally feasible in many areas," so that alternatives such as waste transport to a more suitable area should be investigated. ENVIRONMENTAL PROTECTION AGENCY,
III. EMPLOYEE EXPOSURE TO HAZARDOUS MATERIALS

The Occupational Safety and Health Act of 1970\(^ {48} \) had as its primary purpose the reduction of safety hazards and assurance, so far as possible, of safe and healthful working conditions for every working man and woman. The Act set up the Occupational Safety and Health Administration (OSHA) to carry out the purposes of the Act. One of the means prescribed by Congress to provide employees with a safe and non-hazardous environment is the authority vested in the Secretary of Labor to set mandatory safety and health standards.\(^ {49} \) Special attention was given in the Act to the dangers of occupational exposure to hazardous or toxic materials:

The Secretary, in promulgating standards dealing with toxic materials or harmful physical agents under this subsection, shall set the standard which most adequately assures, to the extent feasible, on the basis of the best available evidence, that no employee will suffer material impairment of health or functional capacity even if such employee has regular exposure to the hazard dealt with by such standard for the period of his working life. . . . In addition to the attainment of the highest degree of health and safety protection for the employee, other considerations shall be the latest available scientific data in the field, the feasibility of the standards, and experience gained under this and other health and safety laws.\(^ {50} \)

Most OSHA standards are uniform for all employers to which the Act is applicable, rather than varying for different industries. For this reason, an OSHA standard which establishes requirements for conduct or exposure levels sufficiently stringent to meet the criteria set forth above will frequently be considerably more stringent than such a standard would be if established only for the transportation industry, where exposures to hazardous materials are likely to be brief and widely intermittent.

Almost all employers are familiar to some extent with OSHA. Health and safety standards covering a wide range of workplace conditions and exposure levels have been in existence for several years; protective equipment, employee health monitoring, workplace environment monitoring, and warning signs and labels are currently required for at least eighteen substances, while employee exposure limits have been established for numerous other substances.\(^ {51} \) Spurred on by the current Administration's commitment to the control of toxic substances in the workplace and by increasing pressure from labor and environmental groups, OHSA has re-

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49. Id § 655(b). The term "occupational safety and health standard" is defined as: "A standard which requires conditions, or the adoption or use of one or more practices, means, methods, operations or processes, reasonably necessary or appropriate to provide safe or healthful employment and places of employment."
50. Id § 655(b)(5).
cently launched a series of rulemaking proceedings which will greatly increase OSHA’s involvement in assuring employee protection from the dangers of hazardous and toxic materials. Such proceedings are underway for establishing occupational exposure levels for suspected carcinogens, and for establishing standards relating to various hazardous or toxic chemicals in the areas of labeling, data availability to employees, and employee training. The first carcinogen occupational standards, for benzene and inorganic arsenic, have been promulgated. OSHA estimates the first-year costs for compliance with the benzene exposure standard will be in excess of $2 million for the transportation industry alone.

A. Applicability to the Transportation Industry

In considering the impact of these OSHA regulatory developments upon the transportation industry, the threshold question is whether OSHA health and safety standards can be applied to the transportation industry, which is already regulated by the Department of Transportation. Section 4(b)(1) of the Act provides: “Nothing in this [Act] shall apply to working conditions of employees with respect to which other Federal agencies exercise statutory authority to prescribe or enforce standards or regulations affecting occupational safety or health.” It is now well-settled that this provision of the Act does not provide an industry-wide exemption from the Act for the transportation industry. “It is clear that the exemption applies only when another Federal agency has actually exercised its statutory authority. It does not apply where such an agency has regulatory authority but has failed to exercise it.” Whether another regulatory agency’s

53. 43 Fed. Reg. 5918 (1978). Note that liquid mixtures containing 0.5% or less benzene have been exempted from the standard for three years, and liquid mixtures containing 5% or less benzene which are already packaged have been exempted from labeling requirements of the standard. 43 Fed. Reg. 27,962 (1978).
54. The Court of Appeals for the Fifth Circuit issued an order staying enforcement of the benzene standard until the Court rules on its validity. American Petroleum Institute v. OSHA, Civ. No. 78-1257 (5th Cir. April 18, 1978).
56. The term “working conditions” has been defined as something more limited than every aspect of an entire industry, encompassing both a worker’s “surrounding” and the “hazards” involved in his work. Corning Glass Works v. Brennan, 417 U.S. 188, 202 (1974).
actions will preempt OSHA regulations depends upon the intent of that agency. The other agency need not exercise its regulatory authority in the same manner or in an equally stringent manner as OSHA; however, it must articulate some formal position that a given working condition should go unregulated or that certain regulations—and no others—should apply to a defined subject.

A good example of this principle of exemption under § 4(b)(1) is provided in Southern Pacific Transportation Co. v. Usery with respect to the Federal Railroad Administration (FRA): "[c]omprehensive FRA treatment of the general problem of railroad fire protection will displace all OSHA regulations on fire protection, even if the FRA activity does not encompass every detail of the OSHA fire protection standards, but FRA regulation of portable fire extinguishers will not displace OSHA standards on fire alarm signaling systems." In Southern Railway v. OSHRC, for example, the fact that the Secretary of Transportation had exercised his authority to promulgate various safety regulations affecting the working conditions of railway employees did not exempt petitioner's maintenance facility from OSHA safety standards. The Court noted, "The safety regulations of the Department of Transportation are confined almost exclusively to those areas of the railway industry which affect over-the-road operations such as locomotives, rolling stock, signal installations, roadbeds and related facilities. While the regulatory program in these areas reflects a concern for the safety of the employees, it is directed primarily toward the general safety of transportation operations."

The applicability to the transportation industry of conduct and exposure standards promulgated and being developed for hazardous and toxic materials has not yet been clearly determined. OSHA obviously intends for these regulations to be applicable to the transportation industry. However, a different conclusion was reached by an OSHA Review Commission Judge in Hermann Forwarding Co., where an interstate trucking operation was determined to be exempt from OSHA regulations concerning the handling of hazardous materials because it was subject to DOT regulations governing the activity. In Hermann, the employer was cited for violation of OSHA regulations requiring availability of respirators during truck loading.

62. 539 F.2d 386, 392 (5th Cir. 1976).
63. Id. at 391.
64. 539 F.2d 335 (4th Cir. 1976).
65. Id. at 338.
66. In the preamble to the benzene exposure standard, for example, the unqualified assertion is made that: "Companies engaged in the transportation of benzene and benzene contaminated products are covered by the benzene standard." 43 Fed. Reg. 5918, 5938 (1978).
and unloading for use in case of spills of hazardous materials. The OSHA Review Commission Judge based his determination on the fact that DOT's enabling statute was addressed to securing safety in transit, including loading and handling, and that a DOT publication used as a reference by the employer suggested use of respirators in case of spills. 68

The applicability of OSHA health and safety standards for hazardous materials to the transportation industry will have to be determined through application of the criteria discussed in the Southern Railway and Usery cases discussed above. Current DOT regulations governing hazardous materials transportation are arguably addressed primarily to the general safety of transportation operations rather than to health hazards for individual employees. There are no DOT regulations requiring health monitoring or workplace environment monitoring for employees exposed to hazardous or toxic materials, no requirements for employee training programs for employees routinely exposed to chemicals, no specific requirements for the use of respirators or protective clothing for employees exposed to chemicals. 69 Labeling and marking requirements fall far short of proposed OSHA labels which would include a description of the hazard of exposure to the chemical, symptoms of exposure, appropriate emergency treatment, and precautions for safe use or exposure. 70 Because of the Carter Administration's emphasis on the dangers of toxic materials in the workplace, the increasing concern over worker exposure expressed by labor groups, and the considerably broader scope of OSHA hazardous materials regulations, it seems likely that most of the recent and pending OSHA regulations concerning use of and exposure to hazardous and toxic materials will be enforced against the transportation industry by OSHA and by the courts.

B. CARCINOGEN EXPOSURE STANDARDS: THE BENZENE EXAMPLE

The recently promulgated OSHA standard for occupational exposure to benzene 71 is indicative of the extent and complexity of OSHA hazardous materials regulations, especially those for suspected carcinogens. This standard provides for the measurement of employee exposure, engineering controls, work practices, protective clothing and equipment, signs and labels, employee training, medical surveillance, and recordkeeping. The supplemental information published with the benzene standard itself occupies

68. Because this decision was handed down before the appellate courts considered the question of exemption for the transportation industry in several cases and because the actual evidence of an OSHA violation or any endangerment of worker health was slight, this decision seems to be a very weak precedent.
forty-five pages of the Federal Register. The standard applies to the storage and discharge of gasoline and other petroleum products at bulk terminals; OSHA estimates that 23,471 drivers are potentially exposed to benzene at such terminals and that first-year compliance costs for bulk terminals will be approximately $17.9 million, recurring annual costs approximately $3 million, and capital investment approximately $51.5 million. Within thirty days after the effective date of the benzene standard, initial monitoring of airborne exposure levels is required by each employer who has a place of employment where benzene is produced, reacted, released, packaged, repackaged, stored, transported, handled or used. Employees must be notified of the results of this monitoring. Discovery of exposure levels over specified limits will require additional periodic monitoring, engineering and work practice controls where feasible, free medical surveillance, and use of personal protective equipment where necessary. All employers involved with the transportation or handling of benzene will be required to provide employee training programs, certain precautionary signs and labels, and extensive recordkeeping. As OSHA develops exposure standards for more hazardous and toxic materials, and as awareness of employees and labor organizations of the dangers of workplace exposure to chemicals increases, many shippers and carriers will be required to expend much time and capital to comply with OSHA exposure standards.

C. PROPOSED LABELING STANDARD

Section 6(b)(7) of the Occupational Safety and Health Act authorized the Secretary of Labor to issue standards which "prescribe the use of labels or other appropriate forms of warning as are necessary to ensure that employees are apprised of all hazards to which they are exposed, relevant symptoms and appropriate emergency treatment, and proper conditions and precautions of safe use or exposure." A Standards Advisory Committee on Hazardous Materials Labeling was set up in § 7(b) of the Act to develop guidelines for the implementation of § 6(b)(7). In September, 1976, the Committee on Government Operations of the House of Repre-

72. Id. at 5937.
73. March 18, 1978; however, see note 53 supra
74. 43 Fed. Reg. 5918, 5964 (1978) (to be codified in 29 C.F.R. § 1910.1028(d)).
75. The Act recognizes that the promulgation of some of the standards will have to be completed before sufficient data is available to make a fully informed decision. AFL-CIO v. Hodgson, 499 F.2d 467, 474 (D.C. Cir. 1974). In addition, standards are not limited by existing technology; they may require refinements in existing technology or the development of new technology. Society of the Plastics Industry, Inc. v. OSHA, 509 F.2d 1301, 1309 (2d Cir.) cert. denied 421 U.S. 992 (1975). These "technology-forcing" aspects of OSHA standards could make compliance with some standards extremely costly.
77. Id. § 656(b).
sentatives issued a report\textsuperscript{78} which concluded that OSHA had failed to adequately implement § 6(b)(7) of the Act. As a result of pressure from Congress and petitions from various public interest groups, OSHA published an Advance Notice of Proposed Rulemaking which indicated OSHA's intent to develop a labeling standard,\textsuperscript{79} and a draft of the proposed chemical labeling standards was circulated on December 30, 1977.\textsuperscript{80}

This draft standard sets up a hazardous chemical information program which involves requirements for: (a) a list of chemical and common names of all chemicals used in the workplace which would be posted or available to employees; (b) labeling of all chemical containers in the workplace, including special labeling requirements for hazardous or toxic substances; (c) substance data sheets to be prepared and available for each hazardous or toxic substance in the workplace; and (d) programs for education and training of all employees who are routinely exposed to chemicals. The draft regulations would define "hazardous substance" as any chemical which is listed in the DOT Hazardous Materials Table,\textsuperscript{81} or which meets the OSHA criteria for classification as a combustible substance, compressed gas, explosive, flammable substance, organic peroxide, oxidizer, or unstable (reactive) substance. "Toxic substance" is defined as a chemical which is listed in the National Institute for Occupational Safety and Health’s Registry of Toxic Effects of Chemical Substances, or which is reported in the Federal Register or known to the employer as being mutagenic, teratogenic, injury or disease causing, or affecting mental alertness or behavior.

An economic analysis of the draft labeling standard was to be completed in April, 1978, and may result in some reductions in the scope of the final standard. Proposed regulations will probably not be published until mid-summer, 1978, and final regulations should not be expected prior to the fall of 1978 at best. These regulations, which could impose much greater recordkeeping, employee training, health and environment monitoring, and labeling requirements on carriers who handle hazardous or toxic chemicals, will undoubtedly require major compliance efforts by many carriers. In addition, increased availability of data on exposure to chemicals and increased awareness of the dangers thereof will undoubtedly multiply the claims for occupational injuries and disease by employees.

IV. Toxic Substances Control Act

The Toxic Substances Control Act\textsuperscript{82} was enacted in 1976 after five years of Congressional hearings and consideration of bills. The purpose of

\textsuperscript{81} 49 C.F.R. § 172.101 (1976).
the Act is to prevent unreasonable risk of injury to health or the environment associated with the manufacture, processing, distribution in commerce, use, or disposal of chemical substances.\textsuperscript{83} Congressional concern was expressed over the growing number of new chemical substances introduced into commerce each year, the uncertainty over the long-term health and environmental effects of such chemicals, and the wide variety of often overlapping and uncoordinated regulatory authorities concerned with toxic substances. The word "toxic" here does not necessarily mean highly poisonous or dangerous, but rather refers to the serious effects which the substance may have on human health or on the environment over short- or long-term exposures. The control of toxic substances has been assigned a very high priority by the current Administration and by the EPA.\textsuperscript{84}

The Act, which became effective January 1, 1977, sets up an Office of Toxic Substances within the EPA to implement the toxic substances control program.\textsuperscript{85} In order to avoid development and widespread use of new chemical substances without adequate knowledge of their effects on health and the environment, EPA may require testing of a new chemical substance prior to its introduction into commerce. An inventory, to be published late in 1978, is to be developed of all chemical substances currently in use; after the inventory is published, a manufacturer must notify EPA 90 days prior to the introduction of any chemical substance not on the inventory list. EPA may also require testing of any existing substance if such substance may permit an unreasonable risk to health or the environment when distributed in commerce.\textsuperscript{86}

There are two provisions of the Act which could have a significant impact on the transportation industry: EPA regulation of chemical substances and mixtures determined to be toxic and the requirement that EPA be notified of any information indicating that a chemical substance or mixture presents a substantial risk to health or the environment. Under section 6 of the Act,\textsuperscript{87} if the Administrator finds that there is "a reasonable basis to conclude that the manufacture, processing, distribution in commerce, use or disposal of a chemical substance or mixture, or that any combination of such activities, presents or will present an unreasonable risk of injury to health or the environment," he must take steps necessary to prevent such a risk. Regulation of chemical substances and mixtures under this section

\textsuperscript{83} Id. at § 2601.

\textsuperscript{84} EPA Administrator Douglas Costle has predicted that, within the decade, the EPA program for toxic substances control "will drive all others in EPA. Increasingly, our efforts will be focused on preventing the introduction of harmful substances into our air, water, and soil, rather than cleaning them up after the damage has been done." [1977] Envr. Rep. Current Developments (BNA) 857.


\textsuperscript{86} Id. §§ 2603-2604.

\textsuperscript{87} Id. § 2605.
may be: a total prohibition on manufacturing, processing, distribution, or use of a chemical substance or mixture; limitations on the amount of the substance which may be manufactured or distributed or on the types of uses for which the substance may be provided; limitations on the manner or method of commercial use or disposal of such substance or mixture; a requirement for notification of such unreasonable risk of injury to distributors or users of such substance or mixture; and other labeling and recordkeeping requirements. Such action has already been taken with respect to one chemical substance, polychlorinated biphenyls (PCB's), as mandated by section 6(e) of the Act.

The recently promulgated PCB regulations give some indication of what may be required of transporters of chemical substances which are regulated under section 6. After October 1, 1978, any motor vehicle or rail car loaded with PCB containers containing more than 45 kilograms of PCB's or PCB mixtures or loaded with one or more PCB-filled transformers must be marked in accordance with EPA regulations for precautionary labels. Additionally, any tank car or other PCB container must be decontaminated in accordance with specific requirements. As the implementation of the Act proceeds and numerous other substances are regulated, transporters of these substances will have to be aware of and comply with an increasing number of performance standards.

In addition to regulations under section 6, the Administrator, if he determines that a chemical substance or mixture presents an imminent and unreasonable risk of serious or widespread injury to health or the environment, may commence a civil action for seizure of an imminently hazardous substance or any article containing such substance. The Administrator may also seek relief against any person who manufactures, processes, distrib-

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88. Apparently "distribution in commerce" encompasses the transportation of a substance as well as its marketing. "Distribution in commerce" of a chemical substance or mixture is defined to mean "to sell or the sale of the substance, mixture, or article in commerce, to introduce or deliver for introduction into commerce, or the introduction or delivery for introduction into commerce...; or to hold, or the holding of the substance, mixture or article after its introduction into commerce."

89. 43 Fed. Reg. 7150, 7159 (1978) (to be codified in 40 C.F.R. § 761.20(a)(2)).


91. 43 Fed. Reg. 7150, 7159 (1978) (to be codified in 40 C.F.R. § 761.20(a)(2)).

92. Id at 7163 (to be codified in 40 C.F.R. § 761.43(a)).

93. Note, however, that § 6(c)(1) of the Act, 15 U.S.C. § 2605(c)(1) (1976) provides that, if the Administrator determines that the risk of injury could be prevented or reduced to a sufficient extent by actions taken under another federal law administered by EPA, action can be taken under § 6 only if the Administrator determines that it is in the public interest to protect against the risk under this Act. Thus actions to control hazardous materials, the problems of which are limited to waste management, will be taken under the Resource Conservation and Recovery Act rather than the Toxic Substances Control Act.
utes in commerce, or uses or disposes of such substance or article.94

Section 8(e) of the Act95 requires that any person involved in the manufacture, processing, or distribution of a chemical substance who obtains information which "reasonably supports the conclusion" that a chemical substance or mixture presents a substantial risk of injury to health or the environment must immediately notify EPA of such information unless such person has actual knowledge that EPA has been adequately informed of such information. This would apply to a corporation which obtains such knowledge by virtue of the fact that its employees have such knowledge or that such information was obtained by an independent laboratory under contract to the corporation. Failure to report such information could subject the person to civil or criminal fines of up to $25,000 per day or imprisonment for not more than one year.96 EPA has issued a "Statement of Interpretation and Enforcement Policy"97 to provide guidance for compliance with the substantial risk notification requirements of the Act. This policy statement suggests that human health effects which would constitute substantial risk information include: (1) any instance of cancer, birth defects, mutagenicity, death or serious or prolonged incapacitation if one or a few chemicals are strongly implicated; or (2) any pattern of defects or evidence which reasonably supports the conclusion that the chemical substance can produce cancer, mutation, birth defects, or toxic effects resulting in death, or serious or prolonged incapacitation.98 Companies wishing to avoid direct submission to EPA of substantial risk information by lower-level employees, may, through the establishment and internal publicizing of corporate procedures for employee submission of data to the corporation, relieve such employees of any responsibility for further reporting substantial risk information directly to EPA.99 Labor organizations will soon become aware of this type of statutory provision, if they are not already. Consequently, transporters which carry a considerable amount of potentially hazardous materials should consider a program to deal with possible substantial risk data.

V. SPILLS OF HAZARDOUS SUBSTANCES

Section 311 of the Federal Water Pollution Control Act100 sets up a regulatory scheme for the prevention and cleanup of spills of oil and hazardous substances. This section provides for civil and criminal penalties for discharges, liability for cleanup costs, and federal authority to prescribe spill

94. Id. § 2606.
95. Id. § 2607(e).
96. Id. § 2615.
98. Id. at 11,112.
99. Id. at 11,111.
prevention measures for vessels and facilities handling, transporting, or storing oil or hazardous substances. Section 311(b)(2)(A) requires the EPA Administrator to promulgate regulations designating as "hazardous substances": materials which, when discharged in any quantity into the waters of the United States, would "present an imminent and substantial danger to the public health or welfare . . . " Due to internal delays and unavailability of data, no hazardous substances had been designated by EPA until March 13, 1978, when 271 substances were designated as hazardous. Although many of these 271 substances are complex organic compounds with limited use, a large number of common substances, such as ammonia, sulfuric acid, and sodium nitrite, which are frequently transported in large quantities, are included on the list.

The prohibition of discharges of oil and hazardous substances is not limited to discharges from vessels, but also applies to the owner or operator of any on-shore facility, which is defined in the Act to include motor vehicles and rolling stock. For each hazardous substance, EPA regulations set forth the amount which is considered to constitute a harmful quantity, and any discharge in excess of this quantity is a per se violation of the Act and subjects the owner or operator to imposition by the U.S. Coast Guard of a civil penalty of up to $5,000. In addition, if the substance is one which EPA has determined cannot be removed after a discharge, EPA may assess a civil penalty of up to $500,000 in the case of an on-shore facility (including tank car or truck) or up to $5,000,000 in the case of a vessel. Finally, with some exceptions for discharges for which the owner or operator was blameless, any owner or operator who discharges a hazardous substance is liable to the federal government for the actual cost of removal of the hazardous substance or other attempts to mitigate the effects of the discharge, up to a maximum of $50,000,000.

Clearly a motor carrier could incur some very large liabilities if a leak or spill of one of the designated hazardous substances should enter a sewer or a nearby body of water. EPA is authorized to establish a maximum liability for cleanup costs for on-shore facilities of less than $50,000,000 but not less than $8,000,000, and the agency is currently working on regulations.
for that purpose.\textsuperscript{108} Aside from cleanup costs, EPA has followed a policy that any spill, regardless of fault, should result in imposition of a civil penalty; consequently considerable monetary liability could be incurred by the discharge of a hazardous substance even if no cleanup was necessary. EPA and the U.S. Coast Guard have also pursued a strict enforcement policy for failure to comply with Coast Guard regulations requiring prompt reporting of any spill of oil or other hazardous materials.\textsuperscript{109} Knowing failure to report is a criminal violation of the Act which could be punished by a fine of up to $10,000 or imprisonment of up to one year, or both.\textsuperscript{110} Thus, carriers will find that they have been suddenly subjected to large potential liability for spills of a great number of substances. Increased precautions in transportation of these substances as well as adequate employee training with respect to spill prevention and notification will be necessary.

VI. PROBABLE IMPACTS OF NEW HAZARDOUS MATERIALS REGULATIONS

A. INCREASED POTENTIAL LIABILITY

As a result of the hazardous materials regulations being developed by EPA and OSHA, transporters of hazardous materials will be subjected to some new potential liability for violation of statutory requirements as well as for injury to employees or to the public. The added liability for civil and criminal penalties for violation of the new regulations should be of some concern, but should also be reasonably easy to protect against through an effective compliance program.\textsuperscript{111} The uncertain factor in analyzing the impact of these new regulations on the transportation industry is the extent to which carriers of hazardous materials will be subjected to new liability for injuries caused to their employees, the environment, or the public arising out of the transportation of hazardous materials. This question is of particular concern in light of the tremendous property damage and loss of life.

\textsuperscript{110} Section 311(b)(5), 33 U.S.C. § 1321(b)(5) (1976). Note that a knowing violation of the Act does not require actual knowledge of the owner or operator of the facility, but such knowledge can be imputed from an employee. Apex Oil Co. v. United States, 530 F.2d 1291 (8th Cir. 1976).
\textsuperscript{111} Of course it should be anticipated that, because these regulations are addressed at protecting the public and the environment from a perceived threat from hazardous materials, violations of these regulations will be taken more seriously and result in higher penalties than violations of similar statutes not addressed to such hazard. It should also be noted that, because these statutes are for the protection of a public interest, courts will be more willing to impose corporate liability for acts of employees through the doctrine of \textit{respondeat superior} “thus stimulating a maximum effort by owners and managers to assure adherence by such agents to the requirements of the Act.” United States v. Hilton Hotels Corp., 467 F.2d 1000, 1005 (9th Cir. 1973); see also Apex Oil Co. v. United States, 530 F.2d 1291 (8th Cir. 1976) (corporate liability for failure of employee to report oil spill to Coast Guard or EPA).
which has occurred in 1978 as a result of incidents involving railroad transportation of hazardous materials.

There is, of course, a doctrine of strict liability in many jurisdictions which may be applied to the transportation of hazardous materials. Under this doctrine, an "ultrahazardous" or "abnormally dangerous" activity may result in the imposition of liability without intentional malfeasance or negligence. The potential for imposition of strict liability on transporters of hazardous materials has been present in most jurisdictions for some time and will not be affected by current regulatory activities except that, as a result of further definition of the dangers of hazardous materials, more activities of transporters may, in the future, fall within the classification of ultrahazardous or abnormally dangerous activities.

The new regulations may, however, serve as a standard of conduct or define negligence itself with respect to either employees or members of the public. The employer's duty to employees may arise either out of the general common law duty to maintain a safe workplace or out of some statutory duty for the protection of employees, such as the Federal Employers' Liability Act or workmen's compensation statutes. In most jurisdictions, the recently enacted statutes could be applied in negligence suits against transporters of hazardous materials through the doctrine of negligence per se. If the plaintiff is within the class of persons which the statute was designed to protect and the injury which occurred was the type of injury against which the statute was designed to protect, an unexcused violation of that statute would be conclusive on the issue of negligence although some of the courts which follow this rule as to statutes would hold that breach of the regulations of administrative bodies is only evidence of negligence for the jury. For example, the courts have repeatedly rejected the argument that the Occupational Safety and Health Act impliedly creates a private cause of action in employees under federal law for violation of OSHA standards, but it has been held that a violation of an OSHA regulation can be negligence per se with respect to an injured employee. Although violation of an OSHA standard could constitute negligence per se only with respect to an

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112. See, e.g., RESTATEMENT (SECOND) OF TORTS § 520; Morris, Hazardous Enterprises and Risk Bearing Capacity, 61 Yale L.J. 1172 (1952).
employee, EPA regulations are arguably designed to protect any member of the public, and an OSHA standard could be admissible as evidence of negligence even against a non-employee.

In addition, an OSHA or EPA regulation may be admissible as evidence of the standard of care, even if such regulation is not strictly applicable to the transporter’s operation.117 This could be true, for example, of OSHA regulations from which a transporter is exempted by virtue of § 4(b)(1) of the Occupational Safety and Health Act.118 Intentional violation of regulations by the injured party or other negligent action on his part may constitute contributory negligence but in some cases such a defense may not be available. Some statutes, such as the Boiler Inspection Act119 and factory acts for the protection of workmen120 have been construed to be intended to protect persons against their own negligence and therefore to place the entire responsibility for protection of that class of persons upon the railroad or factory owner.

If a carrier complies with all OSHA, EPA, and DOT regulations, is this conclusive evidence that he was not negligent with respect to the persons whom those regulations are intended to protect? If the regulatory standard is so comprehensive and so circumscribed that the carrier is precluded from taking any actions or precautions other than those required under the regulations, compliance with the regulation will almost certainly insulate him from any liability for negligence. In any other case, however, courts have generally taken the position that compliance with the regulation only indicates some degree of care, but not necessarily the level of care owed to the injured party.121 In Hubbard-Hall Chemical Co. v. Silverman,122 the defendant pesticide manufacturer had complied with U.S. Department of Agriculture labeling requirements under the Federal Insecticide, Fungicide, and Rodenticide Act.123 In a wrongful death suit for the poisoning deaths of two illiterate farm workers, it was held that the warning provided by Hubbard-Hall was insufficient to provide "adequate instructions or warnings of [the pesticide's] dangerous condition" despite the fact that the label had

117. For the similar issue of the admissibility of voluntary safety codes or standards on the issue of negligence, see Annot., 58 A.L.R. 3d 148 (1974).
118. See text accompanying notes 56-70 supra.
120. Osborne v. Salvation Army, 107 F.2d 929 (2d Cir. 1939).
122. 340 F.2d 402 (1st Cir. 1965).
been fully approved by the Department of Agriculture. Thus complete compliance with the regulatory programs discussed in this article will not ensure the carrier from liability to injuries sustained to employees, the environment, or the public as a result of its transportation of hazardous materials.

B. INCONSISTENCY

It is difficult to predict whether the hazardous waste and toxic substances regulations will have the effect of increasing or decreasing the variation which currently occurs from state to state in the regulation of hazardous materials transportation. In the toxic chemical substance area, several states have already passed legislation dealing with the dangers of toxic chemical substances. Additional states may now follow the federal lead and pass their own toxic substances legislation; however, section 18 of the Toxic Substances Control Act provides for the preemption by EPA regulations of any state law or regulation which is not at least as stringent as the EPA requirement or which, "through difficulties in marketing, distribution, or other factors, unduly burden[s] interstate commerce." Due to the expected complexity of toxic substances control, it seems unlikely that individual states will wish to create or expand their own toxic substances control programs.

Authorized state hazardous waste programs under the Resource Conservation and Recovery Act must be "equivalent" to the federal minimum standards for hazardous waste management, but this does not mean that individual states could not develop different or more stringent requirements for transporters of hazardous waste than established by EPA standards or by other state hazardous waste programs. Unlike the Hazardous Materials Transportation Act, the Resource Conservation and Recovery Act does not have any provision for requesting a determination of whether a state requirement is inconsistent with and therefore preempted by the Act. There is consequently some potential for troublesome variations in

124. 340 F.2d at 405.
128. See text accompanying notes 27-28 supra.
130. For HMTA preemption provision, see 49 U.S.C. § 1811(b) (1976); for DOT regulations for obtaining an inconsistency determination, see 49 C.F.R. §§ 107.201-.225 (1976). Note, however, that, to the extent that EPA regulations incorporate DOT regulations under the HMTA, inconsistent state and local requirements are preempted by HMTA requirements. See 43 Fed. Reg. 22,626-28 (1978).
hazardous waste transportation regulations from state to state under the Act. The threat of inconsistency among states is somewhat less under the Occupational Safety and Health Act, since any state standards developed and enforced under an approved state program relating to a health and safety issue which has been addressed by an OSHA standard must be "required by compelling local conditions" and must not "unduly burden inter-state commerce."  

VII. CONCLUSIONS

The developments discussed above in the areas of hazardous wastes, toxic substances, and employee exposure will affect the transportation industry in several areas. Some firms will find the new regulations cause an increase in their business while others will find that they are unable to profitably handle hazardous materials, but most carriers will experience compliance costs and exposure to significant liability as a result of the regulations now being developed. Compliance costs will vary with the type of operation and amount of hazardous materials handled, but it seems likely that OSHA standards could require the greatest compliance effort. The Resource Conservation and Recovery Act\textsuperscript{132} has the potential for increasing the need for transportation of solid waste and especially hazardous waste. As the transportation of hazardous and toxic materials becomes more highly regulated and requires greater precautionary efforts, many firms will be unable or unwilling to make the necessary compliance efforts, and those firms which are committed to compliance with such hazardous materials regulations will undoubtedly find increased need for their services.

It will take several years for the OSHA and EPA regulatory programs discussed above to begin to have their full impact upon the transportation industry. It is important at this time to become aware of these developments and to ensure, so far as possible, through participation in the rulemaking process, that these regulations do not present an unreasonable burden to carriers of hazardous materials.

Toward Responsible State Regulation of Air Pollution: Oregon's Mandatory Inspection/Maintenance Program

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INTRODUCTION

The Federal Clean Air Act\(^1\) calls for state and local solutions to the national problem of air pollution. The Act requires states to devise State Implementation Plans (SIP's),\(^2\) in which strategies for controlling pollution sources are to be proposed for the purpose of bringing that state's air quality within EPA air quality standards. These Plans must be submitted to the

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2. Id. § 7410.
EPA for its approval. Certain states, which contain areas in which levels of pollutants associated primarily with motor vehicles exceed national standards, are also required to submit Transportation Control Plans (TCP’s) for those areas as part of that state’s SIP. Although states have submitted SIP’s, local solutions to mobile source air pollution, as envisioned by the Act, have, for the most part, not been forthcoming.

Because of the states’ traditional control over motor vehicle registration, the states are best equipped to play the major role in controlling and reducing mobile source air pollution. The apparent failure of the states to assume the primary role in controlling vehicular air pollution has prompted major litigation raising constitutional issues which go to the heart of the federal system. This litigation has brought into question the traditional notion

3. Id. § 7410(a)(1), (2). "The Administrator shall, within four months after the date required for submission of a plan under paragraph (1), approve or disapprove such a plan or each portion thereof. . ." Id. § 7410(a)(2). The Act also required EPA approval of any revision of a SIP. Id. § 7410(a)(3)(A).

4. The EPA has compiled a list of such areas for which TCPs are required. See note infra.

The Clean Air Act Transportation Control Plans have been defined by EPA regulations as "the summation of individual actions (transportation control measures) that will, when taken collectively, reduce concentrations of carbon monoxide and photochemical oxidants in the atmosphere from those achieved by the Stationary Source Control Program and the Federal Motor Vehicle Control Program (FMVCP) to the level prescribed by the National Ambient Air Quality Standards." 40 C.F.R. § 51.1(f) (1975). Current Federal regulations require that Plans shall contain "[a] description of enforcement methods including, but not limited to, procedures for monitoring compliance with the selected traffic control measures, procedures for handling violations, and a designation of enforcement responsibilities (i.e., air pollution control agency, State police, State Department of Motor Vehicles, State Registrar of Motor Vehicles, etc.)." 40 C.F.R. § 51.14 (a)(2)(ii)(i) (1977). See also, id. § 51.14 (a)(2)(ii),(iii),(iv). 42 U.S.C. § 7408(f)(1) (1976) suggests appropriate transportation control measures to include motor vehicle emission inspection and maintenance programs, programs for improved public transit, programs to establish bus and carpool lanes, programs to control on-street parking, programs to construct bicycle lanes, and retrofist programs.


6. Congressionally authorized extensions have given many states the opportunity to postpone attainment of air quality standards. 42 U.S.C. § 7410(a)(1), (2) (1976). For example, Oregon was given a twelve-month extension, 40 C.F.R. § 52.1981 (1977). Kentucky was given a two-year extension. Id. § 52.922. Colorado was given a 3-1/2 year extension for attainment of national carbon monoxide standards in the Metropolitan Denver Inlandt Air Quality Region. Id. § 52.322(b). Congressional or administrative indulgence was not the only reason for state delay. Both the states and the EPA Administrator experienced considerable difficulty in developing adequate plans. For example, California’s proposed TCP was disapproved by the Administrator on May 31, 1972, because it contained no provisions for the control of photochemical oxidants. Thereafter, the EPA itself was unable to develop an adequate Plan for California within the time required by the Act. 1 F. Grad, TREATISE ON ENVIRONMENTAL LAW § 2.03, at 2-90.6 (1977). This sequence of events fostered the case of Riverside v. Ruckelshaus, 4 E.R.C. 1728 (D. Cal. 1972), a citizen suit which was brought to compel the Administrator to carry out his non-discretionary duty to promulgate a locally adequate implementation plan. The eventual EPA-imposed plan led to the lower court case of Brown v. EPA, 521 F.2d 827 (9th Cir. 1975). See notes 15, 16 and 17 infra.

7. For a discussion of the reasons for state and local resistance to Clean Air Act mandates and resulting litigation, see Stewart, Pyramids of Sacrifice? Problems of Federalism in Mandating

HeinOnline -- 10 Transp. L.J. 122 1978
that the states have the exclusive right to register, and hence control, motor vehicles owned by their residents. The EPA has sought through such litigation to impose, among other things, vehicle emission inspection and maintenance (I/M) programs where states have failed to promulgate suitable TCP’s. Although an I/M program is no panacea for controlling air pollution from motor vehicles, the EPA has long maintained that an I/M program linked to registration of in-use vehicles can be the most effective method available to the states to reduce pollution from the automobile.

A few states have recognized the utility of I/M programs in abating air pollution. A good example is the I/M program which has been implemented by the State of Oregon in the Portland metropolitan area as part of Oregon’s TCP. Oregon’s I/M program was designed to identify, prior to motor vehicle registration or re-registration, those motor vehicles which fail to meet pollution emission standards and to ensure that remedial maintenance or adjustments are performed on such vehicles. Using the Oregon program as a model, this article will discuss the reasons favoring state level adoption and implementation of an I/M program as part of a Transportation Control Plan called for under the Federal Clean Air Act. It will assess the relationship between the EPA and the states to help identify their respective obligations within the context of the Act. Then, the choices available to states in fashioning unique and effective programs will be discussed in light of the Oregon experience. Finally, the ability of states to regulate interstate mobile source pollution will be evaluated.

State Implementation of National Environmental Policy, 86 YALE L.J. 1196, 1202-05 (1977) [hereinafter cited as Stewart].

8. See, e.g., Maryland v. EPA, 530 F.2d 215 (4th Cir. 1975); cases cited note 15 infra. For a description of the EPA-imposed I/M program for Maryland, see 40 C.F.R. § 52.1089 (1977).

9. The EPA’s position is that inspection and maintenance programs are “the most important of the transportation control measures currently enforced. ...” 42 Fed. Reg. 30,504, 30,505 (1977) (to be codified in 40 C.F.R. § 52). See also note 10 infra.

THE EPA AND THE STATES: A DELICATE BALANCE

The Clean Air Act of 1970 and all subsequent amendments reflect a congressional concern that the states have not fulfilled their role in abating air pollution.\textsuperscript{11} To this end, the 1977 Clean Air Act Amendments give the EPA Administrator authority to identify non-attainment areas which are areas where levels of identified pollutants continue to exceed national air quality standards.\textsuperscript{12} The 1977 Amendments set new deadlines for the submission or revision of SIP's for states which have such areas.\textsuperscript{13} The Administrator is given power by the 1977 Amendments to make appropriate findings which can, commencing July 1, 1979, lead to the curtailment of EPA grants and curtailment of certain highway monies\textsuperscript{14} to any area which has not attained federal air quality standards.

The ability of the EPA Administrator to otherwise enforce the provisions of the Act upon the states has been addressed in the group of cases collectively known as \textit{Brown v. EPA}.\textsuperscript{15} In the \textit{Brown} cases, the EPA sought generally to compel state officials through Clean Air Act enforcement provisions to implement relevant portions of their TCP's, including vehicle I/M pro-

\textsuperscript{11} For example, Justice Rehnquist, in his opinion in \textit{Train v. Natural Resources Defense Council}, 421 U.S. 60, 64 (1975), observed the 1970 Amendments to the Clean Air Act as "amounting to taking a stick to the states."

\textsuperscript{12} 42 U.S.C. § 7501(2) (1976) defines a "non-attainment area" as an area which, for any air pollutant which is shown by monitored data or which is calculated by air quality modeling or other reliable methods determined by the EPA Administrator, exceeds any national ambient air quality standard for such pollutant. Id. § 7407(d)(1) provides that the states shall, within 120 days after Aug. 7, 1977, submit to the Administrator a list identifying air quality control regions or portions thereof which do not meet certain national primary or secondary ambient air quality standards.

The EPA has recently released a list of areas which have not attained required standards. "The listing shows that out of 3,215 total counties in the U.S., 606 counties or portions thereof are violating standards for photochemical oxidants . . . ; . . . 190 counties are violating standards for carbon monoxide; . . . A county may be violating more than one pollutant standard, so the same county may be counted in more than one category in the above totals." EPA, Press Release, Environmental News 2 (Feb. 24, 1978).

\textsuperscript{13} 42 U.S.C. § 7052(a)(2) (1976) provides for plans calculated to achieve attainment of national primary ambient air quality standards for photochemical oxidants or carbon monoxide by Dec. 31, 1987. Id. § 7502(c) requires that a plan revision shall contain enforceable measures to assure attainment of the applicable standard not later than July 1, 1987. Id. § 7502(b)(11)(B) provides that the plans which make a demonstration pursuant to id. § 7502(a)(2) establish, among other things, "a specific schedule for implementation of a vehicle emission control inspection and maintenance program."

\textsuperscript{14} 42 U.S.C. § 7506(a) (1976). In addition, id. § 7506(b) prohibits the EPA from making any grants under the Clean Air Act in areas of a state where state or local officials are not implementing required transportation control measures.

\textsuperscript{15} \textit{Brown v. EPA}, 521 F.2d 827 (9th Cir. 1975); \textit{Arizona v. EPA}, 521 F.2d 825 (9th Cir. 1975); \textit{District of Columbia v. Train}, 521 F.2d 971 (D.C. Cir. 1975); \textit{Maryland v. EPA}, 530 F.2d 215 (4th Cir. 1975). A decision upholding regulations pertaining to Pennsylvania was not before the Brown court. Pennsylvania v. EPA, 500 F.2d 246 (3d Cir. 1974). In addition, Virginia and the District of Columbia filed separate petitions for certiorari from the District of Columbia case. 426 U.S. 904 (1976).
grams. At the Supreme Court level, the EPA abandoned the idea that it could compel the states to enact I/M legislation and the attendant regulations, among other things. However, two circuits have indicated that the Administrator could impose I/M requirements through appropriate injunctive proceedings. An injunction could, for example, prohibit a state from registering any vehicle which does not meet federal pollution standards.

Because an I/M program is nearly impossible to administer efficiently unless somehow linked to vehicle registration, and because states are the sole registrars of most motor vehicles, all EPA enforcement with respect to I/M programs will necessarily involve compulsion of state action. A possible impediment to such compulsion through direct federal regulation of private passenger cars or through injunctive relief is found in the case of National League of Cities v. Usery. In Usery, the Supreme Court held that the 1974 Amendments to the Fair Labor Standards Act, setting federal minimum wage and maximum hour requirements, constituted an impermissible interference with important state and local governmental functions and

16. The EPA sought to compel the states to enact regulations and laws through enforcement sanctions provided in 42 U.S.C. § 7413 (1976). The Ninth Circuit Brown decision involved EPA regulations directing state compliance with a number of TCP measures, including an inspection and maintenance program. 40 C.F.R. § 52.242 (1977). The Ninth Circuit held that the Clean Air Act did not authorize the imposition of such sanctions for any failure of the State of California to comply with the directions contained in these regulations, among others. The basic contention of the states challenging the EPA enforcement regulations was that the commerce power of Congress does not allow Congress to require states to enforce federal regulatory laws, that the states are guaranteed a republican form of government by the Constitution so as to allow them to provide state laws concerning matters of strong local interest and that to so require the states to become mere enforcement arms of the Federal government would be to "reduce the states to puppets of a ventriloquist Congress" and pave the way for the "utter destruction of the State as a sovereign political entity." Brown v. EPA, 521 F.2d 827, 839 (9th Cir. 1975). For an analysis of decisions in other lower court cases, see Stewart, supra note 7; Gordon, When Push Comes to Infringement of State Sovereignty: Implementation of EPA's Transportation Control Plans, Wis. L. Rev. 1111 (1976) [hereinafter cited as Gordon]; Hostetter & Sale, Protection of the Environment and Protection of the States: The Constitutional Issue Raised by EPA Action Under the Clean Air Act, 7 Env. L. Rev. 383 (1977).

17. EPA v. Brown, 431 U.S. 99 (1977). "The [Government's] position now appears to be that, while the challenged transportation plans do not require the enactment of state legislation, they do now contain, and must be modified to eliminate, certain requirements that the state promulgate regulations. See Government Reply Brief, at 14, n.22" Id. (emphasis in original).

18. In District of Columbia v. Train, 521 F.2d 971,994 (D.C. Cir. 1975), the District of Columbia Circuit indicated that "the commerce power does enable the federal government to prohibit the states from registering non-conforming vehicles..." Moreover, in Brown v. EPA, 566 F.2d 665, 670 n.4 (9th Cir. 1977), the Ninth Circuit, on remand, indicated that Congress intended to provide injunctive relief which, if feasible, could provide "for Federal implementation and enforcement of the program (including Federal licensing of private I/M centers... and imposing Federal inspection fees)..." 19. See District of Columbia v. Train, 521 F.2d 971 (D.C. Cir. 1975).


thereby contravened principles of federalism implicit in the Tenth Amendment.22 Usey recognized that there are "attributes of sovereignty attaching to every state government which may not be impaired by Congress."23 However, Justice Blackmun, in his concurring opinion, pointed out that the Court's decision "adopts a balancing approach, and does not outlaw federal power in such areas as environmental protection, where the federal interest is demonstrably greater and where state facility compliance with imposed federal standards would be essential."24

Going further, the collection of cases known as Friends of the Earth v. Carey25 has arguably clarified Justice Blackmun's concurring opinion in Usey to the extent that, if a state does promulgate and submit a TCP which is approved by the EPA, private citizen action to enforce such a Plan against the state will not constitute federal intrusion into essential state functions.26 The spectre of federal intervention through economic sanctions or

23. Id.
24. Id. at 856 (emphasis added).
25. This collection of cases originated as private citizen suits, authorized under Section 304 of the Clean Air Act, 42 U.S.C. § 7604 (1976), in Friends of the Earth v. EPA, 499 F.2d 1118 (2d Cir. 1974) (Friends I), the Second Circuit Court of Appeals, while approving the TCP for metropolitan New York City, denied immediate implementation of the plan. In Friends of the Earth v. Carey, 535 F.2d 165 (2d Cir. 1976) (Friends II), the Second Circuit held that, pursuant to Section 110 of the Clean Air Act, "a plan, once adopted by a State and approved by the EPA becomes controlling and must be carried out by the State." Id. at 169. The Circuit Court therefore ordered implementation of the plan. Friends II was remanded to the District Court for the Southern District of New York. On remand, Judge Duffy held that, in light of the decision in National League of Cities v. Usey, 426 U.S. 833 (1976), Congressional use of the Commerce Clause to compel New York City to enforce the plan against others would violate the City's rights under the Tenth Amendment. See Friends of the Earth v. Carey, 552 F.2d 25, 29 (2d Cir. 1977) (Friends III). The plaintiffs appealed Judge Duffy's ruling and obtained a reversal in Friends III. Id.
26. In Friends III the Second Circuit stressed that implementation of the Transportation Control Plans at issue would not amount to the kind of injury found to be impermissible in National League of Cities, since the essential policy choices involved in creating the program were entirely within the control of the State and the participating City agencies, and not imposed by the federal government." Id. at 38. The court in Friends III awarded coercive relief against state officials because the TCP had been devised by the state rather than by the EPA. But see Stewart, supra note 7, at 1205, for a criticism of this reasoning.

The Friends III court followed the tests formulated in Usey because "there was (1) a serious problem which endangered the well-being of all the component parts of our federal system and which only collective action by the National Government might forestall," (2) a carefully drafted program designed for very limited interference with states' freedom, and (3) a program that "displaced no state choices as to how governmental operations should be structured . . . " [citations omitted]." Friends of the Earth v. Carey, 552 F.2d 25, 39 (2d Cir. 1977). In light of these tests, it is probable that the federally promulgated I/M programs for Maryland and California would have been constitutionally objectionable had the EPA not conceded in Brown v. EPA. See note 17 and accompanying text supra. Direct federal compulsion of local or state officials to implement a program which had not been previously promulgated or submitted to the EPA by state officials might have been held to be an impermissible and disruptive interference with state governmental functions proscribed by the Tenth Amendment. Such "heavy handed" enforcement attempts would be
injunctive proceedings, in addition to private citizen suits brought to enforce a state-enacted TCP, should prompt a state to act responsibly to control air pollution and thereby prevent the erosion of its traditional control over motor vehicles.

Although the prospect of federal judicial intrusion into what would otherwise be a state’s internal affairs looms over a state’s failure to take action, the Federal Clean Air Act clearly indicates a congressional intent to encourage cooperation, not only among the states but between the states and the federal government. The EPA Administrator has not been given sole authority to deal with problems of air pollution Congress envisioned the proper role of the EPA in a smoothly functioning federalist system as that of providing assistance, both financial and technical, to states which are designing, implementing and enforcing TCP’s. The states are to retain the power to control mobile source pollution through the innovative exercise of their traditional power to regulate the automobile. It is in the exercise of this power that the states will prevent federal interference.

STATE INTERESTS IN IMPLEMENTING I/M

For some time, means have been available to states to reduce mobile source pollution through their own motor vehicle laws. However, a major reason for state delay in utilizing these means has been the reluctance of state legislators to undertake the control of air pollution through the politically unpopular avenue of further regulation or restriction of use of automobiles owned by their constituents. Delay may also be due to an

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27. 42 U.S.C. §§ 7401(b) and 7402(a), (b) (1976).
28. "The 1977 Amendments reaffirm Congressional intent that States be the prime decision-makers on air pollution policy, and EPA intends to reflect this attitude. Although EPA cannot legally tolerate a situation where human health standards are continuously violated, we intend to allow States all the flexibility the law allows in meeting their clean air goals." EPA Press Release, supra note 12 (quoting EPA Administrator Douglas Costle).
31. "Trying to take the automobile from car-loving Americans is like attempting to rescue Fay
unwillingness to appropriate money for an apparently unpopular program. The reluctance of state officials to face such an unpopular decision may be based upon the premise that if they do not impose additional restrictions on their constituents' automobiles, the EPA eventually will, thus shifting political accountability for such interference elsewhere. Moreover, such regulation is commonly perceived as a deterrent to economic growth and the creation of more jobs; indeed, economic benefits may result if a state appears to be a pollution haven for auto-intensive business.

These political and economic beliefs have been cited as reasons for the enactment of federal measures to compel state action to achieve national air quality goals. However, the validity of these beliefs is questionable. As we will be discussed, an I/M program for most motorists entails little more regulation than that which now exists under state motor vehicle registration laws; and the expense to both a state and its motorists is minimal. Passage of I/M legislation, if handled properly, need not be politically unpalatable to state legislators. Furthermore, no evidence of any mass movement of auto-intensive industry away from areas with I/M has been found. Even if businesses did move to unregulated pollution havens, their gains would be temporary at best because of the EPA's present ability and willingness to impose economic and legal sanctions.

If a state refuses to deal responsibly with its own pollution problem, then it justifiably invites EPA interference. Such interference may result in certain negative consequences which state officials and local legislators may find difficult to explain to their constituents. Centralized EPA policy-making might reflect a lack of sensitivity to local needs, institutions and prejudices. One example of such policy-making is an EPA announcement that San Franciscans had to cut annual auto mileage by 97% and the resul-
tant hostility generated by this announcement. 35 Another example is found in one of the Brown cases, where the EPA sought to require Maryland to submit legally adopted regulations to implement such EPA requirements as "inspection of all . . . motor vehicles at periodic intervals no more than one year apart . . . ." 36 Such a requirement failed to consider the conceivably burdensome conflicts with Maryland's motor vehicle registration laws and presupposed the availability of funds for the program. 37 At the very least, state legislators should immediately examine their motor vehicle registration laws to determine the compatibility of those laws with EPA requirements for vehicle I/M programs. As discussed later, appropriate legislation can be enacted to structure a vehicle registration system which will not be disrupted by any I/M program required by the EPA.

Even assuming that EPA officials will consult with and invite extensive cooperation from local officials in formulating an I/M program, the EPA's major interest will be achievement of national air quality standards. The needs, desires and opinions voiced by the citizenry of the area regarding methods of achievement will be of only secondary concern. 38 Even if eventual EPA imposed programs are similar or even identical to what the local government would have fashioned itself, local citizen debate and idea input will have been lost or diluted. 39 This means that, in ceding the decision-making to a federal agency, the state has undermined to some extent its control over its own tax revenues and the voting power which its electorate might have exercised in determining the outlines of the I/M program. 40

In sum, even though required to be approved by the EPA, a state initiated I/M program preserves: existing state control over motor vehicles reg-

35. 38 Fed. Reg. 31,244 (1973); Stewart, supra note 7, at 1204.
38. "Once a substantial program of environmental protection is launched, these federal bureaucracies' very size, professional orientation, and remoteness also makes them comparatively less sensitive to public discontent when the economic and social costs of such programs become apparent, particularly if these costs fall disproportionately on a few regions. For analogous reasons, public protests, especially if localized, will have less impact on federal judges and legislators than on their state and local counterparts." Stewart, supra note 7, at 1218.
39. "Decisions about environmental quality have far-reaching implications for economic activity, transportation patterns, land use, and other matters of profound concern to local citizens. Federal dictation of environmental policies depreciates the opportunity for and value of participation in local decisions on such matters. The impairment of local self-determination is considerably aggravated when (as in transportation control context) local fiscal resources and governmental powers are conscripted by federal agencies." Id. at 1220-21.
40. The lower court in Brown v. EPA, 521 F.2d 827, 840 (9th Cir. 1975) observed that "voters of other states, acting through their representatives in Congress, would dilute the strength of votes of the state whose revenues would be spent as Congress directs" and that such a result would not promote harmonious federalism.
istered by that state, existing state control over allocation of state revenues, and the right of state residents to determine, through their vote, the nature and scope of the state's I/M program. It reserves to a state's citizens the right to modify and adapt the program as local requirements change. Oregon's I/M program exemplifies how one state has preserved these traditional functions for itself and its citizens while achieving a substantial reduction in air pollution levels throughout the Portland metropolitan area.

A STATE'S ABILITY TO ACHIEVE RESULTS: THE OREGON EXPERIENCE

A. VOLUNTARY PROGRAM

Because of the number of violations of federal primary ambient air standards occurring in the Portland metropolitan area, Oregon's Environmental Quality Commission (EQC), the agency charged with establishing air quality policies, recommended in 1972 that a vehicle I/M program be initiated in the four Oregon counties comprising this area. Pursuant to the recommendations of the EQC, a voluntary compliance program was instituted in early 1974. Over 105,000 voluntary emission tests were conducted from February, 1974 through June, 1975.

This voluntary program had several advantages. Test results obtained during the voluntary phase were used to establish inspection program pass/fail criteria for each and every type of automobile subject to the inspection requirement. The standards, designed to promote proper emission maintenance of vehicles, incorporated the various maintenance

44. EQC Report, supra note 41, app. C-1.
46. Id. at 348, 349. "These standards, unlike the City of Chicago standards used during the voluntary program, account for differing vehicle designs and thus are more equitable, while still capable of achieving significant reductions." EQC Report, supra note 41, app. C-3. The ability of states to determine their own emission standards is illustrated by the differing approach taken by Oregon from that of the City of Chicago. The Oregon approach sets emission standards for each type of vehicle, with the objective of encouraging proper vehicle maintenance. A state which adopts uniform emissions standards, regardless of the type of vehicle, would seek to encourage maintenance to a lesser degree and discourage ownership of high emission types of vehicles. Such opportunities for states to choose a diversity of standard setting techniques was recognized by Justice Rhenquist in Train v. Natural Resources Defense Council, 421 U.S. 60, 79 (1975), where he noted that "[t]he Act gives the Agency no authority to question the wisdom of a State's choices of emission limitations if they are part of a plan which satisfies the standards of § 110(a)(2). . . ."
requirements of the manufacturers. The voluntary phase also afforded Oregon’s Department of Environmental Quality (DEQ), which was given primary responsibility for administration of the program under policies established by the EQC, the needed lead time to confirm the reliability of the chosen equipment and allowed DEQ inspection personnel to gain experience. In addition, it gave the Legislature time to determine the exact boundaries of the area where I/M was most needed. During 1974, the Legislature established July 1, 1975 as the startup date for mandatory inspection and restricted the area of the program to the boundaries of the Metropolitan Service District (MSD), which includes the city of Portland and most of its significant suburbs. Finally, the voluntary phase provided the DEQ with the opportunity to educate the public about the program and its benefits. As a result of the voluntary inspections and DEQ public relations efforts, most motorists became familiar with the inspection requirement prior to July 1, 1975.

B. Mandatory Program

Since July 1, 1975, all motor vehicles registered within the MSD, with certain exceptions, must pass a standard idle emission test for carbon monoxide (CO) and hydrocarbons (HC) as a pre-condition for Motor Vehicles Division registration. Certification is required for most in-use vehicles, which are required to be re-registered every two years from the date of initial registration by the state. While there are no direct sanctions for failing the inspection, a vehicle which fails to meet the prescribed standard for that make and model of vehicle cannot be registered until it meets such standard. Vehicle HC and CO emissions are measured by gas analyzing

47. Householder, MVECC IV, supra note 43, at 349.
51. Id. The MSD is defined in id. § 268.020(2).
52. See Householder, MVECC IV, supra note 43, at 340, 347, 348. In addition to voluntary testings, the DEQ invited citizen reports on smokey vehicles, and 20,000 bumper stickers were distributed.
53. Or. Rev. Stat. § 481.190(2) (1977) requires dating of certification within 90 days prior to motor vehicle registration or renewal of registration date.
54. Id. § 481.135, provides for a registration or renewal of registration period of 24 consecutive calendar months for most vehicles.
55. Id. § 481.190(2). Approximately 70% of all cars taking the test have passed the first time. Ore. Task Force Report, supra note 49, at 4. Responses to the most recent DEQ survey indicate that, of those cars failing the initial inspection, 65.5% required repairs costing less than $10 to pass the test, with 94.8% passing the test after repair. Vehicle Inspection Program, Dep’t of Environmental Quality, Cost of Repair Survey (DEQ/VIP 77341) (1977). Usually, the solution involves some item of routine maintenance that has been neglected or delayed, such as an idle
equipment at the unloaded engine speed while the vehicle is stationary and the accelerator pedal is released (idle speed). Vehicles which are presently exempt from Oregon's I/M program include new motor vehicles, farm vehicles, special interest (antique) automobiles, vehicles manufactured before 1942, fixed load vehicles, and vehicles operating in interstate commerce.

Oregon's I/M program has been administered and enforced largely by licensed state employees at inspection facilities operated by the DEQ. However, owners of fleets comprising 100 or more in-use motor vehicles are permitted to conduct their own I/M inspection on their fleets under the supervision of the DEQ, provided DEQ-approved gas analyzing equipment is used, and provided the inspector, who may be an employee, has been qualified by the DEQ. Owners of large fleets are encouraged to inspect their own vehicles because fleet self-inspection reduces the number of inspections that the state must make and is also convenient to fleet owners.

At present, owners of fleet vehicles must pay a certificate fee of $2 per vehicle. A fee of $5 is charged the owner of any vehicle which is inspected at state facilities and which passes the DEQ inspection. With the exception of startup costs appropriated during the voluntary phase of the program, these fees have provided sufficient funds to finance the entire I/M program.

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56. Or. Ad. Rules § 340-24-305(18) (July 1, 1977). Vehicle emission control test standards adopted in early 1975 by the EQC were used when the program became mandatory for the MSD. DEQ Motor Vehicle Emission Control Inspection Test Criteria, Methods and Standards, Or. Ad. Rules § 340-24-300 to 350 (effective May 25, 1975). Emission allowance standards for CO and HC vary depending on the make and year of the vehicle and, sometimes, the engine size. Exhaust gas concentrations of CO and HC are measured at idle speed and compared to the appropriate standard. Vehicles exhibiting smoke, exhaust gas dilution, excessive idle speed, or faulty factory installed emission systems will not be issued certificates. Or. Ad. Rules § 340-24-320(1), (2), (3) (July 1, 1977).

57. OR. REV. STAT. § 481.190(3) (1977).

58. EQC REPORT, supra note 41, at app. C.

59. Or. Ad. Rules § 340-24-340(1), (8), (9), (10) (July 1, 1977). Thus far, at least fifteen fleets in Oregon have been certified to conduct private inspections. EQC REPORT, supra note 41, app. D-2.

60. EQC REPORT, supra note 41, app. D-1.

61. Id.


64. ORE. TASK FORCE REPORT, supra note 49, at 4.
C. RESULTS OF OREGON'S PROGRAM

Since the advent of Oregon's I/M program, there has been a significant reduction of carbon monoxide in the Portland metropolitan airshed. For instance, CO exceeded federal minimums on only 27 days in 1976,\textsuperscript{65} as opposed to 88 days in 1970.\textsuperscript{66} There has been a corresponding decrease in hydrocarbons as well.\textsuperscript{67} The reduction of CO and HC pollutants should have beneficial effects upon the health of the inhabitants of the Portland metropolitan area.\textsuperscript{68} In addition to these health benefits, the reduction of pollutants in the atmosphere should improve what is commonly known as the quality of life for area residents. Refusing to espouse the idea of more business at the expense of clean air, Portland has adopted the attitude that cleaner air improves the quality of life.\textsuperscript{69} It has successfully promoted its present quality of life as an attraction to non-polluting business such as tourism and the convention trade.\textsuperscript{70}

In addition to demonstrable improvements in air quality, it is asserted that the maintenance compelled by periodic emission inspection results in decreased gasoline consumption.\textsuperscript{71} Several studies have supported this

\textsuperscript{65} DEPARTMENT OF ENVIRONMENTAL QUALITY, OREGON AIR QUALITY REPORT FOR 1976, AIR QUALITY DATA SUMMARY.

\textsuperscript{66} See EQC REPORT, supra note 41.

\textsuperscript{67} The EQC has estimated that the I/M program reduced vehicle HC emissions by 2.5% in 1975 and 7% in 1976. Id. at app. G-7. Because photochemical oxidants are measured rather than HC, it is difficult to directly measure HC reductions in the airshed. In Sierra Club v. EPA, 540 F.2d 114 (D.C. Cir. 1976), the EPA contended that interrelationships among CO, HC, NOx and photochemical oxidants, as well as relationships between increases in those pollutants and deterioration of air quality, are "poorly understood and cannot be determined with any reasonable degree of accuracy..." and that "the only practical approach for dealing with these pollutants appears to be to minimize emissions as much as possible." Id. at 1130-31.

\textsuperscript{68} For example, CO retards the flow of blood through the body and, in high concentrations, may have adverse effects upon persons suffering from cardiovascular diseases. HC and nitrogen oxides (NOx), the two other pollutants associated with the automobile, combine with each other and other chemicals in the atmosphere. When exposed to sunlight, they form photochemical oxidants which produce "smog." Studies conducted by the World Health Organization, the American Lung Association and the EPA have demonstrated a direct relation between higher levels of NOx and related photochemical oxidants, and the aggravation of and increase in serious respiratory diseases, eye irritation, and changes in heart and lung functions. See H.R. Rep. No. 294, 91st Cong., 1st Sess. \textit{reprinted in}[1977] U.S. Code Cong. & Adm. News, 2642-72 [hereinafter cited as H.R. REP. NO. 294]; ORE. TASK FORCE REPORT, supra note 49, at 6-12.

\textsuperscript{69} "Oregon's quality environment has fostered the substantial development of a tourist trade which infuses several economic sectors (hotel and motel, retail-wholesale, etc.) with large amounts of income." Economic Development Division, Portland Chamber of Commerce, Economic Base of the Portland, Oregon Standard Metropolitan Statistical Area 3 (n.d.).

\textsuperscript{70} Id. B. LUI, PORTLAND NO. 1—AMERICA'S MOST LIVEABLE CITY, 26-29 (pamphlet containing excerpts from MIDWEST RESEARCH INSTITUTE, QUALITY OF LIFE INDICATORS IN THE U.S. METROPOLITAN AREAS) (n.d.).

\textsuperscript{71} Oregon's DEQ has asserted that the concomitant maintenance and engine tuneups necessitated by inspection certification should improve vehicle fuel economy and result in cost savings to the motorist. EQC REPORT, supra note 41, app. K-3; DEQ SECOND ANNUAL ENERGY POLICY
Data compiled from an EPA study of I/M programs, now being conducted in Portland, should, among other things, clarify whether emission reduction and fuel economy improvements are both achieved by an I/M program. The asserted collateral benefits of fuel savings offered by the maintenance aspect of I/M may be used by otherwise reluctant legislators as one justification for their approval of I/M implementation.

Numerous studies have shown that an annual fleetwide decrease in fuel consumption in the range of 2-5% is an additional benefit associated with the implementation of I/M. In some cases, the money saved by the motorist due to increased fuel economy equals or exceeds the testing fee and the amount necessary to repair the failed vehicle.

A study by Sun Oil Company on a random sampling of privately owned cars, using a procedure of (1) visual inspection, (2) exhaust analysis for CO and HC, and (3) instrumental ("electronic") analysis, indicated an average fuel economy improvement of over 13% with "a simultaneous reduction in hydrocarbon and carbon monoxide emissions to levels consistently much lower than existing and proposed state inspection levels." Oberdorfer, Reducing Fuel Consumption and Emissions by an Optimizing Tuneup, in REPORT OF THE FOURTH NORTH AMERICAN MOTOR VEHICLE EMISSION CONTROL CONFERENCE 251, 252-65 (1975). Exxon Corporation reported fuel savings when engine malfunctions associated with high CO and HC are corrected. New Jersey Proposed Regulation Report, supra note 71, at 43. A study conducted by Champion Spark Plug Company indicates similar findings when cars are tuned according to manufacturers' specifications. Champion Spark Plug Co., Tune-Up: Its Effect on Fuel Economy, Emissions and Performance 3 (n.d.) (results of 1975-76 test program). For a recognition and discussion of the fuel economy benefits associated with state I/M programs, see H.R. REP. NO. 294, supra note 68, at 2209, 2453-60, 2493-94; Shult, Overview of Inspection/Maintenance (I/M), in REPORT OF THE FOURTH AMERICAN MOTOR VEHICLE EMISSION CONTROL CONFERENCE 101, 116 (1975).

Specifically, the data will be used to determine: (1) the types of engine maladjustments which cause a vehicle to fail a short test (idle test) used by the Portland I/M program; (2) how soon emissions from a repaired vehicle begin to increase; (3) the cost of an average repair; and (4) the effect of different engine maladjustments on emission levels and fuel economy. The study will also examine effects of field conditions such as "the skill of mechanics who service cars which fail, and the precision with which the short test is made on a high frequency basis, and will provide data to determine the optimum frequency of inspection." Id. at 2. Although the EPA will be testing until March, 1979, interim reports will be issued and can be obtained by writing U.S. EPA, Characterization and Applications Branch, 2565 Plymouth Road, Ann Arbor, Mich., 48105.
PRESENT CHOICES AVAILABLE TO A STATE IN TAILORING ITS I/M PROGRAM

Implementation of an I/M program at the state level provides the state with the opportunity to make choices in the scope and operation of its program. These choices include: the method of financing, the degree of state involvement in operating the program, the manner in which compliance is compelled, and whether certain vehicles should be exempt. The state must also decide whether to make the program statewide or restrict it to urban target areas within the state. Thus, within this framework of major decisions are opportunities for the state to tailor its program to its particular needs.

A. FINANCING THE PROGRAM

The threshold decision facing a state legislature is the method of financing the program. Oregon chose to appropriate startup funds for equipment and inspection facilities during the program’s voluntary phase and has since relied upon inspection fees to pay for the program. States not wishing to fund the program through inspection fees may choose other methods such as increasing gasoline taxes or imposing highway use tolls. Alternatively, the state may leave the funding decision to the voters through initiatives or referendums. In any case, a fundamental consideration will be whether the expense should be borne by citizens statewide or only by those living in the inspection area. A voluntary phase in an I/M program will give the state and local officials time to determine which method of financing will be most appropriate to sustain a mandatory program.

The EPA and some courts have shown indifference as to how a state will raise money necessary to fund various compelled transportation control measures. For example, in Friends of the Earth v. Carey, the Court did not address the issue of funding, but was, instead, satisfied that funding for New York City’s TCP would be made available by the state.74 The Court expressed little concern regarding the effect on other state programs by diversion of monies necessitated by the Court’s decision.75 Because an I/M program involves relatively little initial expense to the state and can be

74. [W]hile the State and City have . . . expressed reservations about their capability of financing the costs of implementation and we are well aware of the current fiscal crisis in which the City finds itself . . . the chief executives of the State and City have indicated that while financing of the Plan would pose problems in policy choices concerning the allocation of resources, they would take the necessary steps to obtain the financial support required. Friends of the Earth v. Carey, 552 F.2d 25, 39 n.7 (2d Cir. 1977).

75. The City’s claim of federal interference with its . . . budgetary policies, and with other services wholly within its control, is neither substantial nor directed toward an integral governmental function . . . . The necessity of appropriating funds for the construction of toll facilities (from which it will receive revenue) or for the acquisition of private garages under the business district parking reduction plan does not amount to the kind of injury found to be impermissible in National League of Cities . . . .

Id. at 38.
paid for by the motorist, compelled implementation of an I/M program probably would not seriously impair state finances. In any event, if a state selects an I/M program as part of its TCP, the decisions concerning the method of funding should be made by state and local officials at or prior to that state’s implementation rather than allowing the EPA or a federal court to ultimately decide the matter.

B. The Degree of State Involvement in Vehicle Inspection

Oregon has chosen total state control of inspection, with the exception of allowing state agencies and certain qualified businesses to perform self-inspection. Arizona, on the other hand, has contracted with a private testing firm to conduct inspections through a network of inspection facilities constructed, owned, and operated by the private contractor under state supervision.76 Aside from the private nature of the inspector, a privately contracted inspection program and a state-conducted inspection program can be substantially identical.77

One advantage of private contracting is that it takes the state out of inspection activity and replaces it with private industry, thus preventing increases in bureaucracy while increasing employment in the private sector.78 Another advantage is that it need not require initial capital outlay by the state.79 The main disadvantage is that, if the contract is of long duration and the terms of the contract allow little leeway to the state to modify the basic provisions of the program as state needs or EPA mandates require,80 then the state may not be able to institute needed changes without considerable financial loss.81

77. See, e.g., id. at 332 (I/M is linked to registration; provision for fleet self-inspection; certificate fee of $5 charged.).
78. EQC REPORT, supra note 41, app. 0-2. The Oregon EQC recommended a private contractor approach, especially if the program were converted to annual inspection. Id. at 5. Aware of the benefits of a privately contracted I/M program, the Oregon Legislature has directed the EQC to conduct a cost-effectiveness study to determine if a private contract approach would be appropriate for Oregon, and to contract with private firms “[u]pon finding that savings to the public and increased efficiency would result and the quality of the program would be adequately maintained...” OR. REV. STAT. § 468.377 (1977).
79. EQC REPORT, supra note 41, app. 0-2.
80. Although a state may delegate by contract some of its governmental functions, its police power remains inalienable. Any contract entered into by the state is subject to the state’s police power, which transcends contract requirements when the state must respond, changing safety or health policies. See, e.g., Morris v. City of Salem, 179 Or. 666, 174 P.2d 192 (1946) (Municipality’s contract for installation and operation of parking meters did not deprive city council of right to remove meters in exercise of its inalienable police power, if deemed conducive to public safety or welfare.)
81. When a state, through legislative repeal, seeks to impair an existing contractual obliga-
Rather than utilize either of the above approaches, a state may choose to rely on existing private garages to perform the inspections. Inspection by private garages will require state certification or licensing of mechanics, to assure competency, and state certification of facilities, to assure use of proper equipment. 82

The advantages of private garage inspection are the convenience to the public and the fact that no capital outlay will be required by the state. 83 However, there is a greater possibility of abuse by both motorists and mechanics, prevention of which may require a state regulatory bureaucracy. 84 Another disadvantage is that, in requiring proper inspection equipment at facilities, the state may give competitive advantage to those garages which can afford that equipment. Furthermore, state certification may be viewed as a first step to general state licensing of private mechanics as inspectors and, therefore, might generate a great deal of automotive industry hostility. 85

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82. E.g., 1977 Colo. Sess. Laws, ch. 564, § 3, at 1902-05 (to be codified at Colo. Rev. Stat. §§ 42-4-307(III)(3), 42-4-310) gives the Air Pollution Control Commission broad responsibility to adopt rules and regulations concerning licensing of private emission inspection stations and certification of their equipment, as well as licensing of private or state employed emission inspectors.

83. But note, Arizona considered the private garage approach and rejected it because of the high capital investment required of the private garages. Iacobelli, MVECC IV, supra note 76, at 332.

84. For example, if there is an independent state supervised check on the quality of repair, then abuse by mechanics is reduced, as was experienced in New Jersey. EQC Report, supra note 41, at app. 1-10. Colorado provides for a referee emissions inspection program to protect the consumer. 1977 Colo. Sess. Laws, ch. 564, § 3, at 1903 (to be codified at Colo. Rev. Stat. § 42-4-309(4)). An Oregon Automobile Dealers Association (OADA) survey indicated that over 80% of their members responding stated that their mechanics believed that "a vehicle set to DEQ standards does not get as good gas mileage and does not run or idle as well as it did before being adjusted to meet the test." ORE. TASK FORCE REPORT, supra note 49, at 14. This belief is shared by many motorists, who readjust their engines after passing the inspection. Id. at 15. These attitudes are misguided because DEQ inspection standards are based on the manufacturers' specifications. As the standards, and benefits of the program, become widely known, these public and service industry misconceptions will become less prevalent. However, given initial public hostility coupled with misinformed mechanics, the need for a state regulatory agency to closely supervise private inspection is apparent.

85. In view of this possibility, the proposal for licensing mechanics as qualified emissions inspectors should be entirely voluntary. For example, Colorado provides for voluntary training programs for mechanics at educational facilities, "oriented toward basic motor vehicle air pollution control systems installed in motor vehicles by the manufacturers." 1977 Colo. Sess. Laws, ch. 564, § 10, at 1911-12 (to be codified at Colo. Rev. Stat. § 25-7-128(2)). Presumably, these educational programs will make clear to automotive mechanics that increasing competence in, and understanding of, correct automotive servicing results in lower emission levels, better fuel economy, and more business for the automotive service industry.
Because local legislators will doubtless be sensitive to the attitude of the service industry to certification requirements necessitated by private garage inspection, they should decide which approach or combination of approaches will produce the most effective result in their state.

C. INCORPORATING I/M INTO EXISTING STATE REGISTRATION REQUIREMENTS

Oregon requires biennial inspection for most vehicles because this approach coincides with Oregon's biennial registration system. This approach produces the desired incentive to comply, since the motorist whose vehicle fails the inspection cannot register his vehicle and will face criminal penalties if he operates that unregistered vehicle on the public highways.\textsuperscript{86} After initial registration, vehicles are required to be re-registered at two-year intervals, commencing two years from the month of initial registration.\textsuperscript{87} This registration produces a "staggered" effect and thus evens out the administrative workload both for licensing personnel and DEQ inspectors. For ease of administration, states whose vehicle registrations fall due at one time should consider appropriate legislative changes to produce a staggered effect.

Nevertheless, Oregon has experienced two drawbacks with its biennial registration system. First, more registrations fall due in even years than in odd years.\textsuperscript{88} A greater number of daily ambient air violations occurred in 1977 because fewer vehicle re-registrations fell due that year.\textsuperscript{89} Secondly, because available data suggest that the benefits of an I/M inspection deteriorate rapidly,\textsuperscript{90} air quality would be improved with more frequent inspection. In this regard, one purpose of the EPA study\textsuperscript{91} is to determine the optimum frequency of inspection. Data gathered by this study is likely to confirm the EPA's contention that inspection should be made at least every

\begin{footnotes}
\footnote{86. Or. Rev. Stat. § 481.105(4)(a) (1977) requires an applicant for auto registration to give his true address. \textit{Id.} § 481.105 allows denial or cancellation by the Motor Vehicles Division of registration or certificate of title for falsification. \textit{Id.} § 481.990(9) prohibits false swearing or certification of any MVD application. \textit{Id.} § 843.805 prohibits operation of a vehicle without a certificate of emissions compliance. \textit{Id.} § 483.820(1) prohibits falsification of the certificate of compliance. \textit{Id.} § 483.825 prohibits tampering with emission control systems. Such sanctions, when combined with major repair costs which the owner is unable to afford, create a hardship on the poor. States may choose to give appropriate rebates or other forms of assistance. Professor Stewart notes that imposition of environmental policy often results in sacrifices imposed upon the poor for the sake of the "elite's vision of a better society." Stewart, supra note 7, at 1221-22. \textsuperscript{87.} Or. Rev. Stat. § 481.135 (1977).}

\footnote{88. EOC Report, supra note 41, app. C-3. All existing vehicles were required to be registered for the first time on a biennial basis in 1974 and thus were not required to be re-registered until 1976. The only vehicles registered in 1975 were new vehicles and vehicles registered in Oregon for the first time.}

\footnote{89. This was predicted by the EOC. \textit{Id.} at app. G-3. In 1977, 33 violations occurred as opposed to 27 violations in 1976. See note 65 supra.}

\footnote{90. EOC Report, supra note 41, at app. I-10 to 17.}

\footnote{91. See note 73 supra.}
\end{footnotes}
D. REASONS FOR EXEMPTING CERTAIN VEHICLES

The major reason states should consider exempting certain vehicles from inspection is that exemptions serve to minimize waste of funds and facilities upon those vehicles for which inspection is cost effective. The basis for granting exemptions to certain classes of vehicles should be examined and Oregon's program serves to illustrate.

There are certain vehicles for which inspection costs, either to the state or to the vehicle owner, would greatly outweigh the pollution reduction benefits gained from those inspections. In Oregon, heavy construction (''fixed load'') vehicles and vehicles licensed as farm equipment are exempt for this reason. A state may also find it desirable to exempt vehicles which are few in number, such as antique vehicles, or for which standards would be difficult to set, such as motorcycles and heavy duty diesel motor vehicles. These particular classes of vehicles are exempt in Oregon for these reasons. But this would be ill-considered in light of predictable public hostility. Recent Oregon legislation requires that those vehicles owned and operated by the state and its political subdivisions, previously exempt from inspection, undergo annual I/M inspection.

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92. EOC REPORT, supra note 41, at app. I-17.
93. OR. REV. STAT. § 481.190(3)(c), (e) (1977). Fixed load vehicles include asphalt spreaders, earth moving equipment, road graders and special construction equipment. Id. § 481.272(2), (3).
94. OR. REV. STAT. § 481.190(3)(b), (d) (1977). These subsections exempt vehicles manufactured prior to 1942 and special interest vehicles (maintained as collectors' items). Administrative emission test criteria established on May 25, 1975, provided no emission standards for vehicles exceeding a combined manufacture weight and maximum load of 8,400 pounds. OR. AD. RULES § 340-24-305(17). Electric vehicles were presumed to comply. OR. AD. RULES § 340-24-320(7). Motorcycles were unregulated due to the absence of motorcycle emission control requirements and reliable testing techniques. DEQ, Memorandum of Vehicle Inspection Program 2 (Feb. 10, 1977) (Accompanying proposed rules relating to standards for gasoline powered heavy duty vehicles). New emission control standards have been developed for heavy duty gasoline motor vehicles in excess of 8,500 pounds. OR. AD. RULES § 340-24-305(16), 340-24-315, 340-24-325, 340-24-335 (July 1, 1977). However, heavy duty diesel motor vehicles are still administratively exempt from testing. See note 119 infra.
95. OR. REV. STAT. § 481.190 (1977). Government owned vehicles are required to be registered only once. Id. § 481.125. The DEQ plans on an annual notification procedure for each agency with follow-up surveillance in conjunction with the Motor Vehicles Division. Memo to EQC, Authorization for Public Hearing to Consider Amending Vehicle Emission Testing Rules to Cover the Testing of Publicly Owned Vehicles (EQC Agenda Item No. L, Nov. 18, 1977). Objections to the proposed rule changes were voiced at hearings on Jan. 16, 1978, by fire agencies, citing high engine restyle costs and length of "down time" necessary to inspect emergency vehicles. School district personnel voiced similar objections, and suggestions were made to amend the definition of fleets (100 or more vehicles) to allow smaller agencies to self-inspect. Oregon Journal, Jan. 17, 1978, at 3, col. 3.
A major decision facing states desiring to implement a comprehensive I/M program is whether or not to exempt certain heavy duty vehicles engaged in interstate commerce. Present licensing arrangement for such vehicles afford a trucking company a great deal of flexibility in locating and relocating its home state ("base plate") truck registrations. For this and other reasons, Oregon, for the moment, has chosen to exempt such vehicles from I/M certification requirements.

Finally, states must exempt from inspection new motor vehicles because the Federal Clean Air Act specifically prohibits state inspection of new motor vehicles prior to their initial sale, titling, or registration. Nevertheless, as a means of protecting its consumers, a state could conduct an I/M inspection for the limited purpose of determining whether or not a vehicle complies with manufacturers' emission warranties required by the Federal Clean Air Act. If the ultimate purchaser's new vehicle failed the

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96. Oregon's reciprocal proration of registration fees enabling legislation, OR. REV. STAT. § 481.620-730 (1977), defines three locations where a vehicle may be properly registered: (1) the jurisdiction where the person registering the vehicle legally resides; or (2) any jurisdiction where a commercial firm registers a commercial vehicle (operated for compensation), provided the vehicle is controlled or operated from that firm; or (3) any jurisdiction where, by agreement between two or more jurisdictions, the commercial vehicle is required to be registered by that jurisdiction. Id. § 481.620(8)(a),(b),(c). Base state ("base plate") is defined under the reciprocity agreement entered into by Oregon, as follows: "(a) in the case of a commercial vehicle the State from or in which the vehicle is most frequently dispatched, garaged, serviced, maintained, operated, or otherwise controlled, or also in the case of a fleet vehicle the State to which it is allocated for registration under statutory requirements." WESTERN HIGHWAY INST., UNIFORM VEHICLE REGISTRATION PRORATION AND RECIPROCITY AGREEMENT § 14(a) (rev. ed. 1974) [hereinafter cited as WESTERN UNIFORM COMPACT].

97. 1977 Or. Laws, ch. 787, § 2(f). One reason the Oregon Legislature may have excluded vehicles operating in interstate commerce from I/M requirements is the fact that complete authority for the registration of fleet vehicles operating under reciprocity agreements with neighboring states is contained in OR. REV. STAT. § 481.620-730 (1977) (specifically 481.730(1)), without any reference to motor vehicle I/M statutory requirements contained elsewhere in Oregon Revised Statutes. Prior to statutory exemption of commercial vehicles operating in interstate commerce, the DEQ had not formulated administrative regulations concerning these vehicles. Currently, the DEQ inspects all vehicles with a gross weight in excess of 8,000 pounds bearing a "T"-prefixed license plate and registered within the MSD. The DEQ does not inspect commercial vehicles bearing a "Y"-prefixed license plate because those vehicles are subject to interstate "apportionment" under reciprocity agreements. "T" indicates a vehicle whose license fee is not apportioned. "Y" indicates a vehicle whose license fee is apportioned among various states pursuant to a reciprocity agreement.

98. Section 209(a) of the Clean Air Act states:

No state or any political subdivision thereof shall adopt or attempt to enforce any standard relating to the control of emissions from new motor vehicles or new motor vehicle engines subject to this part. No State shall require certification, inspection, or any other approval relating to the control of emissions from any new motor vehicle or new motor vehicle engine as condition precedent to the initial retail sale, titling (if any) or registration of such motor vehicle, motor vehicle engine, or equipment. 42 U.S.C. § 7543(a) (1976) (emphasis added).

99. It provides for a warranty of a new motor vehicle emission device to the ultimate purchaser. It also provides for state testing after the date of sale to assure compliance with this warranty and provides that the manufacturer shall remedy any non-conformity within the specified warranty period. Id. § 7541(h)(2), (3). See H.R. REP. No. 294, supra note 68, at 2681.
inspection, a state would still be obligated to issue vehicle registration.\textsuperscript{100} The purchaser, however, could require repair of the emission device at the manufacturer’s expense.\textsuperscript{101}

A legislature may appropriately exempt the classes of vehicles enumerated above either to maintain the cost effectiveness of its I/M program or because it lacks authority to require inspections. However, state legislators should be aware that exemptions should be based upon sound legal or economic reasons in order to minimize the likelihood of EPA disapproval of a Transportation Control Plan.\textsuperscript{102}

**E. CHOOSE IN-STATE PROGRAM BOUNDARIES**

Another method available to state legislatures to conserve state funds and facilities, to minimize bureaucracy, and to optimize public cooperation without undermining air quality, is to target the program to geographic areas of demonstrable need. Target areas will necessarily be areas of dense population.\textsuperscript{103}

The boundaries should include not only urban but also suburban areas which generate a large amount of commuter traffic into and out of urban centers. If the lines are drawn too narrowly, the excluded suburban commuter traffic will render the program ineffective. If the lines are drawn too broadly, persons who contribute no pollution to the target area or indeed have no relationship at all to the urban center will be unfairly included. In establishing boundary lines for an I/M target area, the legislature should also be guided by the geography and wind patterns of the airshed area, as well as by population growth and relocation trends. Ultimately, the effectiveness of the program will be determined by the percentage of vehicles regularly driven in the target area which can be made subject to inspection.\textsuperscript{104}

Whether a target area approach or a statewide approach is chosen will, of course, vary from state to state. States which have dense population evenly distributed throughout much of the state, such as New Jersey, could justifiably consider their entire state as a target area.\textsuperscript{105} States in which

\textsuperscript{100} This interpretation that a state could not impose I/M testing as a precondition to registration or titling was voiced by Mr. Mike Scibinico, U.S. EPA, Mobile Source Division, at a "207(b) workshop" held on September 30, 1977, in Portland, Ore.

\textsuperscript{101} 42 U.S.C. § 7541(h)(1), (2) (1976).

\textsuperscript{102} In those states where the EPA has proposed its own I/M program, an exemption has been granted for only "classic or antique vehicles." See 40 C.F.R. §§ 52.242(c), .1089(c) (1977) (California and Maryland respectively).

\textsuperscript{103} H.R. Rep. No. 294, supra note 68, at 2436-37, lists twenty-nine metropolitan areas that are now subject to transportation control requirements.

\textsuperscript{104} Important considerations for the establishment of inspection within the MSD boundaries were vehicle registration distribution by county, and passenger car and truck traffic patterns in the Portland Region. EQC REPORT, supra note 41, at app. L.

\textsuperscript{105} See note 10 supra Elston, New Jersey’s Auto Emission Inspection program: An As-
population is concentrated in distinct areas, such as Oregon, should consider the target area approach.\footnote{106}

The decisions concerning the program boundaries should be made at the state rather than at the local level. State control over vehicle registration gives the state the capability to include areas which otherwise might not participate. For example, the Oregon Legislature may soon consider EQC recommendations to create new target areas in the downstate Salem, Eugene and Medford metropolitan areas because violations of primary ambient air standards are occurring with increasing frequency there.\footnote{107} Since Oregon’s I/M program is linked to statewide vehicle registration, the Legislature can very easily make vehicle owners in these three metropolitan areas subject to the precondition of I/M certification by merely redefining the inspection areas.

The flexibility offered by a target area approach linked to state vehicle registration should be attractive to those states which do not have evenly distributed population. For many of these states, the inspection of vehicles within their selected target areas should produce such a reduction in air pollution from motor vehicles that other, perhaps more extreme, transportation control measures will be unnecessary.\footnote{108}

\textbf{Capability of States to Inspect Out-of-State Commuter Traffic or Trucking Engaged in Interstate Commerce}

Even though an I/M program linked to vehicle registration can achieve substantial improvements in air quality, there exist “non-attainment” areas which, because of their location near interstate borders, would continue to experience difficulty achieving the desired air quality if the state were merely to require inspection of vehicles registered within that state.\footnote{109} A

\footnote{106} Arizona, Colorado, and Nevada also restrict their I/M programs to target area counties. See note 10 supra.

\footnote{107} EQC Report, supra note 41, at app. H. The problem of ambient CO violations is most serious in the Medford area. Oregon’s “non-attainment” area includes Portland, Salem, Eugene, and Medford. Letter from H.M. Patterson, Mgr., Air Pollution Control, to Mr. Schultz, EPA Region 10, Seattle, Wash. (March 6, 1978).

\footnote{108} For example, the estimated actual reduction of CO from the I/M component of Oregon’s TCP was 14%, while that from traffic flow improvements was 22%, during the period 1970-1976. Estimated actual reduction of HC for the same period for Multnomah County was 7% for the I/M component and 8% for all other components. See EQC Report, supra note 41, app. G-2, G-6. Other measures more burdensome to both the motorist and to the state, might include gas rationing, retrofit programs and large scale relocation of downtown parking facilities.

\footnote{109} Portland, as evidenced by its thirty-three violations occurring in 1977, continues to experience difficulty in attaining acceptable air quality standards despite implementation of its I/M program and other transportation control measures. Its location on the Oregon-Washington border, placing it at a cross-road of north-south interstate traffic and east-west interstate and intrastate...
state enactment requiring inspection of vehicles registered outside the jurisdiction of that state presents legal and political problems wholly separate and apart from considerations involving the scope of an I/M program within a state.

A. Negotiations Among the States to Achieve Cooperative State Action

A state may find that a TCP developed for metropolitan areas in that state is compromised because of unregulated vehicular traffic from urban areas outside that state’s jurisdiction. The Oregon EQC has estimated that Oregon’s I/M program as it exists is reduced to 90% of its full effectiveness by pollution from unregulated traffic.\(^{110}\) One area which generates a great amount of unregulated traffic and thus contributes a major portion of vehicular air pollution in Portland is Clark County, Washington, which includes the city of Vancouver.\(^{111}\)

If the problem can be so narrowed to an identifiable out-of-state area, such as Vancouver, Washington, then the first step that a “suffering” state should consider is discussion between its representatives and representatives of the “offending” state. Such discussions, encouraged by the Federal Clean Air Act,\(^{112}\) can be useful to the involved states as a forum for traffic, thus limits the effectiveness of its current program, which can reach only vehicles owned by MSD residents.

\(^{110}\) EQC Report, supra note 41, at 3 and app. L.

\(^{111}\) Of a total of 181,450 average daily traffic counts (ADT) made of traffic coming into and going out of the MSD for all roads, Clark County, Wash., accounts for 25.2% of the ADT through the MSD. Id. at app. L-7 to L-10.

In 1977 we estimate there were 192,000 (approximately) people employed in the city; of this total 103,000 live in Portland and the remainder in the four-county area, including Clark County, Washington. Since 97% of all commuter traffic from Clark County is auto traffic, we conclude that this is having an impact on the quality of the Portland Airshed. . . .

[T]he City of Portland requests that the [EQC] direct the [DEQ] to undertake a study. . . . We would hope that a possible outcome of this work would be the expansion of the inspection program to include all vehicles registered in Clark County. . . .


\(^{112}\) Prior to the 1977 Amendments, an interstate conference procedure was provided for under 42 U.S.C. § 1857d (1970). This procedure was repealed by section 114 of the 1977 Amendments, 42 U.S.C. § 7415 (1976). The Administrator is now authorized to encourage cooperative activities by states and local governments to enact improved and, “so far as practicable in the light of varying conditions and needs, uniform state and local laws relating to the prevention and control of air pollution; and encourage the making of agreements and compacts between States. . . .” Id. § 7402(a). Cooperative interstate planning among the governors and local elected officials with respect to the revision of implementation plans is encouraged in those areas of non-attainment where national primary ambient air quality standards for CO or photochemical oxidants will not be attained by July, 1979. Id. § 7504.
aerialing disputes, identifying current areas of agreement and disagreement, and exploring ways of resolving existing conflicts. Where agreements are reached by states sharing an air quality control region, interstate compacts, subject to congressional approval, may be entered into by the states sharing that designated air quality control region.\(^{113}\)

The opportunity for self-determination, and the possibility of federal regulation of local private transportation if such self-determination is not exercised, are selling points which can be raised by a state attempting to obtain the cooperation of an "offending" state. Moreover, I/M programs are inexpensive, are fairly easy to incorporate into existing motor vehicle statutes, and achieve immediate, significant results with little interference with private transportation.

If these arguments fail to persuade a neighboring state to implement I/M, the state or the affected metropolitan area might suggest that it will consider judicious use of its taxing power to complement that state's TCP. The "suffering" state or municipality could threaten to impose a tax, levied on out-of-state employees commuting to work in that state's affected area, and justify such a tax as a return to the state for the costs of controlling the pollution which those commuters' vehicles create.\(^{114}\) Whether or not such

\(^{113}\) 42 U.S.C. § 7402(c) (1976). Air quality control regions are defined in id. § 7407(b), (c), and may include interstate "non-attainment" areas as determined by the Administrator. Id. § 7501(2).

\(^{114}\) The validity of a so-called commuter tax has been upheld in American Commuters Ass'n v. Levitt, 405 F.2d 1148 (2d Cir. 1969) (New York City income tax of 1% levied on persons living outside the City who earned all or substantially all of their income in New York City). See also, Non-Resident Taxpayers v. Philadelphia, 341 F. Supp. 1139 (D.N.J. 1971), aff'd 406 U.S. 951 (1972). Cf. Austin v. New Hampshire, 420 U.S. 656 (1975), where the Supreme Court invalidated a 4% tax on all amounts earned by non-residents in New Hampshire because no similar tax was imposed on New Hampshire residents and the tax was therefore violative of the Privileges and Immunities Clause of Art. IV, § 2, of the U.S. Constitution.

If a tax similar to the one described is challenged as violative of Privileges and Immunities or Equal Protection principles, a court would have to balance the degree of interference with the asserted constitutionally or federally protected right (clean air), as opposed to the perceived interference with the same and other rights when considering possible legislative alternatives (enlarging suffering state's I/M target area; more frequent inspection) to achieve the same end. See generally, Austin v. New Hampshire, 420 U.S. 656 (1975); San Antonio Independent School District v. Rodriguez, 411 U.S. 1 (1973).

A proposed tax could be waived upon a showing by the working commuter that his vehicle has passed the taxing jurisdiction's I/M inspection. The tax should be large enough to prompt substantial compliance with inspection. If the tax is so small that it would be easier to pay it than to pass an inspection, the tax will be ineffectual. If it is so large that it in essence amounts to unreasonable discrimination against non-resident employees, then such a tax would not be upheld as a valid air pollution control measure. Austin v. New Hampshire. Assuming a proper tax is achieved, that tax should likewise be applied to all in-state commuters whose vehicles are registered outside the program's boundaries. Exemptions should be given to those working commuters who do not use their own automobiles to commute to work.
a tax is eventually enacted by a "suffering" state, the threat of such a tax could be used as a bargaining point in interstate negotiations.

Lastly, the "suffering" state could threaten to seek EPA intervention.\textsuperscript{115} While such intervention, or threat of intervention, would undoubtedly put pressure upon the "offending" state, the "suffering" state should be cognizant of risks involved in EPA intervention.\textsuperscript{116} In short, the EPA Administrator or, for that matter, a federal court, would be reluctant to intervene on behalf of a "suffering" state if the problem could more easily be solved by an appropriate change in that state's own TCP.

Local taxing measures or other legislation with extra-territorial legal effect, as well as EPA or judicial intervention, will not have to be resorted to if the states involved act responsibly through cooperative efforts to solve their shared mobile air pollution problems.

\textbf{B. Inspection of Heavy Duty Trucking: A Responsibility That Should Be Shared}

States in which mobile source air pollution problems cannot be identified with one or more out-of-state areas should consider the possibility of inspecting vehicles as they enter the jurisdiction. However, air pollution legislation designed to reach all out-of-state vehicles, including private passenger cars, would probably result in intolerable cost burdens on everyone.\textsuperscript{117}

\begin{footnotesize}
\begin{itemize}
\item \textsuperscript{115} See, e.g., 42 U.S.C. § 7413(a)(2) (1976).
\item \textsuperscript{116} Bargaining among states to minimize the losses occasioned by such spillovers is costly . . . and may do little to improve the lot of states in a weak position (such as those in a downwind or downstream location). These states are likely to favor federal intervention to eliminate the more damaging forms of spillover. If spillover losses are sufficiently significant and multidirectional then all states may gain (to a greater or lesser degree) from centralized determination of environmental policies.
\item \textsuperscript{117} Stewart, supra note 7, at 1216.
\item \textsuperscript{116} While a forced revision of both the "offending" and "suffering" states' implementation plans could conceivably result, either one or both states would, in any event, be required to submit a plan revision if they have "non-attainment areas." Revised plans must include evidence that state and local governments "have adopted by statute, regulation, ordinance . . . the necessary requirements and schedules and timetables for compliance, and are committed to implement and enforce the appropriate elements of the plan . . . ." 42 U.S.C. § 7502(b) (1976). Even if the EPA's enforcement of such a requirement is viewed by the Supreme Court as an unconstitutional coercive intrusion into a state's integral functions, under the tests set forth in National League of Cities v. Usery, 426 U.S. 833 (1976), a citizen lawsuit to compel a state to enact such laws or regulations might be distinguishable. In an action brought under the citizen suit provision, the court in Friends of the Earth v. Carey, 552 F.2d 25 (2d Cir. 1977), concluded that the city had waived a possible constitutional claim because of local and state participation in promulgating the plan, and held the plan enforceable against the state. Hence, the effect of private citizen lawsuits to force a revision of a "suffering" state's plan accomplishes the same result as direct EPA intervention without weakening the accountability of federal officials. See also, Stewart, supra note 7, at 1241.
\item \textsuperscript{117} For example, \textit{Oregon State Highway Div., Official Pub. No. 77-1, Traffic Volume Tables} (1977) [hereinafter cited as \textit{Traffic Volume Tables}] show an average daily traffic count for 1976 of 93,644 (both directions) at the interstate bridge on Interstate 5, separating Portland from Vancouver. Approximately 43.9\% of the passenger cars were out-of-state vehicles. A court might
\end{itemize}
\end{footnotesize}
including the state seeking to enforce such a law, and might constitute an infringement on the right of private persons to freely travel from state to state.\textsuperscript{118} This is especially true if neighboring states do in fact implement I/M and, therefore, inspection of passenger vehicles entering the jurisdiction becomes duplicative, uneconomical and unproductive.

However, an unregulated heavy duty gasoline truck can emit as much hydrocarbon as eighteen automobiles and as much carbon monoxide as forty-five automobiles.\textsuperscript{119} Also, states have traditionally had greater freedom to regulate heavy duty vehicles.\textsuperscript{120} Moreover, state facilities already exist for the purpose of inspecting such vehicles.\textsuperscript{121} Therefore, it might be appropriate to initially limit inspection to heavy duty trucks engaged in interstate commerce.

Interstate reciprocity compacts afford, among other things, great flexibility to trucking firms to determine the states where they will base-plate actual registration of any of their trucks.\textsuperscript{122} Therefore, linking emission inspection to the actual registration requirements for such vehicles would be unproductive.\textsuperscript{123} Because interstate trucking agreements such as the Western Regional Compact deal exclusively with registration reciprocity as well as prorated or apportioned license and registration fees,\textsuperscript{124} these agreements leave the contracting states free to determine such matters as weight limitations, safety requirements,\textsuperscript{125} or perhaps pollution emission standards.

\textsuperscript{119} H.R. REP. No. 294, supra note 68, at 2481. Heavy duty diesel engines emit relatively low levels of HC and CO. Id. at n.4. Because of this fact, a state might consider directing its initial CO and HC inspection efforts at heavy duty gasoline powered vehicles only.
\textsuperscript{120} Cf. South Carolina State Highway Dep't v. Barnwell Bros., Inc., 303 U.S. 177, 185-89 (1939) (holding that local regulatory matters which also affected interstate commerce to some degree may be upheld in the absence of congressional action if they are a rational means of dealing with the problem, do not impose too great a burden on interstate commerce and do not discriminate against interstate commerce).
\textsuperscript{121} For example, states such as Oregon have enacted vehicle weight and size limitations and methods of enforcement at weigh stations. OR. REV. STAT. § 483.502-.545(1977).
\textsuperscript{122} See note 96 supra.
\textsuperscript{123} Id.
\textsuperscript{124} WESTERN UNIFORM COMPACT, supra note 96, § 34. Section 34 concerns Statutory Vehicle Regulations. It provides that "[t]his agreement [the compact] shall not authorize the operation of a vehicle in any contracting State contrary to the laws or regulations thereof, except those pertaining to registration and payment of fees; and with respect to such laws or regulations, only to the extent provided in this agreement."
\textsuperscript{125} Oregon and other states have qualifications in addition to vehicle registration which must be met. For example, in Oregon all carriers, interstate and intrastate, must obtain operating authority from the Oregon Public Utility Commission (PUC). OR. REV. STAT. §§ 767.105, .145, .150, .155 (1977). A fuel permit must be obtained from the Motor Vehicles Division on any diesel...
ard.

Because of potential conflicts with these interstate reciprocity agreements, as well as with the Federal Commerce Clause, legislation to inspect interstate heavy duty trucking should be carefully drafted. It must be designed to control only those areas of traditional concern to that state which are not otherwise regulated by a valid federal statute and which do not infringe on rights of private citizens from other states. Whether local I/M legislation regulating out-of-state heavy duty commercial trucking would violate the Commerce Clause depends upon: (1) whether the law achieves its stated purpose; (2) whether the effects of the law discriminate against interstate commerce; and (3) whether the interference with interstate commerce is minimal or substantial, considering the ends to be achieved and the alternative means available to achieve those ends.

State legislation would most likely meet the first test if it could be demonstrated that environmental as well as purported energy benefits were being achieved from the inspections. Secondly, the legislation should be totally non-discriminatory. The legislation should require the same frequency of inspection for interstate trucks as it requires for those trucks operating solely within that state’s jurisdiction. The classifications of vehicles subject to inspection, the criteria for certification, and the certification fees should be uniform for all commercial vehicles whether their operation is interstate or intrastate.

126. 42 U.S.C. § 7416 (1976); Washington v. General Motors Corp., 406 U.S. 109, 115 n.4 (1972) (“[s]tates also retain broad residual power over used motor vehicles.”). See also Huron Portland Cement Co. v. City of Detroit, 362 U.S. 440, 442 (1960) (“Legislation designed to free from pollution the very air that people breathe clearly falls within the exercise of even the most traditional concept of what is com pendiously known as the police power.”)

127. See, e.g., Pike v. Bruce Church, Inc., 397 U.S. 137, 142 (1970) (“Where the statute regulates evenhandedly to effectuate a legitimate local public interest, and its effects on interstate commerce are only incidental, it will be upheld unless the burden imposed on such commerce is clearly excessive in relation to the putative local benefits. . . . If a legitimate local purpose is found, then the question becomes one of degree.”) See also, note 120 supra. But cf. Bibb v. Navaho Freight Lines, Inc., 359 U.S. 520 (1959) (statute requiring contour mud guards in conflict with similar statutes of 45 other states held to impose undue burden on interstate commerce due to impediment on trucks entering Illinois from those other states.)

128. See note 125 supra.

129. See, e.g., South Carolina State Highway Dep’t v. Barnwell Bros., Inc., 303 U.S. 177 (1939); note 114 supra (regarding a balancing test).

130. Adequate study of the extent to which the I/M program is reduced in effectiveness by out-of-state heavy duty vehicles should form the basis for legislative findings stating that environmental, as well as energy, benefits would likely be achieved by the legislation. Major urban commercial centers such as New York City, Chicago and Cincinnati might find much more significant increases in their programs’ efficiency if such legislation were enacted.

131. For example, Oregon requires carriers, both interstate and intrastate, to obtain a permit

powered vehicle not subject to the Oregon PUC weight mile tax. Id. § 319.510-880. A permit must be secured from the Oregon Highway Division for any vehicle in excess of maximum legal weight and size. Id. § 483.528.

HeinOnline -- 10 Transp. L.J. 147 1978
on commerce. To this end, a trucker whose vehicle fails the inspection
might be issued a temporary pollution permit, valid for a limited time, to
enable him to complete his business on that particular trip into the jurisdic-
tion. Temporary permit fees can be greater than the actual cost to the state
of inspection, in order to compensate the state for the excess pollution
and also to encourage compliance.\textsuperscript{132} Heavy duty trucking subject to certification
requirements of other jurisdictions which are as strict or stricter than the
requirements of the inspecting state should also be exempt.\textsuperscript{133} Also, all
new trucks inspected under the Federal New Motor Vehicle Program should
be exempt until such time as their operation on the highways warrants in-
spection.\textsuperscript{134}

To further minimize burdens on interstate commerce while minimizing
administrative costs to the state, inspections should be combined with other
required inspections for heavy duty trucks at "points of entry" into the jurisdic-
tion.\textsuperscript{135} To avoid a duplication of inspections and a multiplication of in-
spection points, a program of I/M inspection in industrial states for heavy
duty interstate trucks should be made statewide. A state such as Oregon,
whose target area represents a small portion of its total area, might find
such a statewide inspection program inappropriate because it would be in-
specting many trucks which never travel into or out of the target area. As an
alternative, a state in this situation might confine inspection to those trucks
which regularly travel to or through the target area. Pursuant to present reciprocity agreements, states have enacted laws requiring truck operators to

\begin{itemize}
  \item for operating authority. See note 125 supra. Oregon could compel all such vehicles to submit to a
    uniform I/M inspection for each type of vehicle as a precondition to the granting of operating per-
    mits and empower the PUC to suspend or revoke permits when the owner repeatedly fails to obtain
    the uniform periodic inspection certification required. Certification fees should be levied uniformly
    for all types of vehicles, operating both interstate and intrastate.

  \item 132. Uniform permit fees for vehicles failing the inspection should be used to offset the cost
    to the state of the extra manpower and equipment needed to conduct the inspections and the
    administration of the program. Those trucks passing the inspection should be issued stickers valid
    for the inspection period so they will not be required to be retested until the sticker expires. A state
    might also choose to waive the inspection requirement upon payment of the permit fee. For in-
    stance, a state could charge $5 per inspection, whether or not the vehicle passes or fails. It could
    issue a temporary pollution permit for $2.50 and waive the inspection. This provision will reduce
    the actual number of inspections and save time to the trucker. This system would encourage those
    who make frequent trips into a target area to comply, while not being an undue burden on those
    who infrequently enter the target area.

  \item 133. See, e.g., Dean Milk Co. v. City of Madison, 340 U.S. 349 (1951) (an ordinance require-
    ing dairy inspection to be conducted within 25 miles of the city was disapproved, where the city
    could rely on certification by inspectors outside that area).

  \item 134. See 42 U.S.C. § 7521 (1976). It is not clear when a new motor vehicle ceases to be a "new
    motor vehicle." See id. §§ 7541(n)(3), 7543(a), (d). For this reason, and because of the
    presumed effectiveness of EPA factory imposed emission inspections, a state should exempt a
    new, heavy duty motor vehicle from its initial inspection requirement.

  \item 135. See Or. Ad. Rules, ch. 860, sub. 5 (rules relating to motor carriers).
\end{itemize}
file periodic reports showing pro-rated mileage traveled in each state.\textsuperscript{136} Oregon could therefore require I/M inspection for those trucks which travel an established percentage of miles in Oregon and offer an exemption to those truck operators who can demonstrate that their vehicles do not operate in the target area on a regular basis.\textsuperscript{137}

While it is legally possible for states to inspect certain classifications of vehicles operating in interstate commerce, state officials should be aware of the potential economic consequences stemming from such inspection.\textsuperscript{138} Some trucking concerns may avoid the target areas or inspecting jurisdictions to eliminate the possibility of inspection and potential fines. Should this occur, complying trucking firms within and outside of the inspecting jurisdiction may grow or increase in number to meet the demand for the transportation of goods into the inspecting jurisdiction. Such relocations of commerce would have greater disadvantageous impact on some jurisdictions than in others. In those jurisdictions where the impact is likely to be severe, it can be expected that state officials will be quite reluctant to impose emission inspection of interstate trucking because of the political repercussions they will face, not only from their constituents but from trucking lobbies.\textsuperscript{139}

Assuming, however, that legislation is enacted, it must be determined where the inspection will take place and who will do the inspecting. Considering the heavy volume of truck traffic in many locations, any inspection of interstate trucking at "points of entry" will necessarily be random, because of constraints on the state's budget and manpower.\textsuperscript{140} Granting exemp-

\textsuperscript{136} In Oregon, annual prorate applications must be filed with the Proration and Reciprocity Section of the Motor Vehicles Division. OR. REV. STAT. § 481.645 (1977); OREGON MOTOR VEHICLES DIVISION DEP'T OF TRANSPORTATION, PROPORTIONAL REGISTRATION INSTRUCTIONS, UNIFORM VEHICLE REGISTRATION AND RECIPROCITY AGREEMENT (1978).

\textsuperscript{137} Such a percentage could be determined either upon the history of the fleet or, for a new carrier, upon areas in which that firm intends to operate. For large fleets, basing the percentage on total fleet miles may be inappropriate. See WESTERN UNIFORM COMPACT, supra note 96, at §§ 50, 52. A large fleet may escape inspection because fleet miles in other states greatly exceed fleet miles within the inspecting jurisdiction, even though in-state fleet miles may be substantial. For this reason, inspection should be on a truck-by-truck basis.

\textsuperscript{138} With regard to possible economic impact to the inspecting state, opinion has been expressed in Oregon that an I/M requirement for interstate commercial vehicles subject to reciprocity agreements might result in retaliation by sister states in the form of abrogation of existing reciprocity agreements with a resulting loss of revenue to the state. Memorandum from Director of DEQ to EOC, Vehicle Emission Testing Rule—Authorization for Public Hearings to Consider Amending Vehicle Emission Testing Rules to Include Gasoline Powered Heavy Duty Vehicles, attachment A (Feb. 10, 1977).

\textsuperscript{139} The assertion has been made that "[t]hese already weak state agencies are exposed to intensive pressure from politicians, industry, unions, and citizens reacting to the costs (economic and otherwise) of controlling pollution and the possibility of unemployment and curtailment of economic development." Stewart, supra note 7, at 1201.

\textsuperscript{140} Of the average of 93,844 vehicles computed by average daily traffic counts at the
tions to those trucks which have complied with inspection requirements of other jurisdictions will reduce the number of vehicles subject to inspection. A jurisdiction could also provide out-of-state trucking firms an exemption based upon proof of self-inspection if that firm is based in a state having no inspection requirements. But any out-of-state compliance measure would be difficult for the inspecting state to enforce, other than through random inspection of out-of-state trucks.

In addition to the difficulties faced by the inspecting state, hardships may be experienced by truckers who are confronted with dissimilar standards and tests adopted by the various states in which they operate.\textsuperscript{141} Moreover, such standards may create a burden on interstate commerce which could outweigh the benefits to be gained from such inspections.\textsuperscript{142}

Because of the possible political repercussions, the practical constraints facing states desiring to inspect interstate trucking, and the possibility of dissimilar state inspection laws, the inspection of interstate commercial trucking is perhaps an issue which should be addressed by Congress. Congress should act at least to the extent of requiring the EPA Administrator to set uniform inspection standards for each and every make and model of in-use heavy duty vehicle engaged in interstate commerce. At the same time, Congress should authorize the EPA Administrator to prescribe a uniform emission test that can be used by states which choose to inspect such vehicles. Congress could go a step further and allow trucking firms to self-inspect their fleets, utilizing the uniform standards and the uniform test developed by the EPA. Such a program of fleet self-inspection could be supervised by either the EPA or the Department of Transportation. Congress might provide that certification by either of these agencies would exempt any fleet vehicle from any state emission inspection. The net result of such a program, if successful, would greatly reduce the number of inspections that a state wishing to inspect heavy duty commercial trucking would have to conduct.

Such federal decision-making would relieve the political pressure which state and local legislators will experience when and if their states consider the inspection of heavy duty interstate trucking. Federal decision-making would also do much to remove the incentive for trucking firms to

\footnotesize{Portland-Vancouver interstate bridge (both directions), 7.3% of the total were heavy duty trucks. See TRAFFIC VOLUME TABLES, supra note 117.}

\textsuperscript{141} For example, different jurisdictions might employ a short cycle idle emission test such as a Clayton Key Mode Test, or a 2,500 rpm test, or the Federal 3-Mode Test. For a description of the various short test procedures and varying results obtained, see Dekany, Development of a Short Test for Section 207(b)—A Status Report, in REPORT OF THE FOURTH NORTH AMERICAN MOTOR VEHICLE EMISSION CONTROL CONFERENCE 146 (1975).

relocate their operations to pollution havens or to avoid entry into areas which require inspection.

CONCLUSION

A mandatory vehicle I/M program such as Oregon’s confers benefits by improving overall air quality and may increase fuel economy through encouragement of proper vehicle maintenance. An I/M program is most effective when-targeted to specific problem areas. Targeting a program to areas having demonstrable air pollution problems would probably result in the greatest amount of public cooperation and present the fewest legal and economic difficulties.

The states can and should play a major role in developing innovative variations to be used in tailoring I/M programs to the states’ specific needs. A state I/M program gives state citizens the opportunity to determine the means by which national clean air goals will be achieved in their own state. Furthermore, I/M programs in general have proved to be minimally burdensome on a state’s budget and on the local motorist. These advantages of state action serve to dispel the notion that the success of comprehensive federal air pollution control programs need be gravely compromised by their dependence on state and local governments. Because of its control over the automobile, a state should take the initiative in implementing I/M. State implemented I/M programs have the advantage of preserving local self-determination because the flexibility inherent in an I/M program allows voters to modify the program to meet changing needs as they arise locally, so long as those modifications do not significantly undermine the state’s ability to implement its Transportation Control Plan.

States which share a common air pollution problem from the motor vehicle should, through cooperative efforts, seek solutions which are economically and administratively acceptable to the involved states. An I/M program can make a significant contribution to the alleviation of interstate mobile source air pollution.

The inspection of passenger cars should remain the exclusive province of the states. The present constitutional ability of states to inspect heavy duty commercial vehicles engaged in interstate commerce is clear. However, because of practical political, economic and administrative considerations, no state has yet attempted to inspect heavy duty vehicles registered outside its jurisdiction. Congress, assuming it does not wish to preempt control of air pollution generated by heavy duty interstate trucking, can facilitate state inspection by passing laws establishing uniform emission standards and tests for such vehicles.

The Federal Clean Air Act mandates the solution to the national problem of air pollution by calling for action by the states. An I/M program affords the states the opportunity to fulfill this duty without sacrificing any of
their traditional prerogatives. Because of the growing impatience of Congress, the EPA, and certain environmental groups, it is imperative that state officials review with more profound interest their policies regarding implementation of such transportation control measures as I/M.
Coal Slurry Pipelines: a Railroad Perspective

NORMAN M. LORENTZSEN*

Coal is an important element in energy self-sufficiency for this country. The energy plan offered in 1977 by President Carter is built substantially upon a foundation of coal and calls for massive conversion of present and planned facilities to the use of this fuel by 1985. This has important implications for western railroads because this plan envisions nearly a fourfold increase in coal production.¹

The rise in the importance of coal to national planning processes began in the early part of this decade. The energy crisis that stunned this country in October, 1973, had palpable impacts on home and business heating as well as on the availability of gasoline for automobiles. Government and business leaders saw the cutting off of petroleum from the Middle East as an early warning of possibly worse misfortunes that could be expected to befall the U.S. if the country did not immediately undertake to become energy self-sufficient.²

There was another emerging trend that had been developing in the national energy picture since the early 1960's. Rising concern over air quality had resulted in federal, state and local regulations governing smoke-stack emission.\(^3\) Power plants and factories were forced to add expensive pollution-control equipment to diminish the sulphur and other particulates that were inherent in the eastern and midwestern coals used for the production of electricity and for industrial purposes. As a result of this development, there was a sudden interest in the vast reserves of coal that were known to exist under the arid lands of the western states.\(^4\) Previously, there had been little other than local demand for western coal because, although lower in sulphur and pollutants, western subbituminous and lignite also have comparatively less heat content than eastern and midwestern coals.\(^5\) Before 1970, western coals were too distant from major markets to be competitive in price with eastern and midwestern coal even though western coal could be strip-mined at less expense than eastern and midwestern coal which was deep-mined. However, the situation began to change in the mid-1970's as new mines were opened in the West and production rose dramatically.\(^6\) In addition, the Middle East oil embargo of 1973 accelerated the pace of western coal development. All-coal unit trains placed into service by rail carriers made this region’s coal competitive in price over an expanding area of the United States. For example, today Burlington Northern is hauling coal from western mines to users as distant as 1500 miles;\(^7\) moreover, it is expected that these distances will increase as additional power plants are built.

Despite the cost and low sulphur benefits, western coal has developed at a slower pace than was originally envisioned.\(^8\) This is because the lead time required for opening mines and for construction of new power plants is an important factor in coal development. Most coal is sold on long-term contracts that can vary in length from five to thirty years. Both the utilities and the mines benefit from this kind of contractual arrangement—mine operators protect their investments, and utilities have the assurance of a long-

\(^3\) Id. at 39.
\(^4\) National Energy Transportation, supra note 1, at 441. Identified coal reserves in the U.S. total nearly 2 trillion tons. Approximately 70% of these are in states west of the Mississippi River.
\(^5\) Id. at 445.
\(^6\) Coal production in Wyoming doubled between 1969 and 1972, to a total of 10,920,000 tons; by 1975 production had risen to nearly 24,000,000 tons. See 1977 Keystone Coal Industry Manual 710.
\(^7\) Burlington Northern’s longest movement of coal is from Belle Ayr, Wyoming, to Elmendorf, Texas, a distance of 1642 miles. This movement has been in operation since 1978.
term supply of fuel—sometimes as long as the expected life of the plant. The lead time factor is further affected by the impact of government regulations, including environmental protection requirements, strip-mining method laws, and site location constraints. Consequently, although the desired rate of conversion to coal envisioned in the National Energy Plan may be delayed somewhat, over the long run the imperatives of the nation’s need for energy will most likely require that the coal be produced and that it be produced in very large volumes.

It is also important to examine the demand side of the coal equation. At present, the major users of coal are electric utilities, and there is already evidence of a strong trend for increased use of coal in the generation of electricity. National Energy Plan projections call for utilities’ percentage of total energy use to rise from 45% in 1976 to 54% in 1985. This translates into an increase in utility coal demand from 406 million tons in 1975 to 770 million tons in 1985. However, changes in energy conservation, plant retirements, and intensity of electrical use could alter these figures.

Often overlooked is the demand for coal in the general industrial sector. Here the rate of growth in coal demand is more pronounced and conversion features of the National Energy Plan will have the greatest impact; the Plan calls for more than an 85% increase in the demand of industrial users for coal, caused largely by conversion from oil to coal. So that, although the growth and demand will be greatest in electric utilities, increases in the rate of coal consumption will be much higher for industrial users. Moreover, the increase in industrial use will be more dramatic in instances where it entails sharp reversal of the established patterns of energy consumption. Also important is the vast number of facilities that would be using coal for industrial purposes. A 1977 tabulation by the Federal Energy Administration identified 3500 major industrial plants, diffused over a wide geographic area, which might convert to coal. While some of the plants are relatively large users of energy, most are very small and would require only modest deliveries of coal. The number, size, and geographic scatter of these industrial coal users poses a major challenge when viewed from a transporation perspective because the overall mission of this

12. Id.
13. Id. at 7.
14. Id. at 11.
country's transporation system will be not only to move massive amounts of coal, but to move this coal over great distances and to a variety of individual locations in varying amounts.

RAILROADS AND COAL

When the requirements of the National Energy Plan are viewed in the light of transportation needs, it is likely that major responsibility will fall on the nation's railroads.15 Railroads historically have handled most of the coal movements in the United States, and this mode of transportation will probably continue to be important because the commodity is easily adapted to rail handling. Coal is a bulk commodity that requires little in the way of protective services; it can be quickly loaded and unloaded; and it moves at a steady rate of flow over long distances.

Although compatibility has allowed railroads to be the dominant carrier in coal transport, the traffic is subject to variations in volume and railroads have had to adjust their operations accordingly. In recent years, rail coal traffic has fluctuated significantly because of demand patterns. In 1945 for example, the railroads originated almost 400 million tons of bituminous coal, but as users shifted to alternate fuels, the market for coal diminished with the result that by 1960 rail coal tonnage was down about 100 million tons from post-war levels.16 Then, as users began gradually to shift back to greater use of coal in the 1970's, the coal traffic for railroads rose to levels where it had been fifteen years earlier.17

In the last five years, the railroads have experienced substantial increases in the volume of coal handled. Burlington Northern, for instance, almost doubled its coal tonnage and tripled both coal ton miles and daily unit train origins between 1972 and 1976.18 Moreover, it is expected that by 1981, Burlington Northern will be handling more than three times its 1976 volume of 43 million tons.19 The rail industry as a whole has seen steady and substantial increases each year, and as the National Energy Plan takes effect, these increases will continue. The coal traffic expansion of the past few years was accommodated on relatively short notice and at a time when non-coal traffic was also growing20—evidence of the industry's physical ability to expand quickly.

There are some who, when looking ahead at the large volume of coal to be transported, question the capacity of the national rail freight system to

15. NATIONAL ENERGY TRANSPORTATION, supra note 1, at 460.
17. Id.
18. Coal ton-miles in 1972 were 11,11 billion; in 1976 they totaled 32.1 billion. In 1972, an average of 4 unit coal trains were originated daily; by 1976, the average was 12 per day.
19. See H.R. 1609 Hearings, supra note 8, at 361.
meet the increased demand for coal transportation. Yet, although the volume of coal to be transported is substantial, the increases must be considered in a perspective with all other traffic. In this light, the increase in total rail traffic volume would not be overwhelming; with coal added to non-coal traffic the annual growth in total tonnage would be just over 3%. Past experience indicates that the anticipated growth in coal traffic, although large and challenging, will be manageable.

Increased coal volume will greatly improve the utilization of the physical facilities of the rail industry which is characterized by overcapacity—in terms of both individual lines and the overall system of 200,000 miles of rail line now in service. The Department of Transportation has determined that a third of the rail lines carry only one percent of railroad traffic. Measured in gross ton miles, the Department has reported that two-thirds of the traffic moves on just 40,000 miles or twenty percent of the lines. The expected coal volume will result in added traffic for many of the underused lines and any isolated capacity deficiencies on more intensively used lines that might be presented can be remedied through operational changes and by modifications of the physical plant.

In considering rail coal-handling capacity, recognition must be given to the fact that the movement of coal lends itself well to high-utilization techniques such as unit-train handling. Unit trains are composed of 100 or so cars and power units that are dedicated entirely to one movement. The unit train is in almost constant motion shuttling between origins and destinations. These trains avoid the delays of conventional handling by circumventing major terminals and by being loaded and unloaded rapidly. Unit-train movements also are highly predictable, permitting maximum efficiency in use of main-line capacity. These characteristics translate into important operational capacity enhancement notwithstanding any consideration of the excess physical capacity. Recognizing these capabilities, recent studies by the Office of Technology Assessment and the Department of Transportation have concluded that the nations’ railroads have the physical and operational ability to meet the transportation needs of the National Energy Plan.

For railroads, the surge in coal traffic does not present capacity problems; however, it does present a challenge in terms of the investment required to acquire equipment and to improve the quality of tracks and

21. See NATIONAL ENERGY TRANSPORTATION, supra note 1, at 460.
22. The Race to Carry Carter’s Coal, BUSINESS WEEK, May 16, 1977, at 78 [hereinafter cited as BUSINESS WEEK].
23. BARBER, supra note 11, at 31.
roadbeds over which coal will be hauled. One study by the Department of Transportation has estimated U.S. railroads’ investment needs for coal to be about ten billion dollars.\textsuperscript{25} This challenge is heightened because these massive investments are required before the coal is to move. Burlington Northern, for example, currently is in the process of investing nearly one billion dollars in equipment and track improvements so that it can be ready to handle the coal that is scheduled to be moved over the next several years.\textsuperscript{26}

While utilities, industry, and coal producers also face large-scale capital needs, it is expected that they will be able to adjust their prices sufficiently to show a level of earnings needed to attract the necessary capital. The generally anemic financial conditions of the rail industry, however, cast railroads in an unfavorable light when competing in the money markets. Since the mid-1960’s, railroad earnings have been in a general decline.\textsuperscript{27} To a degree, this has been caused by the diversion of traffic to other modes of transportation leading to a reduction in the revenues needed to offset the costs of unused plant capacity. Reflective of this decline, U.S. railroads’ ratio of net income to net worth fell from just over 5% in 1960 to 1.8% in 1976.\textsuperscript{28} By comparison, unregulated manufacturing firms’ ratios for 1976 averaged 15% and electric and gas utilities showed ratios of nearly 12%.\textsuperscript{29} Because of this prolonged drought in earnings, railroads have not been able to generate sufficient internal funds to finance long-term capital investments; and consequently, have had to rely increasingly on external sources of funding. This pattern is evident in the railroad industry capital structure. The share accounted for by equity declined from 65% in 1964 to less than 56% in 1974.\textsuperscript{30} This increased reliance on debt has been accompanied by large increases in interest costs: between 1965 and 1975, interest payments on funded debt rose 87% while interest on unfunded debt—as used in equipment financing—showed an increase of 558%.\textsuperscript{31}

Not only has the increased reliance on debt been costly, it has not been adequate for the industry’s needs. Because of the lack-luster record of earnings, much of the debt financing the industry has been able to obtain often is conditional and restricted to equipment acquisitions.\textsuperscript{32} Funds needed for improvements in physical plant are difficult to obtain, and where internal earnings are insufficient, individual railroads have no choice but to

\textsuperscript{25} Coal’s Clouded Post-Strike Future, Time, April 17, 1978, at 75.
\textsuperscript{26} 1977 Annual Report of Burlington Northern, Inc. 5.
\textsuperscript{27} Barber, supra note 11, at 46.
\textsuperscript{28} Id. at 48.
\textsuperscript{29} Id.
\textsuperscript{30} Id. at 50.
\textsuperscript{31} Id. at 51.
\textsuperscript{32} See National Energy Transportation, supra note 1, at 464.
delay improvements on tracks and roadbeds.33

The foregoing indicates that the expected burgeoning of coal traffic presents a two-dimensional prospect to the railroad industry. First, it is an immense opportunity to solve the overcapacity problems and generate the cash flows that will, in turn, allow greater financial self-sufficiency and much-needed rehabilitation of the physical plant. It will also be a challenge of equal proportion in terms of the large-scale investments required. It is hoped that the investment community will place enough reliance on future prospects of coal revenues to advance the funds necessary to realize such revenues.

**COAL SLURRY PIPELINES VERSUS THE RAILROAD INDUSTRY**

Set against the backdrop of the railroad industry’s desire to handle the large volume of coal envisioned by the National Energy Plan, coal slurry pipelines represent a threat to the attainment of those volumes. Coal slurry is a relatively new technology that involves the pulverization and mixing of coal with water so the mixture can be pumped through large pipelines over long distances. Several proposals are now being advanced to move coal by slurry pipeline from western and Appalachian coal fields to destinations as far as 1,000 miles.34 The major proposals envision movements of as much as 25 million tons of coal per year by a single pipeline.35 This would be the equivalent of about 250,000 rail carloads; only two lines of this size could move an amount equivalent to the total coal Burlington Northern carried from western mines in 1977. In terms of coal revenues at today’s rate levels, a single, 25-million ton slurry pipeline would have the potential to divert about one-quarter of a billion dollars annually from rail transport36—a prospect that has caused a marked degree of alarm to the railroad industry and could affect the attitudes of the investment community which is expected to supply the capital for coal-related rail improvements.

To acquire the right-of-way for their facilities, pipeline promoters are seeking the powers of eminent domain in Congress and in certain states to condemn land.37 Their most aggressive lobbying effort has been at the federal level. In 1974, a coal slurry eminent domain bill was passed by the

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33. Id.
34. Although a number of coal slurry pipelines have been discussed, most prominent is a pipeline, 36 inches in diameter, that would run from near Gillette, Wyoming, to Little Rock, Arkansas, a distance just over one thousand miles. This pipeline is being promoted by Energy Transportation Systems, Inc. Coal Transportation Task Force, supra note 24, at IV-2.
35. See id.
36. Assumes a freight cost of $10.00 per ton or $.01 per ton-mile. This is a rough average of current Burlington Northern unit train coal rates. Actual revenue losses would depend on the specifics of the movement diverted and the rate-levels in effect at the time.
37. See Coal Transportation Task Force, supra note 24, at IV-2.
U.S. Senate but not by the House. In 1975, four similar bills were introduced in the House of Representatives and extensive hearings were held by the Committee of Interior and Insular Affairs, focusing on H.R. 1663. This bill was tabled in 1976 pending a study by the Office of Technology Assessment on the impacts of coal slurry pipelines. Legislative efforts were renewed in 1977 in the form of H.R. 1609, which was delayed until February of 1978 when an amended version passed the House Interior and House Public Works and Transportation Committees. The bill came before the House on July 19, 1978, and was defeated by a vote of 246 to 161.

Developers of coal slurry pipeline proposals are attracted by the prospect of profits through the construction and financing of the projects. Burlington Northern made an extensive study of the feasibility of constructing a slurry pipeline out of the Powder River Basin coal fields which it serves. The study indicated that the profit potential from construction could be diminished by environmental and water source problems. Moreover, it was felt that the cost uncertainties and inflexibility would be a severe handicap in obtaining customers for the line. Construction opportunities notwithstanding, the transportation aspects of slurry pipelines did not offer much in the way of profit potential nor economic viability.

For firms such as Bechtel Corporation and Lehman Brothers, whose perspectives are on construction and finance rather than transportation, however, the profit prospects of slurry lines evidently appear more sanguine. Thus, they strongly supported the efforts to obtain authority for eminent domain. They have argued that there is compelling need for coal slurry pipelines to meet National Energy Plan goals and that pipelines are needed to break a railroad "monopoly" in the transportation of coal. Railroads and other allied groups have responded that there is no need for a duplicate transportation system to be built, and have emphasized the potential hazards to water supply, to the environment and to the national economy inherent in development of slurry pipelines.

As Congressional deliberations of the coal slurry legislation progressed, it became clear that this was much more than a parochial skirmish between industry interests. The issues that emerged were of serious

42. Study done jointly with Bechtel Corp. and Peabody Coal Co.; information is not publicly available.
43. Id.
44. See BUSINESS WEEK, supra note 22.
45. Id.
46. See generally H.R. 1609 Hearings, supra note 8.
and far-reaching nature with direct and substantial impact on a number of public policy questions. The Office of Technology Assessment, which was asked by Congress to provide an assessment of major issues, identified the main areas of public concern as follows:

At least three major sets of policy questions must be addressed to arrive at a legislative conclusion. The first involves the desirability from social, economic, and environmental standpoints of developing a coal slurry pipeline industry. The second is related to the extent to which the present regulatory and institutional arrangements would have to be altered to provide for the allocation of coal traffic between pipelines and railroads in a way that would represent the least cost to society. The third concerns the balance of Federal and State control over such areas as water resource allocations, land ownership, and local environments, and how conflicting regional interests might be resolved.47

The foregoing indicates that the consequences of coal slurry line development, resulting from granting of eminent domain authority, would affect millions of citizens. Western ranchers and environmentalists concerned about use of water, railroad employees and the communities of which these employees are a part, electric power consumers whose chief concern is a reliable and low cost source of electricity: all have a direct interest in this legislation.

EXAMINATION OF COAL SLURRY ISSUES

EMINENT DOMAIN

Eminent domain is the power to take private property without the owner's consent provided he is compensated on the basis of fair market value.48 The concept is of ancient derivation, originally based on an inherent power of a sovereign, and is sparingly given. Usually the power is granted by a state only in situations where a significant public need is to be filled by the services of the instrumentality seeking the authority.49

It should be noted that when eminent domain is conferred, it is usually a result of state legislation; it is rarely granted by the federal government.50 Inasmuch as six western states have specifically granted conditional eminent domain to coal slurry pipelines, a proposed pipeline from Gillette, Wyoming to Little Rock, Arkansas being promoted by Energy Transportation Systems, Inc. might be built under those authorities—or possibly under a general authority in some of the other western states.51 From the standpoint of the slurry promoters, however, it would be much easier to have the blan-
ket federal eminent domain authority and not have to prove "public benefit" conditions in each state along the routes of the lines.

In petitioning for federal eminent domain authority, the slurry advocates have put forth several arguments as justification. First, they claim that there is a significant need for another system of transportation because of insufficient rail capacity. Further, they argue that another mode of transportation is needed to provide "rate competition" for the railroads. Finally, they argue that natural gas pipelines have federal eminent domain authority, and so should slurry pipelines.52

The argument that railroads do not have the physical capabilities to handle the coal needed in the future has been largely laid to rest by numerous studies, conducted by independent analysts.53 Moreover, while one part of the Bechtel organization was proclaiming that western railroads were deficient in capacity, another Bechtel group concluded, in a study performed for a midwest power pool, that "there appear to be no significant physical, operational, or environmental reasons why western coal growth cannot be accommodated by the railroads."54

To the contention that slurry pipelines are needed to provide competition to railroads, there is competition between coal and other types of fuels such as nuclear and oil, competition among geographic coal-producing regions, competition among modes of transportation and competition among rail carriers. As an example, the Powder River Basin coal-producing area will be served by Burlington Northern, as well as by the Chicago North Western.55 In addition, coal is currently being trucked out of that area to market.56 In short, the competition among fuels, regions, modes and railroads has been an influence in keeping transportation costs for western coal at levels well below that of other commodities.57 This should indicate that rail coal rates are not based on monopoly pricing. But even were the contrary true, the Interstate Commerce Commission has and exercises full authority to review and change any rates felt to be unjustifiably high (or for that matter, unreasonably low).58 As legislation now stands, customers of slurry pipelines would not have this kind of governmental protection against excessive pricing.59

52. Walker, supra note 48.
53. See sources cited in note 24 supra.
54. BECHTEL CORP., WESTERN COAL UTILIZATION IN THE MID-CONTINENT AREA POWER POOL, A PRELIMINARY ASSESSMENT PERFORMED FOR THE MID-CONTINENT AREA POWER POOL at 7-54 (1975).
55. H.R. 1609 Hearings, supra note 8, at 254 (testimony of J. Wolfe).
56. Address by A. Stenseth, Director of South Dakota Dept. of Railroads, Western Rural Editor’s Exchange, Rapid City, South Dakota (April 20, 1978).
57. See Walker, supra note 48, at 265.
58. Id.
59. A later section will deal in more detail with this and other anti-competitive aspects of coal slurry pipelines. See text accompanying notes 68-72 infra.
Finally, as to the argument that because federal eminent domain has been given to natural gas pipelines, it should also be given to slurry pipelines, an examination of the facts indicates little similarity between natural gas and coal slurry pipelines. The grant of federal eminent domain to natural gas pipelines was only a part of a general plan for comprehensive regulation of the natural gas industry.\textsuperscript{60} The slurry-line promoters and the coal industry have not sought and are not subject to this type of regulation. Moreover, pipelines are the only means by which natural gas can be feasibly transported over long distances.\textsuperscript{61} Coal, on the other hand, is being transported by highway, water and rail transport.\textsuperscript{62}

In summary, the usual justifications voiced in support of granting eminent domain authority are questionable. Furthermore, as the following discussion will indicate, the development of coal slurry pipelines may have consequences which are detrimental to the environment, to a balanced transportation policy and to the consuming public.

\textit{WATER PROBLEMS}

In the West, coal slurry pipelines face a water problem. This, far more than comparative costs or pace of development, will serve to limit their usefulness. The development of several [large diameter] lines out of a given area will require a water draw-down that may seriously impact other regional developments.\textsuperscript{63}

The water-depletion hazard associated with slurry pipelines has been one of the most potent deterrents to passage of eminent domain legislation. One ton of water is required to transport each ton of coal in the slurry method; for a 25 million ton per year line, the water used amounts to about six billion gallons per year.\textsuperscript{64} Because of prohibitive costs of recycling, the water must be obtained from the area where the coal is mined, making the problem especially severe in the western coal regions where water is already in short supply.\textsuperscript{65}

Aside from the physical depletion of water resources, there is serious concern that federal eminent domain for coal slurry pipelines may undermine the right of individual states to control their own surface and ground-

\textsuperscript{60} See O.T.A., supra note 24, at 135.
\textsuperscript{61} Id.
\textsuperscript{64} E. Wasp, Progress with Coal Slurry Pipelines (Sept. 30, 1975) (paper presented at American Mining Congress, 1975 Mining Convention, San Francisco, California) [hereinafter cited as Wasp].
\textsuperscript{65} Id.
water resources. The recent evaluation of issues by the Office of Technology Assessment pointed out the possibility that an individual state might not be able to impose water-use restrictions on a slurry pipeline company once that company had received federal certification. These concerns about misappropriation and deterioration of control of water have united major agricultural and environmental organizations into a bloc of opposition which may effectively impair the development of large coal-slurry pipelines in the West irrespective of eminent domain questions.

**Anticompetitive Characteristics**

Competitive abuses may be inherent in coal slurry pipeline development. An OTA report has pointed out that "coal slurry pipelines will make arrangements with shippers by throughput and deficiency agreements or ship-or-pay contracts. Although these arrangements can serve valid business purposes, they also impose a restraint on trade." The throughput—or "take-or-pay"—contract is an arrangement which would obligate the shipper to take, or pay for, a fixed volume of coal annually over a period of 20 to 30 years. While the use of throughput contracts would offer extraordinary competitive advantage to slurry pipeline operations, the restraint-of-trade effects could be devastating to other modes of transportation and disadvantageous to electric power consumers. Common carrier railroads are not allowed to make similar long-term contracts. One effect of the "take-or-pay" device would be to insulate large segments of coal traffic from competition by other modes for long periods of time. Because the shipper would be contractually obligated to the slurry pipeline, such traffic would be lost beyond recall despite any cost or operational innovations which might be effected by a competing carrier. This would amount to a virtual coal slurry pipeline monopoly of the traffic involved. Moreover, not only would competing carriers be shut out, but also the electric consumer would be prevented from taking advantage of any benefits which might develop over the period from fuel technology changes or from improved productivity in transportation.

There are several other aspects of coal slurry operation which may give an unfair competitive edge to that mode. Slurry pipelines will probably not

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66. According to O.T.A., supra note 26, at 20, the Commerce and Property clauses of the U.S. Constitution provide sufficient power to the Federal government to assure adequate water supplies to a coal slurry line despite any restrictions by a state. Moreover, the report warns that First Iowa HydroElectric Cooperative v. Federal Power Commission, 328 U.S. 152 (1946), suggests that federal certification of coal slurry pipelines will negate state attempts to control use of its own waters for this purpose.

67. See *Business Week*, supra note 22.

68. O.T.A., supra note 24, at 130.

69. Id. at 126.

70. Id. at 130.
be required to assume the public responsibilities and regulations required of common carrier railroads. Essentially private carriers, slurry pipelines would not be subject to strict regulations on entry, abandonment and extension as are common-carrier railroads. In addition, railroads are required by the Interstate Commerce Commission to perform unprofitable services on low-volume branch lines and must provide service to small and large customers alike.\textsuperscript{71} Slurry pipelines would have no obligations in these areas.

A sound national transportation system depends on a balance among modes of transportation. Consequently, if one carrier is allowed to use monopolistic contract privileges and is given absolution from common-carrier regulation, the system could be destructively imbalanced to the detriment of the economy as a whole.\textsuperscript{72}

\textit{Impact on Railroads and Users}

Slurry pipeline development could have a devastating effect on the marginal segments of the railroad industry as well as on businesses who ship by rail. This danger was recognized by former ICC Chairman, George Stafford, who stated that:

\begin{quote}
Diversion of coal traffic could result in railroads having to reduce their service to coal producing areas, further depriving them of revenue and perhaps forcing them to increase their rates on other commodities to cover operating costs. In some cases, such diversion could pose a threat to a railroad’s very existence.\textsuperscript{73}
\end{quote}

Massive new investments will have to be made prior to the time the larger coal volumes move and will come mostly from borrowed funds.\textsuperscript{74} Construction of proposed coal slurry lines would not significantly reduce the railroads’ capital investment requirements, because, as common carriers, the railroads would be required to deliver the coal while the pipelines were being constructed.\textsuperscript{75} Consequently, the diversion to pipelines would leave the railroads with a huge debt service and repayment burden while a substantial part of the coal revenues, which were being counted on to repay the debt and interest, would be locked away from competitive recapture.

Diversion by a single, 38-inch pipeline could result in a loss of rail coal revenues approximating $250 million.\textsuperscript{76} Faced with a shortfall of these dimensions, it is possible that marginal railroads could be forced into bank-

\begin{itemize}
\item \textsuperscript{71} \textit{Id.} at 125.
\item \textsuperscript{72} \textit{Id.}
\item \textsuperscript{73} \textit{Coal Slurry Pipeline Legislation: Hearings on H.R. 1863, H.R. 2220, H.R. 2553, and H.R. 2986 Before the House Committee on Interior and Insular Affairs, 94th Cong., 1st Sess., 625 (1975)} (testimony of G. Stafford, Chairman of the Interstate Commerce Commission) [hereinafter cited as Stafford].
\item \textsuperscript{74} \textit{See} \textit{Barber, supra} \textsuperscript{12}, at 58.
\item \textsuperscript{75} \textit{See} \textit{H.R. 1609 Hearings, supra} \textsuperscript{9}, at 345 (statement of Louis W. Menk).
\item \textsuperscript{76} \textit{See} \textsuperscript{note 36, supra}.
\end{itemize}
rupticy; or at the least, have to cut drastically back on service and try to raise rates on other commodities to generate cash flows sufficient to meet fixed charges.\textsuperscript{77} These consequences would have a direct and negative effect on the overall economy as well as on individual communities.

Diversion of coal to slurry pipelines would also cause higher shipping costs to shippers whose needs would not match the huge volumes necessary for slurry transport.\textsuperscript{78} Shrinkage in rail revenues without a corresponding reduction in unavoidable costs of coal-related plant expansion would result in net income reduction. This could mean that rail shippers of coal and other commodities would be called upon to bear a larger part of these costs if railroads could not absorb the shortfalls.\textsuperscript{79} This could hit medium and small coal shippers especially hard, but could result in higher transportation costs for shippers of grain, lumber and other rail-carried products as well.\textsuperscript{80} In short, coal slurry pipelines' benefits would accrue to only a handful of giant firms while the costs and burdens would have to be carried by the shipping public at large.

Another related negative impact of coal slurry pipeline development would be loss of job opportunity for thousands of railroad workers. Pipelines are much less labor-intensive than railroads, requiring considerably fewer employees to operate the system.\textsuperscript{81} Construction jobs for pipeline construction are of short duration. Slurry pipeline developers admit that a diversion of 25 million tons of coal from rail to slurry would result in a net loss of about 2200 jobs.\textsuperscript{82} The effects of this on local economies must be factored into any evaluations of public impacts expected from coal pipelines.

**CONSUMER CONSIDERATIONS**

Perhaps the greatest obstacle to coal slurry pipeline development will be the cost uncertainties, inasmuch as there are no large-diameter coal slurry pipelines in existence in this country, and all cost estimates at this time are hypothetical.\textsuperscript{83} The necessity to predict future costs of construc-

\textsuperscript{77} See Stafford, supra note 73.
\textsuperscript{78} See generally Barber, supra note 11, at 73.
\textsuperscript{79} See O.T.A., supra note 24, at 81.
\textsuperscript{80} Id.
\textsuperscript{81} 1 F. Armbruster & B. Candela, Research Analysis of Factors Affecting Transportation of Coal by Rail and Slurry Pipeline 146 (Hudson Institute document HI-2409-RR, 1976) [hereinafter cited as Hudson].
\textsuperscript{82} Wasp, supra note 64.
\textsuperscript{83} See M. Reiber & S. Soo, Route Specific Cost Comparisons: Unit Trains, Coal Slurry Pipelines and Extra High Voltage Transmission 18 (Center for Advanced Computation, University of Illinois at Urbana-Champaign Document No. 190, 1976); Hudson, supra note 81, at 142.

The only coal slurry pipeline currently in operation is a 270-mile line from Black Mesa, Arizona, to Mojave, Nevada. This 18-inch line is one-half the size and only one-fourth the length of the...
tion, in itself, adds a major element of uncertainty to pipeline cost determination. Pipeline construction costs have increased at a steep rate in recent years and there are no indications that this will change in the future.84 Uncertainties about future labor productivity and inflation rates, as well as legal delay, compound the task to a point where the range of uncertainty associated with prediction of pipeline costs relative to rail costs can be as great as the difference between them.

The risks of these uncertainties, however, are to be borne by the consumer rather than by the pipelines or utilities. An important aspect of slurry pipeline development is that total costs are not known to the utility customer until after the pipeline is built.85 The utility, however, is required to bind itself to a long-term take-or-pay contract prior to beginning of construction so that the pipeline builders can obtain project financing.86 If after actual construction and operational costs were realized, the pipeline transportation costs were higher than the rail alternative, the utility would be contractually bound to take the coal at the higher price; and the consuming public would have no choice but to underwrite the extra costs. Referring to this danger, the Hudson Institute study states: "We fail to see why the public with no vested interests in a private enterprise must bear its risk of going sour."87 This feature of slurry transportation can be regarded as antipathetic to the public interest.

From a national coal consumption standpoint, slurry pipelines by nature do not match actual and projected demand patterns. To achieve their claimed maximum economies, pipelines must be of gigantic capacity and terminate at facilities equipped to use coal in quantities equivalent to the pipelines' annual throughput capacity.88 In reality, such conditions will likely not exist. Air protection regulations prohibit large-scale concentrations of coal-burning, power-generating plants.89 Even a large 800 megawatt plant would require only about one-eighth of the volume of a 38-inch pipeline as is being proposed.90 The actual patterns of future coal demand will be characterized by thousands of widely scattered coal users with a wide range of needs in terms of volume and types of coal.91 While these

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85. See HUDSON, supra note 81, at 144.
86. See O.T.A., supra note 24, at 130.
87. HUDSON, supra note 81, at 144.
88. See BARBER, supra note 11, at 62.
89. Id. at 63.
90. Id. at 62.
91. Id.
need patterns make a good match with existing rail transportation capability, they will not be met by a large, inflexible system such as a coal slurry pipeline. If eminent domain privileges are to be predicated upon substantial benefit to the overall public, coal slurry pipelines would fall far short of meeting this test because of consumer risk and consumer inaccessibility.

**TRANSPORTATION POLICY**

Although clothed as an energy-related proposal, the legislation for slurry pipeline eminent domain probably should be viewed in the light of national transportation policy. There is the danger that concern about energy development might override practical considerations implicit in the nation’s need for a sound and balanced transportation system. Under law and existing policy, the Congress contemplates the development of a balanced and economically sound system of common carriage.\(^92\) This is to provide the public an integrated transportation system in which each mode complements every other mode so as to maximize the nation’s logistic capabilities. In view of these considerations, it is important to examine the effect on the transportation equilibrium that would occur if development of coal slurry pipelines is encouraged through the grant of eminent domain.

The railroad industry views coal slurry promoters as striving for a position of special advantage.\(^93\) The federal power to condemn land is a privilege not given to rail coal transportation carriers;\(^94\) without the responsibilities or the regulations of true common carriage, coal slurry pipelines would be essentially private carriers, handling only one commodity and providing service only to those few large customers that offer them the most profitability.\(^95\) These advantages, plus the ability to use “take-or-pay” contracts, give slurry transportation the capability to upset the balances needed to maintain a sound transportation system overall. The ways by which such potentially destructive competition could financially devastate carriers dependent on coal movements have been discussed,\(^96\) and these consequences will have to be borne not only by railroads but also by the communities and shippers dependent on rail service.

\(^92\) See Walker, supra note 48, at 264.

\(^93\) Congressman Skubitz has also expressed this view: “We are, I suggest, talking about legislation to grant a special and totally unprecedented privilege to a small group of promoters seeking to use our legitimate concern about the Nation’s energy needs as an opportunity to pocket some fast bucks.” 122 Cong. Rec. H5009 (daily ed. May 27, 1976) (remarks of Rep. Skubitz).


\(^95\) See O.T.A. supra note 24, at 125.

\(^96\) See text accompanying notes 68-72 supra.
Coal will play an increasingly important role in this country's move to self-sufficiency. If the related transportation task is to be accomplished efficiently, a high standard of performance by the nation's railroad industry is essential. The industry has demonstrated its competence; that competence must not be undermined in the interests of construction and financial firms.

In the final analysis, the coal slurry pipeline controversy comes down to a question of public policy: Is it in the best interest of this country to facilitate the development of another specialized carrier when such development would darken the future of an entire existing industry? Coal slurry pipeline development could very well debilitate the financially fragile portion of this country's railroads and lead the industry dangerously close to the fate of the Penn Central. If this happens, the energy crisis may be joined by a "railroad crisis" of alarming proportions. The cost of this to the national economy would be enormous. This realization should cause sober reflection by the nation's policymakers, and one can only hope they will not overlook the dangers that lurk amidst the flurries of excitement over new technologies.
Commercial Zones and Terminal Areas: History, Development, Expansion, Deregulation

DANIEL W. BAKER*
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Under service date of August 11, 1975, the Interstate Commerce Commission issued an order in Ex Parte No. MC-37 (Sub-No. 26), Commercial Zones and Terminal Areas, directing that a proceeding be instituted for the purpose of considering modification of the then existing rules defining commercial zones and terminal areas. That notice is the genesis of what has become one of the more significant and controversial decisions that has been issued by the Interstate Commerce Commission.1 The notice informed interested persons that:

The purpose of this document is to institute a proceeding to determine whether commercial zones and terminal areas of motor carriers and freight forwarders should be redefined.

Section 203(b)(8) of the Interstate Commerce Act exempts motor carrier operations about municipalities from Federal economic regulation. The geographic area within which exempt motor carrier operations may be performed is referred to as a commercial zone. The existing regulations provide two

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** Handler, Baker & Greene, P.C., San Francisco, California. A.B., University of California, Berkeley, 1953; J.D., University of California, Hastings College of Law, 1958.
methods of defining the size of a particular commercial zone. The customary
method is by reference to a population mileage-formula developed in the mid-
1940's. The alternative method provides for an individual determination
of the commercial zone of a specific municipality. The present proceeding is
instituted for the following three purposes: (1) to determine whether, and the
extent to which commercial zones (and corresponding terminal areas of motor
carriers and freight forwarders) should be enlarged by expanding or other-
wise changing the present population-mileage formula; (2) to attempt to devise
a rule of general applicability for all commercial zones and terminal areas of
motor carriers and freight forwarders, at least with respect to incorporated
communities, thus dispensing with the need for the present individual definition
of irregularly shaped zones which are sometimes difficult to describe and in
need of subsequent revision; and (3) to make adjustments in the rule of appli-
cability about unincorporated communities compatible therewith.\(^\text{2}\)

Changes in the scopes of the commercial zones and terminal areas
were proposed in the notice, including adjusting the long-established popu-
lation-mileage formula,\(^\text{3}\) as follows:

\[
\begin{array}{cccc}
\text{Population} & \text{From} & \text{To} \\
\text{Less than 2,500} & 2 \text{ miles} & 3 \text{ miles} \\
2,500-24,999 & 3 \text{ miles} & 4 \text{ miles} \\
25,000-99,999 & 4 \text{ miles} & 6 \text{ miles} \\
100,000-199,999 & 5 \text{ miles} & 8 \text{ miles} \\
200,000-499,999 & 5 \text{ miles} & 10 \text{ miles} \\
500,000-999,999 & 5 \text{ miles} & 15 \text{ miles} \\
1,000,000 \text{ and up} & 5 \text{ miles} & 20 \text{ miles} \\
\end{array}
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The interim report and final decision of December 17, 1976, adopted
this proposal and thereby exempted from regulation by the Commission
extensive areas of the United States. There are many interesting and per-
plexing aspects of this decision. Certain of the most vigorous supporters of
regulation among the members of the Interstate Commerce Commission
were the strongest sponsors of the deregulation that results from this order.
Moreover, this deregulation is not confined to limited local areas. It em-
braces all large and small municipalities, metropolitan areas and unincorpo-
rated communities in the United States, ranging from such monsters as Los
Angeles, California, with a commercial zone encompassing an estimated
land area of over two thousand square miles, to small unincorporated com-
\(^\text{4}\) The effect of the order of the Commission is to achieve a more complete deregulation than
that advocated by any but the most resolute proponents thereof relating to

\(^{3}\) Id.
\(^{4}\) Ex Parte No. MC-37 (Sub-No. 26), Commercial Zones and Terminal Areas, 128 M.C.C.
422, 432 (1976).
interstate motor carrier transportation. Thus, we are confronted with the paradox of why the "regulation" of motor carriers in all metropolitan, municipal and unincorporated areas of the United States is not in the public's best interests, when the "regulation" of motor carriers outside these areas is in the public's best interests.

The order also is inconsistent with many existing and long-established policies of the Commission. For example, by determining the scope of terminal areas in the manner set forth in the decision, the Commission has defined service points and areas for most of the carriers under its jurisdiction in terms of radii from points of boundary lines. The Commission's long-established policy is against describing authorities in this manner. In the Fox-Smythe Transportation Co., Extension decision, the Commission declared its "policy" with respect to the use of territorial and service restrictions and its intention to establish "guidelines for the drafting of proper and workable motor carrier property applications." It is stated that grants of authorities in terms of mileage radius about a certain point "are discouraged as they might lead to interpretive problems." There are a number of recent decisions in which the Commission found, based upon specific data, that certain areas were not commercially parts of the base municipalities. For example, Ex Parte No. MC-37 (Sub-No. 14B) involved a petition to expand the Atlanta, Georgia, commercial zone, but an order issued on February 26, 1973, found that the area proposed was not commercially or economically a part of that city. The proposed area extended as far as nine miles from Atlanta. A petition to expand the Cincinnati, Ohio, commercial zone was considered in Ex Parte No. MC-30 (Sub-No. 2) and was denied on October 7, 1976, because the commerce in the proposed area could not be linked to the commercial zone of Cincinnati. On October 8, 1976, petitions were denied to expand the Minneapolis-St. Paul, Minnesota, and the Spokane, Washington, commercial zones. Thus, predicated upon specific data relative to each of these areas, the Commission issued recent rulings that the proposed extensions were not commercially parts of these base municipalities. However, in spite of these determinations, by its order in Ex Parte No. MC-37 (Sub-No.}

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6. 106 M.C.C. 1, 1 (1967).
7. Id. at 13.
9. Ex Parte No. MC-30 (Sub-No. 2), Cincinnati, Ohio, Commercial Zone, 125 M.C.C. 657, 660 (1976).
10. Ex Parte No. MC-37 (Sub-No. 2D), Minneapolis-St. Paul, Minn., Commercial Zone, 125 M.C.C. 649, 651 (1976); Ex Parte No. MC-37 (Sub-No. 27), Spokane, Wash., Commercial Zone, 125 M.C.C. 652, 654 (1976).
26) of December 17, 1976, it has reversed its position and has determined that all of these areas were commercially parts of the base municipalities.

The propriety of the Commission's rulings in this proceeding has been recently tested and affirmed after an appeal to the United States Court of Appeals for the Ninth Circuit in \textit{Shorthaul Survival Committee v. United States}.\textsuperscript{11} The decision of that court affirming the December 17, 1976, order of the Commission in \textit{Ex Parte No. MC-37} (Sub-No. 26) was issued March 17, 1978, and will be discussed hereafter. Neither the Commission nor the court stayed the order and the commercial zone and terminal area expansions became effective March 29, 1978. There was no petition for a writ of certiorari to the Supreme Court of the decision of the Ninth Circuit Court of Appeals.

Nevertheless, the inconsistency between the regulations promulgated by the challenged decision and past policies and rulings of the Commission, the espousing of deregulation by regulators, and the anticipated effect of the expansions of the exempt zones and areas, have raised the status of the Commission's order to one of significance and interest as a reflection of the Commission's present and future regulatory course and policy.

To understand the issues and consequences of the considered decision, a review of the history of commercial zones and terminal areas is essential. The following sections of this article will review the legislative and regulatory proceedings and procedures which created and determined commercial zones and terminal areas and the effect of the commercial zone deregulation and terminal area extensions upon motor carrier and freight forwarder services and upon the general public.

\textbf{Genesis of Commercial Zones}

Section 203(b)(8) of the Interstate Commerce Act permits the establishment of commercial zones and was enacted as a provision of the "Motor Carrier Act of 1935."\textsuperscript{12} Since enactment, the Commission and the courts have shared the burden of interpreting the language of the provision and determining the intent of Congress and the purpose of this discretionary exemption. To determine the congressional purpose for authorizing this conditional commercial zone exemption, reference must first be made to the language of the statute and its literal meaning.\textsuperscript{13} Are the purpose

\textsuperscript{11} 572 F.2d 240 (9th Cir. 1978).
\textsuperscript{12} Ch. 498, § 203(b)(8), 49 Stat. 543 (codified at 49 U.S.C. § 303(b)(8) (1976)).
\textsuperscript{13} Subsections (7a) and (8) of § 203(b) of the Act, as amended, provide:

(7a) ... nor, unless and to the extent that the Commission shall from time to time find that such application is necessary to carry out the national transportation policy declared in this Act, shall the provisions of this part, except the provisions of Section 204 relative to qualifications and maximum hours of service of employees and safety of operation or standards of equipment apply to:

(8) the transportation of passengers or property in interstate or foreign commerce wholly
and intent definitely and unequivocally expressed or did Congress afford the Commission only broad and general guidelines to follow? Are there any limitations or standards which must be observed and applied by the Commission in deciding if, and to what extent, commercial zones should be established and the transportation therein exempted from regulation? Section 203(b)(7a) provides that only "unless and to the extent that the Commission shall from time to time find that such application [of regulation] is necessary to carry out the [N]ational [T]ransportation [P]olicy" 14 shall motor carrier operations within such zones be subjected to economic regulation under Part II of the Interstate Commerce Act. Thus, any exemption authorized must be in conformance with the standards set forth in the National Transportation Policy. Section 203(b)(8) further specifies that the exempt area may be "wholly within a municipality or between contiguous municipalities or within a zone adjacent to and commercially a part of any such municipality or municipalities." 15 The fact that the limits of the exempt area are not more closely delineated leaves the Commission the right to exercise its investigatory authority and expertise, as it has done in the Ex Parte MC-37 proceeding considered herein. Thus, Congress has established commercial zones of municipalities and their related and adjacent

within a zone adjacent to and commercially a part of any such municipality or municipalities, except when such transportation is under a common control, management, or arrangement for a continuous carriage or shipment to or from a point without such municipality, municipalities, or zone, and provided that the motor carrier engaged in such transportation of passengers over a regular or irregular route or routes in interstate commerce is also lawfully engaged in the intrastate transportation of passengers over the entire length of such interstate route or routes in accordance with the laws of each state having jurisdiction.


14. 49 U.S.C. § 303(b)(7a) (1976). The declaration of the National Transportation Policy was formerly included in section 202(a) of the Motor Carrier Act of 1935. It was made applicable to all forms of transportation and placed before Part I of the Interstate Commerce Act by the Transportation Act of 1940. The National Transportation Policy enunciated by Congress is as follows:

It is hereby declared to be the national transportation policy of the Congress to provide for fair and impartial regulation of all modes of transportation subject to the provisions of this Act... so administered as to recognize and preserve the inherent advantages of each; to promote safe, adequate, economical, and efficient service and foster sound economic conditions in transportation and among the several carriers; to encourage the establishment and maintenance of reasonable charges for transportation services, without unjust discriminations, undue preferences or advantages, or unfair or destructive competitive practices; to cooperate with the several States and the duly authorized officials thereof; and to encourage fair wages and equitable working conditions—all to the end of developing, coordinating, and preserving a national transportation system by water, highway, and rail, as well as other means, adequate to meet the needs of the commerce of the United States, of the Postal Service, and of the national defense. All of the provisions of this Act... shall be administered and enforced with a view to carrying out the above declaration of policy.

Act of Sept. 18, 1940, ch. 722, § 1, 54 Stat. 899 (codified at 49 U.S.C. preceding § 1 (1976)).

business or commercial areas, exempt from economic regulation by the Commission to the extent it finds warranted by the National Transportation Policy as enunciated by the Congress.

The Commission and the courts have declared that the language in section 203(b)(8) and the related legislative history furnish little assistance in determining the purpose of this provision or the intent of Congress. They have described the language and history of the statute as being indefinite, lacking in specific guidance, and having no precise definition; and they have applied interpretations from time to time predicated upon speculation as to the purpose of the exemption and to the intent of Congress. In construing the intent of Congress, the legislative history is resorted to, including the committee reports and, particularly, the records of the congressional debates. Because of the complexity of modern federal legislation, these debates have become increasingly more significant and useful in construing legislative intent. The debate in the Senate was led by Senator Wheeler who introduced Senate Bill 1629, which was adopted as the Motor Carrier Act of 1935. The bill was introduced at the request of the Interstate Commerce Commission. Senator Wheeler advised the Senate that the bill had the endorsement of the Commission, the American Trucking Association, many shippers, practically all of the state commissions, and the truck and bus industries of the United States. With respect to the commercial zone exemption, he stated:

Furthermore, an exemption is made, unless the Interstate Commerce Commission finds that the law cannot be made to work without its inclusion to some extent, of the transportation of property locally or between New York City and New Jersey, and also, for instance, as between Washington and Alexandria, and other contiguous cities where the transportation is regulated by the local governments themselves.

Provision is also made that regulation shall not apply to what may be termed 'intramunicipal' or 'occasional' operations 'unless and to the extent

16. Representative Moorhead has described the use of congressional debates to establish the congressional intent in the adoption of statutes as follows:
Mindful of this judicial scrutiny, legislators of today have used the opportunity of debate to achieve legislative goals which might otherwise be unattainable. Indeed, by the use of the 'friendly colloquy' two men may be able to legislate more effectively than all of Congress.

This type of colloquy is presented in the form of a friendly exchange of questions and answers about the pending legislation between members, one of whom is usually a member of the committee from which the legislation emanated. This seeming repartee is not accidental. In fact, it is just the opposite. It has been carefully planned by the parties for the express purpose of providing a legislative interpretation of a statutory provision which might otherwise be differently interpreted.

that the Commission shall from time to time find that such application is necessary to carry out the policy of Congress enunciated in Section 202. The first of these two conditional exemptions concerns the transportation of passengers or property in interstate or foreign commerce within a municipality or between contiguous municipalities or within a zone adjacent to and commercially a part of any such municipality or municipalities, except when such transportation is part of a continuous carriage or shipment to or from a point without such local area.\textsuperscript{18}

The concern of the states with respect to the failure of the federal government to regulate motor carrier transportation was significant and pervaded the debates in both the Senate and the House of Representatives. In explaining the effect of the lack of federal regulation of motor carriers, Senator Wheeler reported that "[t]he absence of such regulations has in some instances created chaotic conditions beyond the control of any state or municipal body."\textsuperscript{19} In discussing the controls or restraints placed upon the Commission, Senator Wheeler advised the Senate that "[s]ection 202 [(a)] of the pending bill . . . makes clear that the policy of the Congress is to deal fairly and impartially with transportation by motor carriers and to preserve the natural advantages of such transportation."\textsuperscript{20} He also described the fear on the part of some bus and truck operators that the Commission would not deal with them fairly and said that to safeguard these operators:

We specifically wrote into the bill, in the declaration of policy provision, and at other places throughout the bill, that the peculiar features of transportation by truck and by bus should be taken into consideration at all times by the Interstate Commerce Commission, and we put such provision in the declaration of policy.

The exercise of authority by the Commission under certain sections of the bill is directly related to the declaration of policy and the added provisions with respect to discrimination, preference, and unfair or destructive competitive practices lay a stronger and more definite basis for administrative action.\textsuperscript{21}

The debate concerning Senate Bill 1629 in the House of Representatives was led by Representative Sadowski. He described the hearings and the testimony taken by the Interstate and Foreign Commerce Committee of the House and the reports of the state utility commissions and stated that:

It is self-evident that there is a positive need for interstate regulation of motor carriers. Legislation over interstate motor carriers, to be practical, must conform with the principles of regulation now in effect in the 48 States which regulate common carriers and the 42 States that regulate contract carriers. The State commissions have asked Congress to pass this bill so that there may be harmony between States as to motor-carrier regulation and since 1926

\begin{thebibliography}{9}
\bibitem{18} 79 Cong. Rec. 5649-51 (1935).
\bibitem{19} Id. at 5651.
\bibitem{20} Id. at 5650.
\bibitem{21} Id.
\end{thebibliography}
Congress has had before it legislation of this character.\textsuperscript{22}

Representative Sadowski acknowledged that "the purpose of the bill is to provide for regulation that will foster and develop sound economic conditions in the industry, together with other forms of transportation so that highway transportation will always progress."\textsuperscript{23}

Finally, Representative Sadowski noted that states are empowered to grant or deny the use of their public highways but cannot regulate operations of interstate motor carriers. This hiatus of regulation resulted in abuses and problems for the state and federally regulated transportation services. He stated that:

In the case of Buck v. Kuykendall the court held that a State could not regulate motor carriers operating in interstate commerce, and that the matter of control of carriers in interstate commerce was entirely in the hands of Congress to provide for Federal regulation.

This decision left the door wide open. It permitted all sorts of abuses by irresponsible operators at the expense of the intrastate motor carriers and other transportation agencies who were under strict State and Federal regulation.\textsuperscript{24}

Not surprisingly, it was evident throughout the debate that strong pressure for the enactment of the legislation was coming from the states that were affected by the absence of regulation over the interstate transportation. It was observed that: "The regulatory bodies of the various states which are grouped together in a national organization, composed of the 48 state commissions, have investigated this subject. All of the state commissions, out of vast experience they have had, are now calling upon this Congress to pass this bill."\textsuperscript{25}

Clearly, the discretion given the Commission by Congress in interpreting section 203(b)(8) of the Act includes power to define the areas of expen1

\textsuperscript{22} 79 CONG. REC. 12,204 (1935).
\textsuperscript{23} Id. at 12,205.
\textsuperscript{24} Id. at 12,206.
\textsuperscript{25} Id. at 12,210. Representative Sadowski, in responding to questions concerning commercial zone and other exemptions in section 203(b) stated:

We felt that the Commission itself ought to have some power there to interpret this Act according to section 202, wherein we set down the policies to be carried out in the bill. It should have the power to interpret those three remaining exemptions [including commercial zones] in connection with section 202 so that we would not have somebody coming in by subterfuge, chiseling in, using these last three exemptions to break down the very things that we are trying to correct.

MR. FORD of Mississippi: Does the gentleman think it would be better for the Congress to decide what should be exempted rather than to leave it in the hands of the Commission that might nullify the entire intentions of Congress?

MR. SADOWSKI: We do that very thing. The Commission can only consider this in reference to the policy set down by the Congress in section 202. They have to take into consideration the policy of Congress.

Id. at 12,225.
empt commercial zones of municipalities or between contiguous municipalities or within zones adjacent to and commercially parts of such municipalities. Congress declared its intent that the exempt transportation is to be limited to movements locally or between contiguous municipalities or commercial zones and that these zones shall exist unless and to the extent the Commission is able to find they are consistent with the standards of the National Transportation Policy.  

The Commission, therefore, is required to consider the effect of the exempt zones upon these policy standards established by Congress. But has the Commission considered and issued findings from time to time that these zones "encourage the establishment and maintenance of reasonable charges for transportation services, without unjust discriminations, undue preferences or advantages, or unfair or destructive competitive practices," in accordance with the National Transportation Policy standard? Has the Commission cooperated with the several states to find if the presently constituted zones create or encourage the chaotic conditions and the abuses which caused states to propose and support the regulation of interstate motor carriers? Has the Commission made findings from time to time that retention of the zones has promoted safe, adequate, economical and efficient service, fostered sound economic conditions and encouraged fair wages and equitable working conditions?

INITIAL COMMERCIAL ZONE PROCEEDINGS

The first proceeding in which the Commission was required to interpret the intent and declared policy of Congress relative to commercial zones was St. Louis, Mo.-East St. Louis, Ill., Commercial Zone. It was initiated by the filing of a petition by Columbia Terminals Company of St. Louis, Missouri. That case was assigned MC-C-1, and involved the scope of the commercial zone of St. Louis, Missouri, and East St. Louis, Illinois, two cities which are separated by the Mississippi River. While that matter was pending, the Commission, on its own motion, commenced investigations to determine the areas embraced by the New York and Chicago commercial zones. Orders in the three proceedings were issued by the Commission concurrently on April 5, 1937. In the initial case, the Commission found that nothing intervened between the populated areas of St. Louis, Missouri, and East St. Louis, Illinois, except the Mississippi River, that they were connected by bridges over which there was a constant flow of vehicular traffic and that the two cities were contiguous. It limited the territory coming.

26. See notes 14 and 15 supra and accompanying text.
27. See note 14 supra, for the text of the National Transportation Policy.
28. 1 M.C.C. 656 (1937).
29. New York, N.Y., Commercial Zone, 1 M.C.C. 665 (1937); Chicago, Ill., Commercial Zone, 1 M.C.C. 673 (1937).
within the commercial influence of the municipalities to that in which transportation by motor vehicle was in the nature of an intraterminal or city-type movement, and excluded any areas between which the transportation was intracity in nature. Based upon these determinations, the Commission established a single commercial zone for St. Louis and East St. Louis, and specifically defined the bounds of the area commercially a part of that zone. However, it eliminated from that zone service to or from the contiguous city of Belleville, Illinois, upon finding that movements between it and East St. Louis were linehaul or over-the-road, rather than local or intraterminal transportation. The Commission stated:

We find that the application of all provisions of the Motor Carrier Act, 1935, to transportation by motor vehicle between Belleville, on the one hand, and points in the St. Louis-East St. Louis commercial zone, on the other, is and will be necessary to carry out the policy of Congress enunciated in section 202(a) and that the exemption with respect to such transportation provided in section 203(b)(8) should be removed.30

Predicated upon the guidelines set forth in the St. Louis-East St. Louis order, the Commission determined areas included in the New York, Chicago and Washington, D.C. commercial zones.31

In another 1937 decision, Los Angeles, Calif., Commercial Zone,32 the Commission concluded that two commercial zones should be created in the Los Angeles area. The main business area of Los Angeles was connected with its port by a narrow strip of annexed land, which was between one-half and three-quarters of a mile wide, and was described as the "shoestring" strip. No highway between Los Angeles and its port was entirely within the city limits and the primary routes between the two areas traversed both thickly and sparsely settled areas. The Commission found that movements between the main business and industrial areas of Los Angeles and its port were not local, but intercity, in character and should be regulated. It did so by dividing the considered area into a Los Angeles Commercial Zone and a Los Angeles Harbor Commercial Zone. Then, following its practice of defining the limits of the individual commercial zones as problems arose requiring investigation, the Commission established, during the period between 1939 and 1943, the limits of commercial zones of the cities of Philadelphia,33 Cincinnati,34 Boston,35 Kansas City,36

30. St. Louis, Mo.-East St. Louis, Ill., Commercial Zone, 1 M.C.C. 656, 663 (1937).
31. New York, N.Y., Commercial Zone, 1 M.C.C. 665 (1937); Chicago, Ill., Commercial Zone, 1 M.C.C. 673 (1937); Washington, D.C., Commercial Zone, 3 M.C.C. 248 (1937).
32. 3 M.C.C. 248 (1937).
34. Cincinnati, Ohio, Commercial Zone, 26 M.C.C. 49 (1940).
36. Kansas City, Mo.—Kansas City, Kan., Commercial Zone, 31 M.C.C. 45 (1941).
and a tri-city zone for Davenport, Iowa, and Rock Island and Moline, Illinois.\textsuperscript{37}

It was not until 1946 that the Commission ceased attempting to administer this exemption by specifically defining the commercial zones of individual and contiguous municipalities, based upon the particular facts affecting each zone. Nevertheless, it was still required to determine, formally and informally, whether the operations of a large number of carriers were within or without the zones of municipalities located throughout the United States.

**Ex Parte MC-37 (First Report)—Commercial Zones**

In 1943, the Commission instituted, on its own motion, a general investigation to determine the zones adjacent to and commercially a part of every municipality in the United States, other than those which had been previously determined. That same proceeding was also to include the investigation of the scopes of terminal areas of motor carriers and freight forwarders under the recently enacted section 202(c) of the Interstate Commerce Act. But, due to the complexity of the problems presented pertaining to commercial zones, consideration of terminal areas was postponed to a later proceeding.

At the conclusion of the investigation, a report and order was issued in *Ex Parte No. MC-37, Commercial Zones and Terminal Areas*, in which the Commission declared that its "piecemeal" approach to the commercial zone problem was impractical and that effective and uniform administration of the Act required a determination of the scope of the exemption as it applied to all municipalities as soon as possible.\textsuperscript{38} Until the limits of the commercial zones were defined, the Commission stated, there could be no wholly effective administration of section 203(b)(8).

Based upon the information developed in the investigation, the Commission concluded that the commercial zone of each municipality in the United States consists of:

1. the municipality itself hereinafter called the base municipality, (2) all municipalities within the United States which are contiguous to the base municipality, (3) all other municipalities within the United States and all unincorporated areas within the United States which are adjacent to the base municipality as follows: (a) when the base municipality has a population of less than 2,500, all unincorporated areas within 2 miles of its corporate limits and all of any other municipality any part of which is within 2 miles of the corporate limits of the base municipality; (b) when the base municipality has a population of 2,500, but less than 25,000, all unincorporated areas within 3 miles of its corporate limits and all of any other municipality any part of which is

\textsuperscript{37} Davenport, Iowa—Rock Island and Moline, Ill., Commercial Zone, 41 M.C.C. 557 (1943).

\textsuperscript{38} 46 M.C.C. 665 (1946).
within 3 miles of the corporate limits of the base municipality; (c) When the base municipality has a population of 25,000, but less than 100,000, all unincorporated areas within 4 miles of its corporate limits of the base municipality; and (d) when the base municipality has a population of 100,000 or more, all unincorporated areas within 5 miles of its corporate limits and all of any other municipality any part of which is within 5 miles of the corporate limits of the base municipality; and (4) all municipalities wholly surrounded, or so wholly surrounded except for a water boundary, by the base municipality, by any United States municipality contiguous thereto, or by any United States municipality adjacent thereto, which is included in the commercial zone of such base municipality under the provisions of (3) of this finding.39

The premise upon which the Commission based its ultimate finding was:

The limits of the commercial zone of each municipality should be determined in a manner to include, in addition to the area within its corporate limits, all other places or areas which, whether separately incorporated or not, are integral parts of the same business community, and to exclude all places and areas transportation between which and the base municipality is intercity in character.40

The Commission also stated that a commercial zone already exists about each municipality by reason of trade practices, the uses to which the area is put, and geographical and political considerations. The Commission’s function, it stated, is to determine the limits of zones which already exist, and not to create or establish commercial zones.41

By this decision, the Commission attempted to resolve all of the uncertainties concerning the applicability of the exemption, modified certain of its earlier guidelines, and invited any interested person to petition for determination of the limits of the commercial zone of any particular municipality in which the broad rule might prove inappropriate. To this end the important term “municipalities” was defined there to mean:

Only those cities, towns, villages, and boroughs which have been created by special legislative acts, or otherwise individually incorporated or chartered pursuant to general laws, or which are recognized as such under the constitution or the laws of the state in which located, and which have local governments.42

It further found that unincorporated townships or the New England type towns were excluded from this term;43 that the population of any municipality shall be the population determined by the last decennial census;44 and

40. 46 M.C.C. at 685.
41. Id. at 672.
42. Id. at 679.
43. Id.
44. Id. at 699.
that distance from the corporate boundary of the base municipality shall be the airline distance.45

Between the initial decision in Ex Parte MC-37 and the decision of December 17, 1976, there were twenty-eight supplemental reports in which thirty-nine commercial zones were specifically determined by the Commission. In addition, there were innumerable Commission formal and informal proceedings involving problems related to commercial zones and terminal areas.

EX PARTE MC-37 (THIRD REPORT)—TERMINAL AREAS

The 1943 notice of the Commission’s investigation of commercial zones, which resulted in the Ex Parte MC-37 (First Report),46 had for one of its purposes the determination of the maximum terminal areas for Part II motor carriers. However, because of the complex problems related to commercial zones, consideration of terminal areas was reserved for this later and separate proceeding. The order issued in this separate proceeding, Third Supplemental Report of the Commission in Ex Parte MC-37, Commercial Zones and Terminal Areas,47 determined the scope of terminal areas.

There were no terminal areas provided for in the Motor Carrier Act, 1935, and freight forwarders were not under the Commission’s jurisdiction until the enactment of the Freight Forwarder Act, 1942.48 The Interstate Commerce Act was amended to recognize terminal areas for motor carriers and freight forwarders in 1940 and 1942, respectively.49 Prior to the adoption of those amendments, however, motor carriers performing collection, delivery or transfer services that were deemed to be part of rail or railway express services were partially excluded from regulation under Part I of the Act.

Section 202(c) of the Act, exempting terminal area motor carrier operations, reads as follows:

(c) Notwithstanding any provision of this section or of section 203, the provisions of this part, except the provisions of section 204 relative to qualifications and maximum hours of service of employees and safety of operation and equipment, shall not apply—

(1) to transportation by motor vehicle by a carrier by railroad, subject to part I, or by a water carrier subject to part III, or by a freight forwarder subject to part IV, incidental to transportation or service subject to such parts, in the per-

45. Id.
46. Id. at 665.
47. 48 M.C.C. 418 (1948).
formance within terminal areas of transfer, collection or delivery services; but such transportation shall be considered to be and shall be regulated as transportation subject to part I when performed by such carrier by railroad, as transportation subject to part III when performed by such water carrier, and as transportation or service subject to part IV when performed by such freight forwarder;

(2) to transportation by motor vehicle by any person (whether as agent or under a contractual arrangement) for a common carrier by railroad subject to part I, an express company subject to Part I, a motor carrier subject to this part, a water carrier subject to part III, or a freight forwarder subject to part IV, in the performance within terminal areas of transfer, collection, or delivery service; but such transportation shall be considered to be performed by such carrier, express company, or freight forwarder as part of, and shall be regulated in the same manner as, the transportation by railroad, express, motor vehicle, or water, or the freight forwarder transportation or service, to which such services are incidental.\(^{50}\)

In the Third Supplemental Report in *Ex Parte MC-37*, the Commission concluded that neither section 202(c) nor any other section of the Act contains any definition of the terms "transfer," "collection" or "delivery service" or "terminal areas." It was assumed by the Commission that definitions were not included in the Act because these terms were regularly used and had accepted meanings in transportation parlance. "Collection" had been long-established as "transportation performed in the picking up, gathering together and assembling of shipments prior to a linehaul movement."\(^{51}\) Conversely, "delivery service" was that performed in the distribution of shipments to final destinations after the linehaul had been completed.\(^{52}\) The "transfer service," within the meaning of section 202(c), was deemed to be the movement of freight between the terminals of the same carrier in the same municipality or terminal area, or movements within such area from the dock or terminal of one carrier to the dock or terminal of a connecting carrier.\(^{53}\)

Although the Commission found that the words "terminal area" were not defined in the Act, it concluded that the meaning could be determined with reasonable certainty when examined in the light of earlier decisions of the courts and the Commission. Based thereon, it held that there were areas within which were performed collection, delivery, or transfer services incidental to some intercity or intercommunity linehaul transportation, and where terminal facilities were available and terminal handling occurred. "In other words," the Commission stated, "the 'terminal area' of a particular carrier at any municipality which it serves, within the meaning of Section...

\(^{50}\) 49 U.S.C. § 302(c) (1976).
\(^{51}\) 48 M.C.C. 418 (1948).
\(^{52}\) Id.
\(^{53}\) Id. at 421.
202(c), does not exceed the area within which bona fide collection, delivery, or transfer service, as distinguished from linehaul service is performed. The services were "essentially local in character and are confined to the particular municipality served and to such contiguous, or closely adjacent municipalities, or unincorporated areas as are an integral part of a business community."\(^{55}\)

Because these operations were found to be local and intraterminal and the same character of transportation as was performed in commercial zones, the Commission concluded that the limits applied to commercial zones should also be used to define the maximum limits of terminal areas. Upon these considerations, the Commission determined:

Subject to the limitations in its operating authority, the bona fide collection, delivery, or transfer services of any motor carrier or freight forwarder at any municipality authorized to be served by it, may be deemed to extend throughout the commercial zone of such municipality as defined by this Commission.\(^{56}\)

Thus, in this proceeding, the Commission initially established the coexistence of terminal areas and commercial zones. It declared that this policy "achieves a desirable uniformity and contributes in no small way to the simplification of regulation benefiting directly both carriers and public."\(^{57}\)

With respect to terminal areas, however, the Commission was required to consider the application of this exemption to unincorporated communities. Commercial zones under section 203(b)(8) are limited to municipalities. But section 202(c) is not so restricted. The Commission believed it was required to establish a relationship between unincorporated communities and municipalities, as well as a uniformity of the size of terminal areas for comparable unincorporated communities. It determined that it was required to establish some central point to describe the limits of terminal areas, rather than the outlying boundaries of the unincorporated communities. No suitable landmark could be found and the post office was selected as the central point to be used to determine the scope of a motor carrier’s or freight forwarder’s terminal area. The Commission held that a terminal area in any unincorporated community included all points within a fixed radius of the community’s post office. These areas included all points within 2 1/2 miles of the post office of an unincorporated community having a population of less than 2,500, within 4 miles, if it had a population of 2,500 but less than 25,000, and within 5 1/2 miles, if it had a

\(^{54}\) Id. at 422.
\(^{55}\) Id.
\(^{56}\) Id. at 423.
\(^{57}\) Id. at 433.
population of 25,000 or more.58

**Ex Parte MC-37 (Sub-No. 27)**

The previous sections of the article describe the development of and policies related to commercial zones and terminal areas, based upon the Commission's interpretation of Congress' intent and direction. This section will consider the report of the Commission, decided December 17, 1976, in *Ex Parte MC-37 (Sub No–26), Commercial Zones and Terminal Areas*.59

The significance of this proceeding is reflected in the considerable interest in the matter and the number of appearances made before the Commission.60 There were a number of appearances made by motor carriers supporting the proposed commercial zone expansion. They were primarily long-line carriers desiring expansions of their terminal areas, and having no direct interest in "local" commercial zone transportation. These carriers argued that the expansion was warranted by reason of a migration of business and industry to suburban areas located outside existing commercial zone and terminal areas. Expansion of these areas, it was contended, would result in extensions of their single-line through services thereby conserving fuel and resulting in lower transportation charges to shippers.

Conversely, many motor carriers (primarily short haul carriers) vigorously opposed the proposed expansion of the commercial zones and terminal areas. They alleged that there had been no significant migration of business and industry to suburbs and where such occurred it was to points beyond the limits of the proposed areas. The short haul carriers argued that the proposed expansion would be tantamount to deregulation which would open the expanded exempt areas to rigorous competition to the financial detriment of existing, authorized carriers. It was also contended that the proposed terminal area expansion for freight forwarders, would be similarly harmful to short line carriers.

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58. *Id.* at 435.
59. 128 M.C.C. 422 (1976).
60. Indeed, the Commission makes note of this fact in its decision stating:

A numerical breakdown of the representations indicates that 313 motor carriers have filed individual and joint representations and 13 motor carrier associations also presented their views. Two freight forwarders filed comments, and the Freight Forwarder Institute submitted evidence on its own behalf and that of its 26-member forwarders. Individual shipper and warehouse interests filed 63 representations, and 23 shipper associations and conferences presented their views. Various local interests (i.e., local governments, realtors, land developers, and Chambers of Commerce) filed 58 representations. Four state agencies have submitted written comments. Two labor unions, 144 individuals, one maritime interest, and one law firm also filed representations. Four members of the United States House of Representatives expressed views concerning our proposed commercial zone expansion on their own behalf and on behalf of their constituents.

*Id.* at 434.
A number of specialized motor carriers appeared in opposition to the proposed expansion. The National Automobile Transporters Association argued that by reason of the unique description of the operating authorities held by its carriers, motor carriers which do not hold certificates with such descriptions would be able to serve manufacturing plants which are outside the present commercial zones but within the proposed expanded areas, thereby diverting traffic from existing carriers. The National Tank Truck Carriers, Inc. (NTTC), represented bulk carriers of liquid commodities. Normally, this type of service does not involve transportation over great distances. NTTC believed that the Commission’s decision would result in almost total deregulation and at the same time deprive the shipping public of the safety in movement provisions that have heretofore been applied to the transportation of this traffic. The Movers and Warehousemen’s Association of America, Inc., representing transporters of household goods, argued that such expansion would only, without justification, increase the number of carriers, offer duplicating services, and result in ensuing traffic congestion, waste of fuel, air pollution and rate cutting.

In addition to the foregoing, many specific objections were addressed to the proposed expansion insofar as it applies to certain specifically named large cities such as New York, Chicago, Los Angeles, Portland, Seattle and Vancouver (Washington). To apply the rather broad-based population-mileage formula to these large metropolitan areas, it was contended, would cause great confusion, develop unbridled competition and, in effect, deregulate expansive population areas.

There were a large number of shippers which appeared in support of the proposed expansion. Their support was based upon their collective belief that the proposed expansion would decrease delays and loss and damage to shipments, and result in lower rates. Conversely, there were a number of shippers opposing commercial zone expansion. These particular shippers argued that the expansion would adversely affect the financial stability of existing small short haul carriers, and would create safety and claim problems.

A brief was submitted by the Short Haul Survival Committee, composed primarily of members of the Local and Short Haul Carriers Conference of the American Trucking Association, Inc. This committee submitted a detailed analysis of the problems, citing legislative history and the basic philosophy which has permeated prior Commission decisions relating to commercial zones and terminal areas, arguing that these exemptions apply only to “local” and “intra-community” movements of traffic. Ultimate approval of the proposed expansion, the committee stated, would create additional and unnecessary competition, would deprive shippers of protections they now have relative to loss or damage claims, safety, and prejudicial or
discriminatory rates, would adversely affect the human environment, and would cause severe financial damage to existing carriers.

As set forth above, in virtually each of the decisions which were issued prior to the promulgation of the *Ex Parte MC-37* decision referred to herein, the Commission uniformly took the approach that only traffic which was of an *intraterminal or city-type nature would be considered within the geographical ambit of a commercial zone*. Specifically excluded was transportation of an inter-city nature. This basic ideology was reaffirmed by the Commission in its initial decision in *Ex Parte MC-37 Initial Report*, but apparently was abandoned by the Commission in the decision of December 17, 1976, in the Sub-No. 26 proceeding. The word "abandoned" is applied purposefully, simply by reason of the fact that in the ninety pages of discussion in the latter decision, only three paragraphs are utilized to consider the long-followed "intra-terminal v. inter-community or inter-city test." It is also important to note that this brief discussion referred only to the subject of *overlapping* zones which of course has no real relevance to the previously espoused test. Such discussion also failed to consider the reality of the situation where different zones overlap, leaving to the motor carrier the choice of selecting any available zone that will permit the involved transportation outside the scope of Commission regulation. Such "choice" in effect further expands the geographical area immune from economic regulation by the Commission.

Yet another line of policy rulings espoused a basic principal which the Commission would appear to be dismissing herein. It was established that if a particular city experienced a rather significant or substantial increase in population during the period of time occurring between decennial censuses, an interested party could file a petition asking that, on the basis of such population growth, the scope of the commercial zone be extended commensurately. However, it is most important and indeed significant to note that the Commission, in considering requests for extensions based upon this particular set of facts, did not automatically grant these extensions on an arithmetical basis, that is, by simply adding up the population and applying the population-mileage formula to extend the area. The Commission quite unequivocally stated that in addition to the population growth, there must be shown some unusual or abnormal economic increase or development brought about by an extraordinary event, such as establishment of a large industrial complex. This is more akin to the reasoning utilized by the Commission prior to its recently adopted "slide

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63. *Id.*
rule" regulations and, of course, appears to be directly contrary to its opinions expressed in Ex Parte MC-37 (Final Report).

In order to understand the significance of the proposal insofar as it relates to increases in geographical areas free from economic regulation one need only draw maps of existing zones surrounding points of commercial interest, and then at the same time circumscribe the areas with descriptions of the areas which would be encompassed by the zones created under the new formula. Insofar as California carriers are concerned, the situation in Los Angeles probably most graphically and poignantly illustrates the geographical scope of the Commission’s proposal. The Los Angeles area was divided into two separate and distinct commercial zones. Under the new formula, that distinction is abolished and a commercial zone of vast area is established. It encompasses approximately two thousand square miles and virtually triples the geographical area now encompassed in the existing Los Angeles commercial zone. The new zone runs roughly from Ventura on the north, down the Pacific Coast highway to Balboa, a considerable distance south of Los Angeles. Pursuant to the Commission’s order, this entire geographical area is immune from economic regulation by this Commission.

A similar situation exists in the northern California area surrounding the San Francisco Bay. In light of the Commission’s ruling, a geographical area is created free from economic regulation that encompasses virtually the entire greater San Francisco Bay Area and extends to points in the east and south far outlying even the geographical confines of the San Francisco Bay itself.

And there is yet another point which compounds the geographical significance of the Commission’s proposal. While it is true that commercial zones may not be tacked or combined to effect a transportation service, it is also true that a carrier may select any available commercial zone that will permit the involved transportation. This was a subtle feature of the Commission’s decision that appears to have been overlooked by most parties.

The foregoing outlines the substantial and significant geographical expansion of areas which are now immune from economic regulation of this Commission by reason of the subject decision. In this context, it is also important to note that activity in these areas is totally free from any economic regulation whatsoever, for it has been unequivocally held that local and state agencies may not generate any regulation in existing commercial zones notwithstanding the fact that the Interstate Commerce Commission exercises no economic regulation therein.64

As argued by the short-haul carriers, implementation of the expanded commercial zones will bring about a diversion of traffic now being handled by existing, regulated motor carriers. Such diversion will come about in any number of ways. As an example, the Commission's decision obviously creates and/or otherwise establishes new more extensive authorities for the long-line carriers that will necessarily result in a diminution of their need for the services of existing short-line carriers.

Other traffic will be lost to presently unregulated local carriers which will extend their existing unregulated operations to the increased, expanded commercial zones formed by this decision. These carriers are not subject to any economic regulation and will make every effort to obtain whatever traffic they can divert from existing carriers, primarily through reduced rates. Some of the traffic that will be diverted to both the long-line and local, unregulated carriers will be the more profitable shipments, leaving the regulated short-haul carriers to handle the less attractive and less profitable movements.

The effect of the decision is an absence of any control either by this Commission or the local regulatory agencies, leaving a motor carrier to assess any charge it might wish for commercial zone shipments, discriminate between shippers or shipments, give extended credit periods, limit a shipper's rights relative to filing and processing claims and, generally, disassociate itself with any and all regulations promulgated for the protection of the shipping public.

JUDICIAL REVIEW

As noted, Ex Parte MC-37 was affirmed by an opinion of the United States Court of Appeals for the Ninth Circuit in Short Haul Survival Committee v. U.S.A. The circuit court considered and rejected each of the arguments advanced by the petitioners and affirmed the Commission's decision in all respects.

After initially outlining the pertinent statutory framework within which the appeal was considered, the court found that the Commission's decision was in effect a good faith exercise of its administrative rule-making authority. It went on to find that the Commission was not obligated to proceed by adjudication merely because its action affected carriers individually and in some cases adversely.

The court then considered the scope of its review of Commissions decisions. It emphasized that the scope of review is exceedingly narrow when considering a challenge to the "product" of a rule-making proceeding, and declared: "Our inquiry is limited to determining whether the Com-

65. 572 F.2d 240 (9th Cir. 1978).
66. Id. at 244.
mission's order is 'arbitrary, capricious, and abuse of discretion or otherwise not in accordance with the law.'" 67

The court discussed the rationality of the Commission's action. It cited as the best evidence of the rationality of the challenged decision the Commission's lengthy interim and final reports which were prepared before the issuance of the final decision, and the massive record upon which they were predicated. The court specifically found that these reports demonstrated that the Commission relied upon economic data which supported the ultimate conclusions. In replying to petitioners' argument that the revised population-mileage formula is arbitrary since it applies indiscriminately to all municipalities, the court adopted the Commission's line of reasoning that if any particular municipality objected to the expanded zone it could seek relief on an individual basis by filing an appropriate petition. 68

As to the subject of Congressional intent, the court rejected petitioners' claim that the Commission decision violated the intent of Congress in adopting the commercial zone exemption. It concluded that the Commission's decision is in full accord with the legislative purpose behind the commercial zone exemption of section 203(b)(8). The court opined that the Short Haul Survival Committee's argument to the effect that only "intramunicipal" carriage falls within the exemption is itself contrary to the plain language of the statute. On this particular issue, the court found:

"In Section 203(b)(8) Congress did exempt transportation carried out 'wholly within the municipality' from Federal regulation. It did not rest there, however, but went on to exclude from the Act's coverage transportation carried out 'within a zone adjacent to and commercially a part of' a base municipality. If these words mean no more than intramunicipal transportation they would be mere surplusage, a result which we do not think that Congress intended."

The court concluded that by reason of a substantial urban expansion without a corresponding increase in zone limits, the Commission found itself regulating local transportation which Congress had sought to exclude from its jurisdiction. It then found that the Commission issued the subject decision and adopted the challenged rules so as to avoid this jurisdictional interjection in to local commerce. 70

The court next considered the "adjacency" requirement of the exemption. Petitioners had argued that the newly enlarged zones include areas which are actually not adjacent to one another and which violate the criteria of the statute establishing the exemption. In rejecting this argument, the court held that the key relationship under the statute is the economic nexus between outlying points and the base municipality. It stated: "Two commu-

67. Id. (quoting 5 U.S.C. § 706(2)(a) (1970)).
68. Id. at 246.
69. Id.
70. Id.
nities which are neither geographically contiguous nor economically interdependent may nonetheless qualify for inclusion in a single commercial zone if both are "adjacent to" the same city." 71 It concluded that the Commission's decision cannot be found to be violative of the statute notwithstanding the fact that the expanded zones might include communities which are not in fact geographically contiguous to one another. 72

The argument that the Commission abused its discretion in concluding that the expansion would promote, rather than frustrate, the goals set forth in the National Transportation Policy was reviewed by the court. In considering this argument, the court gave much weight to the "overwhelmingly positive" shipper support for the expanded zones. Cited as reasons therefor were: (1) the fact that suburban shippers may now contract with exempt local carriers equalizing their position with shippers located in the previously zoned areas, and (2) the ability of long haul carriers to serve the same suburban shippers without the necessity of interlining. 73 The court also affirmed the rationality of the Commission's conclusion to the effect that expansion will result in lower rates, shorter transit times and reduced cargo damage for suburban shippers, thereby fostering the National Transportation Policy's stated goal of "economical and efficient service." It thus concluded that the Commission did not in fact act in an arbitrary or capricious manner in balancing the equities among competing interests in rendering its decision. 74

The court quickly dismissed petitioners' argument that the expansion promulgated by the Commission would adversely affect highway safety. It stated that since responsibility for highway safety has now been shifted to the Department of Transportation (DOT) and since that Department's jurisdiction extends to both regulated and unregulated carriers alike within and without the commercial zones, safety in operation will not in any way be affected by the Commission's decision expanding commercial zones. 75

Finally, the court concluded that the Commission's environmental impact statement was in compliance with the applicable terms and provisions of the National Environmental Policy Act (NEPA). In holding that the NEPA is essentially a procedural statute, the court stated that it was simply designed to make sure that the involved agency would be fully aware of the impact of its decision prior to the issuance thereof. The court concluded that it was satisfied that the Commission took a "hard" look at the environmental impact of commercial zone expansion and that it was fully apprised.

71. Id.
72. Id. at 247.
73. Id.
74. Id. at 248.
75. Id.
in the premises prior to the issuance of the decision.\textsuperscript{76}

Thus, the court affirmed every finding of the Commission on appeal.

**THE EFFECT OF COMMERCIAL ZONES AND TERMINAL AREA EXPANSIONS**

The commercial zone and terminal area expansions have been effective since March 29, 1978. What has been the effect of the expansion? Has the expansion promoted safe, adequate and efficient service; fostered sound economic conditions; encouraged the establishment of reasonable transportation charges, without unjust discriminations or preferences, or unfair or destructive competition; resulted in cooperation with the several states; and encouraged fair wages and equitable working conditions as contemplated by the National Transportation Policy? The United States General Accounting Office recently completed a study of the impact of the expansions of the commercial zones and terminal areas. It is not expected that its final report will be released for several months. The study involved a mailing of 3,000 questionnaires to carriers and shippers and about 250 on-site interviews. It has been anticipated that the study will determine that neither the dire consequences nor significant benefits predicted by the participating parties or the Commission are being experienced. The Commission’s Bureau of Accounts had criticized this study as being premature, believing the full impact of the expansion will not be determinable until a reasonable period after the court appeal has been concluded. Commissioner Christian, at the convention of the Short-Haul Carriers’ Conference of the American Trucking Association, on May 3, 1978, stated that the Commission is launching its own study to determine the effects of the commercial zone decision.

To determine the effect of the Commission’s decision for the purpose of this article, a limited investigation was made by contacting representatives of motor carriers, forwarders, and attorneys specializing in transportation throughout the United States.\textsuperscript{77} The correspondence and telephone conferences involved in this study resulted in receipt of reports and data which, generally, indicate the impact of the Commission’s decision. It is concluded therefrom in those instances where zone changes were measurable, that the predictions of both the proponents and opponents were correct. Certificated authorities of the short-haul carriers became less valuable, traffic was diverted from their operations, and some went out of business. Unregulated carriers expanded their services, cut rates for particular traffic and employed drivers at wages which the Teamsters Union and

\textsuperscript{76} Id. at 249.

\textsuperscript{77} The results of this investigation are on file with the authors and the Transportation Law Journal [hereinafter cited as Investigation]. Because of the confidential nature of the correspondence, the parties providing information in this investigation are not identified.
regulated carriers deem low and unfair. Long-line carriers, where economically feasible, expanded their direct services to the new terminal area points and the freight forwarders immediately extended their operations throughout those larger assembly and distribution areas. Such actions were predictable as they reflect normal business conditions and practices experienced in the transportation industry over many years.

A. QUANTIFIABLE EFFECTS

As predicted, there were reductions in the values of the short-haul carriers' certificates which are reflected by the current selling prices of these authorities. The Los Angeles Basin Territory certificates, which included the Los Angeles and the Los Angeles Harbor Commercial Zones, formerly were worth $60,000 to $80,000. Such an authority was recently advertised and offered for sale over a long period of time and eventually sold for $15,000. The Los Angeles Commercial Zone now covers an area of about 2,000 square miles. Local rights in the New York area were previously sold for $75,000 to $250,000. They now have little value. The present New York Commercial Zone embraces parts of the states of Connecticut, New Jersey and New York and has a population of approximately 19,000,000 people. Before the expansion, the Portland, Oregon/Vancouver, Washington Commercial Zone right was worth $15,000 to $20,000. Now these rights have little value. The certificates of registration to serve between the Chicago area and points in Illinois were priced between $175,000 and $75,000. They are currently worth about $45,000. The rights to serve the peddle areas proximate to Boston have dropped from a value of between $75,000 and $45,000 to between $22,500 and $18,000. Such losses are not suffered by large well-financed carriers. These rights are owned by small, local short-haul carriers which, generally, either held and operated under these authorities for many years or bought them over extended periods to meet the requirements of their customers.78

The long-line carriers have extended their peddle or pickup and delivery services to the new points and have developed new markets in the expanded areas. These extensions, however, have been dictated by economic considerations. Where it is advantageous to continue to utilize the regulated short-haul carriers for the terminal area pickups and deliveries, this has been done. Also, long-line carriers are providing portions of their terminal areas with direct service while other areas continue to receive interline service. In some instances, the short-haul carriers are tendered the small shipments and the long-line carrier effects the pickups and deliveries of the larger shipments with its own units. Certain of the long-line carriers

78. Id.
with broad authorities lost more than they gained through the Commission’s action. Though their terminal areas were expanded, they received new competition in their previously authorized territories by the expansion of the terminal areas of other carriers. No information was received that any linehaul rates were reduced because of the Commission’s decision, and it would be impossible to determine the effect of expansion upon damages to the involved traffic.

Freight forwarders have expanded their terminal operations to the new areas, continuing to employ the regulated short-haul carriers for their less-than-carload shipments unless an unregulated carrier is able to offer a comparable assembly or break-bulk service at a lower rate. Truckload movements of freight forwarders, shipper associations and consolidators are being transported by unregulated carriers.

The most immediate and expected reaction is the growth and expansion of the unregulated local carrier services in the extended deregulated zones. Boston will be used as an example of the effect of this expansion but it is similarly applicable to other metropolitan areas of the United States. The rate or charge of the regulated short-haul carriers was $112 for hauling a water-carrier container from a pier in Boston to a point within fifteen miles of that city. To provide this service, a union driver was employed at an average cost (including fringe benefits and taxes) of $12.85 per hour subject to an eight-hour minimum day. In the congested Boston area, it takes substantially all of an eight-hour day to provide this service. Thus, the labor cost alone for this transportation was about $102.80. Unregulated local carriers for the same transportation now charge $80 per container or trailer or more than $20 less than the direct labor cost of the regulated carrier. Similarly, in the San Francisco area, unregulated local carriers are charging about twenty percent less than the regulated short-haul carriers for hauling water-carrier containers.

The cost of labor is the principal difference between the operating costs of unregulated and regulated carriers. The total labor costs of an unregulated local carrier are about sixty percent of those experienced by the regulated short-haul carriers employing union drivers. Regulated short-haul carriers, generally, have been in business for many years, have substantial investments in facilities and rights and employ drivers under a Teamsters’ contract. On the other hand, unregulated local motor carriers usually have small, flexible operations and limited investments. They are able to avoid union contracts, union wages and fringe benefits. Often, unregulated carriers do not even have employees to per-

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79. id.
80. id.
81. id.
82. Author’s telephone conversations with San Francisco area carriers.
83. Investigation, supra note 77.
form the actual transportation as they utilize leased owner-operators who are paid a percentage of the revenues or a fixed fee for each shipment handled. When owner-operators are employed, the operating costs of an unregulated carrier are less than when an employee-driver is utilized for the same work.

Diversion of traffic from regulated short-haul carriers to unregulated local carriers, including owner-operators, is being experienced throughout the United States. However, this new competition is more apparent in the port commercial zones than in their counterparts in the inland areas. It is reported that conditions are chaotic at the New York Harbor area which embraces the ports of Newark and Elizabeth, New Jersey. The regulated short-haul carriers have been virtually eliminated from the hauling of shipments between these piers and the extended areas in the commercial zone. At the present time, a rate war is taking place in that harbor area. Reports were received indicating that certain mob or criminal elements may be taking control of the waterfront operations and that certain of this traffic is being obtained by payoffs and coercion.\(^4\) In the Chicago area, the transportation of water-carrier containers, steel, and piggyback trailers has been diverted to independent owner-operators. Similarly unregulated local carriers and owner-operators, through reduced rates, have taken over a large portion of the local commercial zone truckload traffic in the Philadelphia, Baltimore, Seattle, Los Angeles, San Francisco and Boston areas. It is reported that the small shipment service from Detroit to its airport, which formerly was shipped via regulated short-haul carriers, is now being transported by unregulated carriers.\(^5\)

**B. Uncertain Limits of Commercial Zones and Terminal Areas**

Another problem which is being experienced in all areas is the confusion and uncertainty as to the limits of the respective commercial zones and terminal areas. It is virtually impossible to specifically determine the limits of the commercial zones in the heavily populated metropolitan areas. The extensive New York Commercial Zone embraces parts of three states. Enlargement of the Los Angeles zone embraces a land area of over 2,000 square miles. The Providence, Rhode Island Commercial Zone includes seventy to eighty percent of the population of that entire state. The city of Jacksonville, Florida, which embraces 827 square miles, has a zone of over 2,000 square miles reaching into the State of Georgia. In our newest state, Alaska, the capitol city of Juneau has 3,108 square miles within its boundary. This problem is compounded by the right to select any available commercial zone that will expand the deregulated area and extend an

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84. Id.
85. Id.
exempt operation. For example, the San Francisco Commercial Zone reaches fifteen miles south toward San Jose. But by selecting the Fremont zone, which touches the city limits of both San Francisco and San Jose, the north-south limits of the exempt area extends a distance of sixty miles and embraces both of these heavily populated municipalities. Problems are also being experienced in determining the scopes of the newly authorized terminal areas. Long-line carriers are publishing descriptions of their new terminal areas only to find that other carriers have adopted larger areas in their tariffs. To resolve this problem, carriers are adopting the most extensive terminal areas published by any of their competitors. Obviously, the Commission has created a regulatory monster that will be difficult to control or regulate.

The study has disclosed that unregulated or exempt operations were not confined within the limits of commercial zones prior to the expansion. With the extension of these areas, the Commission’s problem of confining the unregulated services to the exempt zones will be greatly aggravated.

C. SAFETY REGULATION

The Commission and the Ninth Circuit Court of Appeals gave short shrift to the issue of safety. They declared that it is the responsibility of the Département of Transportation’s Federal Highway Administration but neither the Commission nor the court advised the Federal Highway Administration of how it may find these exempt carriers. As early as the congressional debates which resulted in the enactment of the Motor Carrier Act of 1935, Congress recognized the obvious fact that there cannot be an enforcement of regulations unless carriers are regulated. Included in the House debate is the following statement of Commissioner Eastman on this point:

[T]he regulation of motor vehicles will involve many practical difficulties, chiefly resulting from the fact that there are many individual operators. It is not like the case of the railroads where the companies are large. There are thousands of operators of motor vehicles, and many of them operate only one or two trucks. Practical difficulties will arise in locating the carriers and also in enforcing regulations with respect to them.

The requirement for registration with state commissions by interstate motor carriers exempt from regulations by the Interstate Commerce Commission does not produce the needed data to locate unregulated commercial zone carriers. Unregulated commercial zone interstate carriers do not register with the state commissions or comply with their insurance and other requirements. The State of California has over 20,000 individually licensed motor carriers and it is estimated that at least twenty-five to forty percent

regularly or occasionally provide exempt commercial zone services. Only eighty of these carriers are registered with that Commission as exempt interstate commercial zone carriers.86 Commercial zones are known in the industry as the "graveyard for equipment." When vehicles are no longer able or capable of regular highway service, they are used for these local operations. It is the obligation of the Federal Highway Administration to require exempt interstate carriers to comply with safety regulations pursuant to Part II of the Interstate Commerce Act. However, under the existing situation, it is difficult to exercise any effective safety controls over these carriers.

D. OTHER IMPACTS

Many other related matters will be affected by changes in the commercial zones and terminal areas which are either not measurable or which will require more time before an impact can be gauged. As indicated in the legislative history of the commercial zone exemption and in the congressional debates described above, it was of primary concern and importance in enacting the Motor Carrier Act of 1935 to establish a harmony between the states and federal government with respect to motor carrier regulation. The lack of state or federal control over interstate operation resulted in the following situations: "It permitted all sorts of abuses by irresponsible operators at the expense of the intrastate motor carriers and other transportation agencies who are under strict state and federal regulation."89 Representative Merritt advised the House of Representatives that:

So far as I know, these [state regulatory] bodies have been sufficiently successful in state regulation unanimously to recommend Federal regulation of interstate business, and they point out that one of the principal difficulties that they have encountered is in the interference of unregulated interstate vehicles with the state regulated intrastate buses and trucks.90

Under the decision of the Commission considered herein, this situation has been reestablished. Broad territories in and adjacent to all metropolitan areas in all states have been deregulated by the federal government. Within those areas, interstate commercial zone carriers are subject to no regulation while the intrastate motor carriers are regulated by state commissions.

The question of whether deregulation of motor carriers in the exempt zones and regulation of carriers outside the zones will result in rates that are preferential, discriminatory and/or destructive cannot be determined at this time. Further, any violations in this character are and will be difficult to determine and prove unless actual audits are made of the records of the

86. Based upon impromptu survey by California Public Utilities Comm'n, License Branch.
90. Id. at 12,207.
involved carriers and shippers. The Commission presently does not have the means or personnel to conduct such audits.

With the deregulation of the commercial zones, antitrust matters become an element of concern. No report that was received suggested that an antitrust problem has arisen related to the expansions. An antitrust problem may exist, however, for motor carrier rate bureaus that hold section 5a exemptions from the Interstate Commerce Commission and publish rates covering commercial zone movements. A bureau's fixing of rates would be unlawful except for the section 5a exemptions. With the deregulation by the Commission of the commercial zone transportation there may be an issue of whether the prices or rates are lawful for these movements as established and published by rate bureaus. The rates and operations of motor carriers exempt from the Commission's regulation are not subject to Part II of the Interstate Commerce Act. If the fixing and publication of these commercial zone changes are not subject to Part II of the Act, then the section 5a antitrust exemption does not apply.

CONCLUSION

This article has traced the genesis, development and past and present Commission policies relative to commercial zones and terminal areas. Based thereon, it is expected that further consideration will be given this subject because of the many problems that have been and will be raised by the considered decision. The Commission, as found by the appellate court, weighed the arguments for and against the expansions and deregulation and concluded that the overall benefits to the public of "more single-line service and greater flexibility of local operations within terminal areas" justify this action. Therefore the considered decision now has the imprimatur of the United States Circuit Court of Appeals and will govern until modified by the Commission.

The significance of the effect of the decision and the wide interest of the transportation industry in commercial zones and terminal areas and related problems will not permit the matter to rest for long. As noted above, the United States General Accounting Office made a study and the Interstate Commerce Commission soon will commence its investigation of the act of the expansion and resultant deregulation. These studies are expected to demonstrate that the linehaul motor carriers and freight forwarders have extended their terminal area operations. They will further show

93. 572 F.2d at 248.
that there has been a substantial loss of commercial zone and terminal area traffic by the regulated short-haul carriers to unregulated motor carriers, that this diversion is the result of the lower rates which are attributable to lower employee and equipment costs of the latter carriers. The large numbers of unregulated carriers operating in the very extensive commercial zones in all metropolitan areas of the United States will be of great concern to the various regulatory agencies, including the state commissions and the Department of Transportation, and to carriers and shippers. These agencies and entities and the Commission will undoubtedly be impelled to again weigh the benefits of this expansion and deregulation against the problems resulting therefrom.

For these reasons, the recent decision of the Commission on this matter is but a chapter in the unfinished history and development of commercial zones and terminal areas.
Work in Progress—The Latest Solution to the Small Shipment Problem

ROBERT E. McFARLAND*

I. INTRODUCTION

The quest of the Interstate Commerce Commission for a solution to the age-old "small shipment problem" continued unabated in 1978. The most recent tome on the subject, entitled Ex Parte No. MC-98, New Procedures in Motor Carrier Restructuring Proceedings, is the result of a voluminous rulemaking proceeding commenced by notice served January 7, 1976. Simply stated by the Commission, the rulemaking had "the purpose of solving what has been referred to as the 'small shipments' problem.'"1

The culmination of that rulemaking proceeding was the issuance of several recommendations by the Commission, with regard to the treatment of small shipments, as well as the institution of two additional rulemaking proceedings.2 The two rulemaking progenies of this multi-year proceeding included one investigation into the classification system, as utilized by the motor carrier industry,3 and a rulemaking proceeding on released rates in

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2. Id. at 135-36.

3. Ex Parte No. MC-98 (Sub-No. 1), Investigation of Motor Carrier Classification System (Interstate Commerce Comm'n, April 10, 1978).
conjunction with a small shipments tariff. The purpose of this article is to analyze the conclusions of *Ex Parte No. MC-98*, in light of the history of the small shipment problem in the motor carrier industry, from both a service aspect and a rate aspect. It is from these two separate, but interrelated, areas that the small shipment problem appeared as a troublesome controversy with service a continuing complaint from the vantage point of the shipping public and inadequate rates and charges a vexing issue to the motor carrier industry. The Commission has capsulized, repeatedly, the point of view of the shippers, the carriers, and indeed, the perplexed regulatory body itself in past pronouncements. From the shippers' point of view, the lack of adequate transportation of small shipments of small shippers at small communities is a problem of monumental proportions and continuing duration. Here, independent motor carriers show minimal interest in all of the involved traffic except that of a few shippers at . . . larger cities . . . It is clear that any effective solution to the problem must include the development of reliable and continuous motor service to small communities. Effective regulation must include the authorization of for-hire motor service which will ameliorate the distressing and long-lamented plight of such small shippers.

On the other hand, the motor carriers "speak of the small shipment problem and submit that the chief cause of the difficulty is that the vast majority of the smaller weighted shipments, particularly those weighing less than 500 pounds, are transported at noncompensatory rates." Voicing its own difficulties in attempting to reconcile these two polar viewpoints, the Commission has stated: "In recent years the problems associated with the transportation of small shipments have become among the most troublesome and difficult of those with which the transport agencies and the Commission have to deal."

The Commission's latest solution to the confusing issues involved in the transportation of small shipments can best be evaluated, then, in light of an historical framework of small shipment service, and the cost of providing that service.

II. MOTOR CARRIER SERVICE IN THE TRANSPORTATION OF SMALL SHIPMENTS

The crucial nature of motor carrier service, in the area of small shipments, is underscored by the fact that motor carriers are the primary mode of transportation of such shipments. Not only are they the most common mode but, in many cases, they are the only means of transportation available to shippers. It is not a new development that shippers have relied

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upon transportation means other than rail to move their small shipments. As the Commission noted in *In Re Express Companies*, the very first pronouncements on the unique characteristics of the transportation of small shipments,

Railroad companies prefer that freight in small parcel and of the nature in other respects considered appropriate to the express business, especially when quick transit is essential, should be handled by those agencies. The public is no doubt better served by them in some respects than it would be by the ordinary methods of rail transportation.10

This disaffection between rail carriers and the small shipment did not necessarily mean that the nascent motor carrier industry would look upon the small shipment field as one attractive to it. In fact, in the years immediately following the passage of the Federal Motor Carrier Act,11 motor carriers exhibited little interest in the transportation of small shipments, as the Commission noted at the time.12 The sole surviving express company at that time, Railway Express Agency, Inc. (REA), had had its traffic diverted, not by motor carriers, but by the Parcel Post, on small shipments.13 The motor carriers, then, came to the small shipment field later, and virtually by default, as the rail carriers discontinued their less-than-carload (LCL) service and reduced greatly the territory that they served, while their surviving express company, REA, in the face of an ever-dwindling volume of freight, became less and less able to provide the shipping public with an adequate service.

As conditions changed, so too did the definition of the "small shipment." Thus one study as late as 1974 reported that the Commission was still basing its small shipment definition on the railroad LCL weight break of 10,000 pounds or less.14 Yet, in a 1954 proceeding, the Commission referred to small shipments as those weighing under 5,000 pounds.15 One Commissioner, dissenting in that proceeding, argued that small shipments should be those weighing not more than 300 to 350 pounds.16

9. I.C.C. 349 (1887).
10. Id. The Commission held that "so-called" independent express companies, i.e., independent from rail carrier control, were, albeit regretfully, outside the coverage of the Interstate Commerce Act, 49 U.S.C.A. § 10101 (West Supp. 1979).
12. Express Rates, 1938-1939, 231 I.C.C. 471 (1939). In this proceeding, the Commission noted that Railway Express Agency, Inc. (REA) had, unlike motor carriers, traditionally been "a carrier of small packages and its organization and operations have been developed accordingly." 231 I.C.C. 471, 499.
13. Id. at 498.
14. AMERICAN UNIVERSITY, SMALL SHIPMENTS—A MATTER OF NATIONAL CONCERN 3 (1974). That study suggested that "for practical purposes, we can accept shipments between 50 and 750 pounds as 'small shipments' requiring special handling." Id. at 4. Any shipment under 50 pounds, according to the study, was a parcel.
16. Id. at 205 (Comm'r Arpaia, dissenting).
No. MC-98, however, the Commission determined that "[t]he problems which are of primary concern affect shipments weighing 500 pounds and under." Accordingly, the Commission determined that small shipments now are those which fit within that classification. As is obvious, the handling and other characteristics of a shipment do not change magically when it increases in size from 500 pounds to 501 pounds. Yet this line-drawing by the Commission is in keeping with many recent rate proposals with regard to the pricing of small shipments and is a reference point, albeit arbitrary, for the measurement of the small shipment.

As motor carriers began to handle more of this traffic, service problems surfaced. As a result, the Commission began to issue certificates of public convenience and necessity to motor carriers desiring to specialize in the transportation of small shipments. These operating rights application proceedings themselves traced the service problems encountered by shippers in the handling of small shipments. Indeed, the shipping public recited a virtual litany of horrors against the service being received from existing carriers. In United Parcel Service, Inc., Common Carrier Application, the shipping public complained of exorbitant minimum charges, both at the hands of REA and motor common carriers. The supporting shippers in that proceeding also pointed to the advantages of a daily pickup, utilizing the United Parcel Service (UPS) system, as well as a next day delivery. In granting the applicant a certificate of public convenience and necessity after evaluating the statutory criteria in the Act, the Commission analogized the minimum charges then in effect by motor carriers to an embargo of the traffic.

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17. Restructuring Proceedings, supra note 1, at 3.
18. See Restructured Rates and Charges, Central States Territory, 352 I.C.C. 502 (1976); Small Shipment Rate Revision, Central and Southern Territory, 337 I.C.C. 158 (1970). These two rate proposals focused on shipments weighing less than 500 pounds (i.e., 499 pounds or less).
19. These application proceedings by motor carriers do not all involve requests for and the issuance of authority limited to the transportation of shipments weighing not more than 500 pounds from one consignor to one consignee in a single day (the common wording utilized by the ICC in restricting a grant of authority to "small shipment" traffic). To the contrary, one small shipment grant may be limited to shipments weighing less than 100 pounds, as in United Parcel Service, Inc., Com. Car. Applic., 68 M.C.C. 199 (1956), while another may be limited to shipments weighing less than 1,000 pounds, as in Allied Delivery Sys., Inc., Ext., Small Shipments—Mich., 120 M.C.C. 110 (1974).
20. 68 M.C.C. 199 (1956).
21. The general freight carrier minimum charge on a shipment was then about $3.00; the REA minimum was at $1.80, while UPS was at 24¢ for a one pound package. United Parcel Service, Inc., Com. Car. Applic., 68 M.C.C. 199, 203 (1956). The disparity today between the UPS rate and general freight carrier rate is even greater, with the UPS rate being 1/20 that of the freight carriers in some instances. However, as the size of the shipment increases, the disparity between the two levels decreases substantially.
23. United Parcel Service, Inc., Com. Car. Applic., 68 M.C.C. 199, 204 (1956). This deci-
Features of UPS in the movement of small shipments that were not available to the shipping public through Parcel Post or REA were cited in United Parcel Service of New York, Inc., Common Carrier Application.24 The Commission there pointed to what shippers in that proceeding termed service advantages of UPS, including (1) daily pickup of small shipments, (2) faster delivery on small shipments, (3) signed delivery receipts, (4) $100 coverage per package, under the released rates authority of UPS, (5) the automatic return of refused or rejected small shipments without charge, (6) three attempts at delivery, if the consignee was not at home, (7) the acceptance of both checks and cash on C.O.D. shipments, (8) the prompt tracing of shipments, and (9) the less rigid packing requirements of UPS.25 The Commission only referred in passing to the service offered by motor carriers on small shipments, but had nothing good to say about such service. It entered a disclaimer as to viewing the application as a "contest" between UPS and Parcel Post. However, the Commission noted that it could not "overlook the realities of the situation, and in particular, the vast amount of traffic now moving in the inferior service of Parcel Post mainly due to the prohibitive cost of using other modes of transportation."26 That so many shipments were moving via Parcel Post, in the Commission's opinion was "an indictment of existing services in the small package field."27

In affirming the Commission's grant of the certificate to operate, Judge Friendly, authoring the opinion of a statutory three judge district court, stated:

The evidence of the shipper witnesses, painstakingly reviewed in the report of Division 1, shows that UPS was offering not simply a cheaper but a better mousetrap. It was better thanParcel Post because of the pickup, assured delivery times, repeated attempts to effect delivery, and other features . . . it was better than any service offered by existing motor carriers because although some of these carriers may have duplicated some particular feature of applicant's proposed service, none offered one so flexible and complete.28

The Commission had, long before these United Parcel Service proceedings, recognized the differentiating features involved in retail store delivery, which again generally involved the handling of small shipments. In fact, UPS itself was one of the first carriers to benefit from the receipt of a retail store delivery grant of authority.29 The Commission held repeatedly that the granting of retail store delivery authority would not be unduly detri-
mental to the services of regular route general commodities common carriers. 30

The packages transported by UPS in its common carrier service grew rapidly from a level of 5,921,228 in 1951 to 63,908,677 by 1959. 31 In 1952, only 2,113 shippers were receiving a daily pickup from UPS, but that number had grown to 31,569 by 1959. 32 The Commission continued to view UPS' chief competition as the Parcel Post although REA strenuously objected that its express service was being jeopardized by the diversion of freight. REA even argued that the dilution of available traffic among different carriers was a major cause of the small shipment problem. 33 The Commission continually held that "the proposed service (of UPS) will not result in appreciable diversion from REA ...." 34

While UPS continued to receive additional grants of authority, and, concurrently, to expand its service area, 35 other motor carriers were also specializing in the transportation of small shipments. The shipper complaints made in these proceedings were similar. In one proceeding, the Commission referred to delays in transit on small shipments, damaged shipments resulting from excessive handling, tracing difficulties, claims processing difficulties, frequently missed pickups, the absolute refusal to handle small shipments, the refusal to make inside deliveries to small shops and factories, as well as homes, and the refusal to provide a protective service during the winter months on freezeable commodities. 36 Reference in these cases was frequently to motor carrier service, as opposed to the service of REA or Parcel Post. Thus, in an application granting a freight forwarder small shipment authority, the Commission stated: "The most persistent and vexing problems appear to occur because of the motor carriers' reluctance to handle so-called 'small shipments', .... excessive de-

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32. Id.
33. Id. at 726.
34. Id. at 741.
lays in transit; and poor unreliable claims and tracing services." The Commission went on to summarize the numerous difficulties experienced by the public witnesses with regard to the movement of small shipments by the vehicle of motor common carriers, stating:

The major problems encountered are split deliveries, inadequate claim service, poor tracing of shipments, delayed and excessive transit times, almost prohibitive rates, and refusal of many motor common carriers to handle shipments. More specifically, it appears that all of the pieces of a multipiece shipment are all too often not delivered simultaneously. Claims regarding damages and lost shipments are handled slowly, if at all. Tracing the whereabouts of small shipments is, at best, time consuming, cumbersome, and expensive. Transit times from pickup to delivery are greatly in excess of that which can be tolerated by shippers and consumers in a competitive market. Finally, carrier refusals to handle small shipments take the form of prohibitive rates, intolerably slow service, and even outright refusal.

Based on records such as this, numerous motor carriers seeking to specialize in the transportation of small shipments were granted authority in that area. In fact, some of these small shipment specialists were even able to successfully oppose encroachments by UPS into their service areas.

The Commission had occasion to address the small shipment problem not only in operating right cases, but also in other investigative or rulemaking proceedings. Thus, in Restrictions on Service by Motor Common Carriers, the Commission scrutinized the problems of restrictions placed in tariffs to evade service on small shipments by common carriers. The Commission there stated:

By way of background, it is evident that some degree of motor carrier selectivity of traffic by means of self-imposed service limitations, through the use of tariffs and of other means, is not a new innovation. An awareness of the existence of such questionable conduct more recently generated two complimentary reports on what is now commonly referred to as the "small shipments problem."

The restrictions which the Commission examined generally were aimed at cutting back on small shipment service altogether, or on traffic originating...
or terminating at points in rural or relatively inaccessible areas. As a result of the proceeding, the Commission promulgated a new rule prohibiting carriers from restricting service in tariff provisions to less than the carrier’s full operating authority.\textsuperscript{43}

The Commission had occasion to address the small shipment problem frequently in its Annual Reports.\textsuperscript{44} Also, an Ad Hoc Committee of the Commission reported on the small shipment problem in 1967. It cited numerous shortcomings among motor carrier service, including (1) withdrawal of service from low traffic density points, (2) service inadequacies in small towns and cities, (3) carrier inability or unwillingness to interline on small shipment, (4) carrier avoidance of small shipments, and (5) cessation of service to cities not on the interstate highway system.\textsuperscript{45}

This, then, was the regulatory background, in terms of service, existing at the time that the Commission issued its notice of rulemaking in \textit{Ex Parte No. MC-98}.

\section*{III. Costs and Rate Problems Inherent in the Handling of Small Shipments}

It was recognized by the Commission, early on, that small shipments were treated differently from a rates and charges standpoint than heavier weighted shipments, at least where express shipments were concerned. As early as 1887, for example, the Commission stated: “It is known, moreover, that in the express business there is very little classification of freight, the tariffs being usually on a uniform basis for 100 pounds . . . .”\textsuperscript{46}

Not only were such shipments treated differently on a rates and charges basis, but, with the advent of the motor carrier industry, the Commission pointed out that the only way motor carriers regarded the small package traffic as profitable was “at rather high minimum rates.”\textsuperscript{47} Even though small shipments were moving via motor carriers at a rate higher than that charged by Parcel Post, there was still a substantial question as to the profitability of those small shipments. In the years immediately following the conclusion of World War II, the Commission expressed repeated concern about the revenue derived from the handling of small shipments in a period

\begin{footnotesize}
\begin{enumerate}
\item 43. 49 C.F.R. § 1307.27(k)(1) (1977).
\item 45. AD HOC COMMITTEE OF THE COMMISSION, ICC BUREAU OF ECONOMICS, SMALL SHIPMENT PROBLEM (1967).
\item 46. In Re Express Companies, 1 I.C.C. 677, 682 (1887).
\item 47. Express Rates, 231 I.C.C. 471, 499 (1939).
\end{enumerate}
\end{footnotesize}
of rampant inflation. In one proceeding approving a dramatic increase in minimum charges applied on small shipments, the Commission correctly predicted that "reasonable minimum charges for the future will be substantially higher than the prior minimum charges." A history of this pricing and revenue dilemma since that time reveals the Commission as a foot-weary referee placed between two uncompromising and stubborn combat-ants in the shipper and the motor carrier interests. They have fought over the quality of service. They have tangled over the level of rates. They have spared over the profitability of transporting the shipments themselves. Each new rate plan designed to price small shipments that was, in the opinion of the motor carrier, compensatory for the costs of providing that service was vigorously opposed by shipper groups.

The dispute itself, in the Commission's view, had its origin in numerous factors common to small shipments. For one thing, the Commission believed that such shipments required more handling. It was also believed that the pickup and delivery facilities of consignors and consignees, respectively, were inadequate. Frequently, small shipments involved consumer goods, as opposed to industrial products. Motor carriers were more likely to encounter traffic congestion in making such pickups and deliveries. Additionally, the smaller shipments were more susceptible to loss and damage than the larger, heavier shipments. There was a pronounced need for expedited service in the transportation of small shipments. There was also a problem in developing effective systems to trace small shipments.

In one of its earliest responses to a motor carrier proposal relating to the revision of the rates to be applied to small shipments, the Commission recognized that the cost differences between the handling of a small shipment and the handling of a larger shipment could be attributed principally to the carrier's higher cost of terminal handling services associated with the smaller shipment. Such elements of carrier costs in transporting small shipments as picking up, handling, and delivering the shipment were independent of the weight of the shipment itself. In the Commission's opinion, the costs of such elements were several times as great per 100 pounds for a 100 pound shipment as for a 1,000 pound shipment. The entire matter was accentuated by the inflationary growth of wage costs at a rate faster than that of other transportation costs.

49. Minimum Charges in Central Territory, 47 M.C.C. 259, 276 (1947).
50. Surcharges on Small Shipments Within Central States, 63 M.C.C. 157, 168 (1954).
51. Id. at 168-69.
52. General Increases, Eastern Central Territory, 316 I.C.C. 467 (1972).
53. Id.
54. Id. For an earlier recognition of the same trend, see Central Territory Gen. Increases, 49 M.C.C. 4, 9 (1948).
Accompanying this trend was a change in the balance between the amounts of small shipments handled by rail carriers and those handled by motor carriers.\textsuperscript{55} The LCL traffic of the rail carriers was decreasing significantly during the late 1950's and early 1960's, with motor carriers being tendered more and more small shipments.\textsuperscript{56} The motor carriers viewed their burden as being more oppressive when the rail carriers began to draw off the lucrative truckload (TL) traffic by the institution of trailer-on-flatcar (TOFC) service.

In the course of ruling on one small shipment rate proposal, the Commission commented on this rail-versus-motor development and its concomitant effect on motor carriers.

For several years, the transportation of the so-called small shipments by motor common carriers has represented a perplexing problem to the carriers, the shippers and the Commission. The successful inauguration by the railroads of trailer-on-flatcar (TOFC) service concurrently with the general elimination of the less-than-carload (LCL) service, made the movement of freight shipments weighing less than 10,000 pounds, and particularly those less than 1,000 pounds, an increasingly significant part of the traffic of the motor carriers. The TOFC service forced the motor carriers to reduce their rates on truckload traffic to be more competitive, and the resulting loss of revenue necessitated a review of the pricing on the other segments of the traffic. This review led the carriers to the conclusion that the rate structure would have to be revised to more narrowly reflect the cost of transporting the different traffic segments if they were to maintain the capability of performing an adequate service on all traffic.\textsuperscript{57}

The respondent in that proceeding, Eastern Central Motor Carriers Association, Inc. (ECMCA), on behalf of its member carriers, maintained adamantly that, although the railroads had discontinued their LTL service, there had been no corresponding shift to other modes of transportation, such as the freight forwarders or REA. Accordingly, the shippers were dependent upon the motor carrier for the transportation of small shipments, but the transportation of such shipments by the motor carriers, especially shipments under 1,000 pounds,\textsuperscript{58} were responsible for the operating deficits of the motor carriers.\textsuperscript{59}

Various suggestions were made to reduce costs on small shipments. At the most basic level, the Commission urged that shippers and carriers cooperate in that regard. It was suggested that the better planning and scheduling of shipping and receiving department operations would also assist in obtaining the goal of lowering the costs of providing the small shipment service. If such departments could be open longer hours, it was felt,

\textsuperscript{56} Small Shipment Rate Revision—Eastern Central Territory, 335 I.C.C. 547, 549 (1969).
\textsuperscript{57} Id. at 548.
\textsuperscript{58} Again, the weight criteria for the definition of small shipments has undergone a downward metamorphosis. See text accompanying notes 14-18 supra.
\textsuperscript{59} Small Shipment Rate Revision—Eastern Central Territory, 335 I.C.C. 547, 552 (1969).
an improvement would also be noted.\textsuperscript{60} Similarly, the availability of additional dock space by shippers could cut carrier costs, as could the sorting of shipments according to designated carriers. Other cases recognized that the manner in which small shipments were handled by motor carriers, in providing cross-dock terminal service, could affect the costs of handling such shipments.\textsuperscript{61}

The various rate bureaus, upon being confronted by this economic crisis, submitted numerous rate proposals to the Commission to alter substantially the charges on small shipments. In addition to setting forth what they believed to be the economic merits of their respective proposals, the bureaus occasionally included veiled threats with regard to the future quality of small shipment service that would occur unless rate restructuring were allowed. For example, one carrier noted that it had

made every effort to contain our costs without sacrificing our service. We have modern terminals, the latest equipment and good personnel. Our I.B.M. model 360 computer provides us with the latest data and information so that we can pin-point any cost that goes out of line, yet in spite of this, we find the costs of doing business increasing to the extent we need this additional revenue on those shipments which we are losing money on. The lack of such an increase could only mean the sacrifice in the service on that segment of traffic that is costing us money to operate and handle.\textsuperscript{62}

Other carriers were more subtle in their evidentiary submissions. For example, one carrier’s representative stated that, if the Commission were to allow a restructuring of the small shipment traffic so that rates were increased on shipments weighing less than 500 pounds, then "[s]uch a step would also tend to improve service on small shipments in general. With the return more in line with the cost of handling, the service problem on small shipments would largely resolve itself."\textsuperscript{63}

Numerous proposals were submitted by the various rate bureaus in order to reduce, or eliminate altogether, the deficit experienced by motor carriers in the handling of small shipments. One of the first proposals involved the designation of "constant charges" on shipments weighing 300 pounds or less.\textsuperscript{64} The Commission there held that: "The increases on this traffic are clearly justified in order to minimize the subsidization of this traffic

\textsuperscript{60} 70 ICC ANN. REP. 5-7 (1956).
\textsuperscript{61} The Commission noted in Small Shipment Rate Revision—Eastern Central Territory, 350 I.C.C. 586, 608-09, 615-18 (1975), that the various methods of platform handling for small shipments, such as two-wheel carts, four-wheel carts, forklifts, draglines, or hand-carrying, could affect the costs of such an operation.
\textsuperscript{62} Statement of Robert G. Bouman, Holland Motor Express, Inc. at 10-11, (July 31, 1972), submitted in In re Restructured Class Rates, Central States Motor Freight Bureau, Docket No. 70740.
\textsuperscript{63} Statement of Dick Buttor, Anderson Motor Service, Inc. at 6 (July 31, 1972) submitted in In re Restructured Class Rates, Docket No. 70740.
\textsuperscript{64} General Increases Eastern Central Territory, 316 I.C.C. 467, 484 (1972).
by larger shipments." 65 That proposal, filed by the ECMCA, and regarded by the Commission as "bold and imaginative," 66 was based on the belief that the various factors utilized in classifying commodities had become irrelevant insofar as small shipments were concerned. 67 Yet, despite the fact that the Commission greeted this proposal enthusiastically, the respondent carriers, after having received the Commission's blessing for the plan, cancelled the constant charges. 68 This development occurred after the larger members of the association declined to continue the constant charges in effect. 69 The Commission, in any event, continued to refer to its belief that the smaller shipments were carrying too large a burden in providing motor carriers with needed revenues. 70

The Eastern Central carriers followed up their constant charge proposal with another rate proposal, one based on the so-called COR (cost-oriented rates) scale. 71 The COR scale involved a single uniform system of rates and charges for the transportation of LTL and any-quantity (AQ) shipments weighing less than 5,000 pounds. In justification of the COR scale, the carriers asserted a need both for increased revenue and for a restructuring, so that smaller shipments would pay a greater share of their cost burden. Although agreeing with the general principle advanced by Eastern Central that rates and charges should be oriented to the cost of providing a particular transportation service, the Commission found that the proposed rates had not been shown to be just and reasonable, 72 as required by the Interstate Commerce Act. 73 In addition to finding that there was no revenue need, the Commission refused to accept certain of the study data submitted by Eastern Central in support of its proposal. Of significance was the fact that the Commission itself developed an alternative class rates structure on small shipments. The Commission emphasized that the carriers were responsible for the initiation of rates, not the Commission. 74

The next proposal by Eastern Central did receive Commission approval, however. 75 In that proposal, the charges for small shipments applied regardless of the classification of the articles included in the

65. id. at 482.
66. id. at 485.
67. id. at 483.
72. id. at 204.
73. 49 U.S.C.A. § 10701(a)(West Supp. 1979) provides that "(a) rate, classification, rule, or practice related to transportation or service provided by a carrier subject to the jurisdiction of the Interstate Commerce Commission under chapter 105 of this title must be reasonable."
shipments, except in those instances where the multiplication of the weight by the otherwise applicable rate per 100 pounds would result in a higher charge.\textsuperscript{76} Shippers attacked this Eastern Central proposal, as they had the earlier ones. Among other charges, it was argued that the proposal did not adhere to the classification principles required by the Act.\textsuperscript{77} It was also argued that the costs and traffic studies contained numerous deficiencies. The Commission accepted the Eastern Central argument that the various classification principles, with the exception of weight, lost their significance with regard to the transportation of shipments weighing less than 200 pounds.\textsuperscript{78} As it had been in the Eastern Central constant charges proposal, the Commission was extremely receptive to the approach presented.

Yet the Commission was not to have the final say in the matter. In \textit{National Small Shipments Traffic Conference, Inc. v. United States},\textsuperscript{79} a three judge district court reversed the ICC's decision. Judge Friendly, writing for the court, found that the Commission had erred in predicating its decision on a 'through basis' cost analysis as opposed to a 'carried basis' cost analysis.\textsuperscript{80} The Commission, on remand, retreated from its earlier finding that the classification principles other than weight lost their significance with regard to small shipments. The Commission found that density and type of handling were partial substitutes for the classification elements.\textsuperscript{81} However, the Commission, after further analysis, upheld the use by Eastern Central of the through basis as the proper method for determining costs-revenue relationships. Such a through basis "best reflects the total traffic at issue from origin to destination,"\textsuperscript{82} the Commission stated. The net effect of the Commission's decision, given its ruling on the classification principles, was that the proceeding was discontinued. Still another

\textsuperscript{76} Id. at 550.
\textsuperscript{78} 335 I.C.C. 547, 564. The classification principles include (1) shipping weight per cubic foot (density); (2) liability to damage; (3) liability to damage of other shipments with which a shipment is transported; (4) perishability; (5) liability to spontaneous combustion or explosion; (6) susceptibility to theft; (7) value per pound in comparison with other commodities; (8) ease or difficulty in loading or unloading; (9) stowability; (10) excessive weight; (11) excessive length; (12) care or attention necessary in loading or transporting; (13) trade conditions; (14) value of service; and (15) competition with other commodities transported. See Motor Car. Rates in New England, 47 M.C.C. 657, 660-61 (1948) and Small Shipment Rate Revision—Eastern Central Territory, 350 I.C.C. 586, 602 (1975).
\textsuperscript{80} The through basis cost analysis involved inclusion of non-study carriers' traffic handled on an interline basis with the study carriers in its survey, as opposed to a carried basis limited to study carriers' traffic alone. 350 I.C.C. 586, 589. Carried costs have been relied upon primarily in establishing cost-revenue relationships, and they involve transportation costs incurred by a carrier from origin to destination on its own line, as well as those costs incurred by the study carrier also on its interline traffic, whether involving origin, intermediate, or destination service. Id. at 598.
\textsuperscript{81} Id. at 618.
\textsuperscript{82} Id.
appeal was taken, however, by shippers opposed to various holdings in the Commission’s decision. In *National Small Shipments Traffic Conference, Inc. v. ICC*, the Commission’s order was vacated and the cause remanded a second time. The court struck down the use of the through basis cost-revenue study once again, despite the Commission’s further analysis, and, additionally, disapproved the reliance by the Commission on a controversial platform service cost study. The Eastern Central proposal has since been the subject of a third appeal, in which the Commission was again reversed by the United States Court of Appeals for the District of Columbia Circuit.

While the Eastern Central controversy was ongoing, another rate restructuring proceeding was achieving success; this proceeding was instituted by members of the Central States Motor Freight Bureau, Inc. In referring to that proposal, the Commission explained:

The purpose of the restructuring before us is to align rates and charges more narrowly with cost and to spread more evenly over the rate structure the burden of producing needed revenues. Restructuring assertedly is also a means of preventing any continued loss of the heavier less-than-truckload (LTL) traffic. While additional revenues will be realized from the increased rates on minimum charge and under 500 pounds small shipments, respondents note that this increase will be largely offset by lower revenues on the heavier LTL shipments as a result of the rate reduction.

The Commission, in approving the Central States’ restructuring, accepted the use of a platform study made by the Commission’s own staff, which study assigned platform handling cost primarily according to shipment size. This was the same platform study, of course, which had been relied upon by the Commission in the much-appealed Eastern Central proceeding.

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84. The Commission had addressed the question of the “through” versus “carried” basis cost revenue comparisons in Ex Parte No. MC-82, New Procedures in Motor Carrier Revenue Proceedings, 339 I.C.C. 324, 332 (1971), 340 I.C.C. 1, 10 (1971) and 351 I.C.C. 1, 19 (1975). The Commission, in each proceeding, refused to preclude carriers from submitting additional data on a through basis, as long as the use of the basis did not result in a substantial sampling bias.
85. Following the second remand, the Commission discontinued the Eastern Central proceeding, and indicated the platform study issues would be considered in Restructured Rates and Charges, Central States Territory, 352 I.C.C. 502 (1976). *See also note 73 supra.* The Court, in *National Small Shipments Traffic Conference, Inc. v. ICC*, No. 78-1099 (D.C. Cir. Oct. 26, 1978), severely chastised the Commission and directed it to adduce evidence regarding the platform study method in the Eastern Central proceeding as originally directed. In the interim, Restructured Rates and Charges, Central States Territory remains open.
86. Restructured Rates and Charges, Central States Territory, 352 I.C.C. 502, 503-04 (1976). *See also note 85 supra.*
Still another recent restructuring proceeding resulted in the cancellation of the proposed rates. This proceeding, as in the above-mentioned Central States proceeding, involved an increase on shipments weighing less than 500 pounds, no change in shipments weighing 500 pounds to 999 pounds, and decreases in shipments weighing over 999 pounds. 88 Because the proponent, the Central & Southern Motor Freight Tariff Association, Inc., failed to present evidence concerning the density of traffic actually moving in its territory, the Commission found that it had failed to meet its burden of proving that the rates were just and reasonable. It also rejected a comparison urged in that proceeding that the Coordinated Freight Classifications used in the New England territory provided a solid basis for ascertaining the average density of certain commodities in the National Motor Freight Classification, the classification system used by Central & Southern. 89 This failure of Central & Southern to determine actual density of its shipments essentially led to the failure of its proposal. 90

This, then, represents the turbulent atmosphere in which Ex Parte No. MC-98 was launched. Attempts to resolve the small shipment problem, both from the standpoint of service and from the standpoint of rates, 91 have resulted in continuing controversy. As the topical nature of these proceedings suggest, small shipments have been, and remain, one of the most pressing issues with which the Commission must deal. 92 Ex Parte No. MC-98 represented a major attempt by the Commission to deal with this conundrum.

88. Importantly, several restructurings on small shipments by the Central States Carriers have been effected since 1972, which have been directed at “achieving reasonably compensatory cost revenue relationships on all weight brackets.” Evidentiary Submission of Central States Motor Freight Bureau in Support of Proposed Restructured Rates and Charges at 3, submitted in Restructuring Proceedings, supra note 1. These restructurings have not involved any departure from the classification system, however.
90. Id. at 880.
91. Id. at 872. An earlier attempt to revise its small shipments rate structure by Central & Southern met with success in Small Shipments Rate Revision, Central & S. Territory, 337 I.C.C. 158 (1970).
IV. Ex Parte No. MC-98

The Notice of Proposed Rulemaking in Ex Parte No. MC-98 termed the problem of restructuring LTL rates as one "vital to the economic health of the regular route common carrier system." It was noted by the Commission that the motor carrier LTL rate structure in use was basically a copy of the classification-based system developed by the railroads. Although the classification system had initially worked to the advantage of the motor carriers, the trucking industry found, as had the rail industry before it, that competitive pressures had siphoned off much of the most desirable freight, which freight had subsidized the less desirable traffic. There is a need for both rates low enough to allow shippers to utilize existing service for LTL shipments, and, at the same time, rates high enough to guarantee continued service by the motor carrier industry at a reasonable profit. The Commission, in the rulemaking notice, did not refer to small shipments as those weighing less than 500 pounds, but referred repeatedly to both LTL and small shipment traffic.

The Commission proposed seven questions to be answered by shippers, motor common carriers, and other interested parties. These questions concerned the level of small shipment service received and the cost to carriers of providing that service, as well as problems with the existing rate structures. Alternative suggestions were solicited with regard to rates and service. The Commission also submitted revisions to 49 C.F.R. §1104.3

94. Id.
95. Id. The seven questions were:

(1) What problems, if any, have you experienced in connection with LTL or small shipment traffic? If you have experienced any problems, e.g. in costs, service, handling, or other, would you please describe them in detail? Can, or should anything be done to change, improve, or replace the present LTL and small shipment rate structure?

(2) Can action be taken to increase the volume of small shipment traffic, other than subsidization by other traffic?

(3) Are there any alternatives to the present physical methods of handling LTL and small shipments by carriers which could, or should, replace current methods?

(4) In light of the criticism of shippers that motor common carriers do not provide adequate small shipment service, and the complaints of carriers that the existing rate structure does not compensate them adequately for the cost of handling small shipment traffic, what can be done to reconcile the need for an adequate rate structure for motor carriers and the need for LTL rates which shippers can afford to pay?

(5) Where certain shippers, industries, or localities have no alternative means of transportation and require LTL service, is there a point at which the carrier burden should be deemed to outweigh the need for the service?

(6) Could, or should, alternative rates based on differing service needs, e.g. expedited, standard, and standby, be offered for LTL service? How could, or should, such alternative rates be constructed?

(7) If you feel certain commodities or classes of traffic are unfairly priced under the existing rate structure, please give specific examples, and suggest how this unfairness can, or should, be eliminated.
which would require the furnishing, under so-called MC-82 procedures, of breakdowns of operating ratios applicable to all categories of traffic, including LTL, in a uniform manner.\textsuperscript{96} Evidence was to be submitted by the parties in writing.

A. \textit{Shipper Representations}

As could be easily predicted, the participating shippers, many of which had been active opponents of the rate restructuring proposals presented to the Commission during the prior 15 years, recited the familiar refrain of shipper complaints. Included among the service problems experienced by shippers were such recognizable items as high minimum charges, unreliable transit times, inability to obtain protective service, the necessity to utilize a plethora of carriers because of limited operating rights, the unavailability of pickups for small shipment protective service on Thursday or Friday, and the inability to obtain pickups at all.\textsuperscript{97} Other shipper organizations mentioned carrier failures with regard to the settlement of loss and damage claims and the multitude of complex tariffs which governed small shipment movements.\textsuperscript{98} Still other difficulties cited included problems with tracing shipments, obtaining off-highway delivery, obtaining redelivery, obtaining proof of delivery, the level of charges for redelivery, and carrier lack of equipment.\textsuperscript{99} The impetus behind these service gaps, the shipper representatives charged, was an attempt on the motor carriers' part to discourage the transportation of small shipments.\textsuperscript{100} Additionally, shippers charged that carriers refused to serve areas authorized, cancelled routing concurrences, established arbitrary charges with regard to small shipments, and, through purchases by long haul carriers of regional carriers, cut back on the amount of local service.\textsuperscript{101} The effect of these service breakdowns was both direct and indirect. As an example of an indirect effect, one shipper complained that the present pricing structure complexities virtually precluded the application of the latest data processing techniques to the motor

\textsuperscript{96} Id. at 1924. See note 84, supra, with regard to the MC-82 procedures.

\textsuperscript{97} Initial Statement of Drug and Toilet Preparation Traffic Conference (DTPTC) and National Small Shipments Traffic Conference, Inc. (NSSTC) at 3, \textit{submitted in Restructuring Proceedings, supra note 1}; Initial Statement of National Retail Merchants Association (NRMA) at 5, \textit{submitted in Restructuring Proceedings, supra note 1}.

\textsuperscript{98} Initial Statement of National Industrial Traffic League (NIT League) at 4, \textit{submitted in Restructuring Proceedings, supra note 1}.


\textsuperscript{100} Initial Statement of Bell & Howell Business Equipment Group at 3, \textit{submitted in Restructuring Proceedings, supra note 1}.

\textsuperscript{101} Initial Statement of NCR Corporation, Systemedia Division, at 3, \textit{submitted in Restructuring Proceedings, supra note 1}.
carrier industry, creating problems for both shippers and carriers. Yet, if there was one complaint expressed more frequently than the rest, it was the virtually unanimous sentiment that charges on small shipments were much too high.

Thus, the shippers and receivers not only felt that the service being provided them was woefully deficient, but also that the price of receiving that inadequate service was too high. This is not to say that the shippers generally felt that small shipments should be cross-subsidized. To the contrary, there was support for the proposition that rates should reflect the cost of service. As was stated by the National Industrial Traffic League (NIT League) in its initial statement:

The League supports the concept of rates reflecting the cost of service so that no one element of carrier traffic is called on to subsidize other traffic. But the cost of service must be a proven, reliable cost, to the extent any costing, by definition, involves the broad use of estimates and assumptions. At best, cost allocation is an art, not a science.

Similarly, the National Retail Merchants Association (NRMA), in its initial statement, stated: "Obviously, the carriers must have compensatory rates if they are to adequately provide the service." The area of disagreement with the carriers was whether existing rates on small shipments were in fact compensatory, however. Such a conclusion could not be made, the shippers argued, based upon present cost analysis. It would first be necessary to develop and apply new accurate and reliable costing systems and analysis. One shipper organization went so far as to allege that the small shipment traffic had been, in fact, subsidizing the larger shipments, which were underpriced.

There was one element of the current costing system utilized by the Commission that was attacked by the shippers. It was the much-maligned platform study. It was submitted that a moratorium be placed by the Commission on restructuring, until such time that there was a new platform

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103. There was, however, a great diversity of opinion not only between shippers and carriers, but between shipper and shipper. One company exclaimed: "We have not experienced any problems in connection with LTL or small shipment traffic." Initial Statement of Armstrong Cork Company at 1, submitted in Restructuring Proceedings, supra note 1.
109. See note 87, supra.
study and more reliable cost analysis.\textsuperscript{110} One organization asserted that it was unfair to assign the great bulk of platform handling cost to the small shipments, in that one of the major reasons why the "small"s underwent such excessive platform handling was because of conscious operation decisions on the part of the carriers themselves. Such platform handling was purportedly engaged in to reduce other expenses, such as line-haul costs which fell most heavily on the larger shipments. By consolidating the small shipments and placing them on trailers with larger shipments, the line-haul costs for larger shipments were accordingly reduced.\textsuperscript{111} The occasion was also utilized to denigrate the "through" as opposed to "carried" method of costing. It was stated that: "To the extent that the through costing method does attribute such additional platforming services to the delivery carrier, the present costing techniques are significantly misleading."\textsuperscript{112} Thus, although there was general agreement that a cost of service rate structure was a commendable goal, it was argued that there were no suitable methodologies for determining the cost of service at this time.

Disagreement among the shipper representatives was more widespread with regard to the merits of the classification system itself. Some groups steadfastly defended the classification system because, in part, of the nature of the commodities they shipped as related to the classification system.\textsuperscript{113} The NIT League stated that it knew of no examples of unfair pricing.\textsuperscript{114} Yet, other organizations attacked the classification system. As was stated by the New Orleans Traffic and Transportation Bureau:

\textsuperscript{115} Likewise, other shippers urged the Commission to resolve the shortcomings of the classification system in a separate proceeding.\textsuperscript{116}

\textsuperscript{111} Reply Statement of NIT League at 7, \textit{submitted in Restructuring Proceedings}, \textit{supra} note 1.
\textsuperscript{112} Initial Statement of NIT League at 14, \textit{submitted in Restructuring Proceedings}, \textit{supra} note 1.
\textsuperscript{113} Reply Statement of Southern Furniture Manufacturers Association at 5, \textit{submitted in Restructuring Proceedings}, \textit{supra} note 1.
\textsuperscript{114} Initial Statement of NIT League at 19, \textit{submitted in Restructuring Proceedings}, \textit{supra} note 1.
\textsuperscript{115} Reply Statement of New Orleans Traffic and Transportation Bureau at 8, \textit{submitted in Restructuring Proceedings}, \textit{supra} note 1.
\textsuperscript{116} Initial Statement of Traffic Managers Conference of California at 6, \textit{submitted in Restructuring Proceedings}, \textit{supra} note 1.
The shippers' representatives propounded numerous recommendations to the Commission for the improvement of the small shipment problem. It was suggested that the Commission should grant small shipment operating certificates of a two year limited term nature for all shipments under 1,000 pounds, over broad geographic areas, with the certificate renewable at the end of the two years if the carrier was in fact adequately serving the public.\textsuperscript{117} The issuance of such a certificate would be conditioned on individual ratemaking. It was suggested, furthermore, that carriers use joint terminals, for the handling of small shipments, and pool freight. Similarly, joint agents for pickup and delivery could be utilized. It was also suggested that a UPS-type service be authorized for shipments weighing up to 300 pounds, and that existing carriers establish separate divisions to transport smaller shipments.\textsuperscript{118} Other participants specifically urged that the weight limits of the UPS authority be increased, as well as those of other small shipment specialists.\textsuperscript{119} One organization expressed the view that, for small shipments to be handled efficiently, a carrier must specialize exclusively in that field.\textsuperscript{120}

The Traffic Managers Conference of California, searching for a more equitable basis on which to structure current small shipment rates, drew an example from other transportation modes. It observed:

Airline and air forwarding companies appeared to have solved this problem by allowing for a break-out in charges between pickup, line-haul and delivery of an order. In many instances they also provide rates on multiple pickup and/or delivery of shipments. We recommend that the Interstate Commerce Commission consider a similar requirement for motor common carrier LTL rates and tariff publications under its jurisdiction.\textsuperscript{121}

Other shippers suggested rate discounts for multiple pickups,\textsuperscript{122} a pickup and delivery allowance, and special rates for a component service only, including pickup, terminal handling, billing, line-haul, and delivery.\textsuperscript{123}

Thus, while steadfastly maintaining their ground on such issues as

\begin{itemize}
  \item \textsuperscript{117} Initial Statement of DTPTC and NSSTC at 7-8, \textit{submitted in Restructuring Proceedings}, supra note 1.
  \item \textsuperscript{118} \textit{Id.} at 8-9.
  \item \textsuperscript{119} Initial Statement of Norris Industries at 4, \textit{submitted in Restructuring Proceedings}, supra note 1; \textit{see also} Initial Statement of NCR Corporation, Systemedia Division at 7, \textit{submitted in Restructuring Proceedings}, supra note 1.
  \item \textsuperscript{120} Initial Statement of Steel Office Furniture Traffic Association at 4, \textit{submitted in Restructuring Proceedings}, supra note 1.
  \item \textsuperscript{121} Initial Statement of Traffic Managers Conference of California at 3-4, \textit{submitted in Restructuring Proceedings}, supra note 1.
  \item \textsuperscript{122} Initial Statement of General Mills, Inc. at 6, \textit{submitted in Restructuring Proceedings}, supra note 1.
  \item \textsuperscript{123} Initial Statement of DTPTC and NSSTC at 6, 9, \textit{submitted in Restructuring Proceedings}, supra note 1.
\end{itemize}
through versus carried costs and the controversial platform handling study, the shippers' organizations submitted numerous proposals to ameliorate the small shipment problem. What was wanted most strongly in the interim was a moratorium on any rate restructuring until such time as more sophisticated costing methods could be devised.

B. GOVERNMENTAL AGENCIES

A total of five departments and agencies of the federal government submitted statements in Ex Parte No. MC-98. Two of those statements, those of the Department of Defense (DOD) and the General Services Administration (GSA), were submitted from the viewpoint of users of motor carrier service in the transportation of small shipments. The statements of the United States Department of Transportation (DOT), United States Department of Justice (DOJ), and Federal Energy Administration (FEA) addressed the policy question of the proceeding from the point of view of those departments themselves.

Despite these two differing viewpoints, there was unanimity of voice among the agencies with regard to the establishment of cost-oriented rates. As was stated by DOJ, "[m]otor carrier LTL rates should, to the greatest extent possible, be constructed on the basis of motor carrier costs properly allocable to the handling of that type of traffic." Even GSA, with its shipper orientation, supported restructuring, if the restructuring was supported by accurate carrier evidence reflecting differences in the cost and handling of transporting respective categories of traffic. There was simply no sentiment in favor of any rate system where cost subsidization was allowed to exist.

The DOJ accepted the view that small shipments were in fact being subsidized by larger shipments. It was stated that:

At present it appears that small shipment tariffs are too low while larger shipment rates are excessive. The result is a system of cross-subsidization or wealth transfers from shippers of large shipments to shippers of small shipments. Small shipment products are wastefully promulgated and large shipment products are artifically suppressed. In this way the waste reaches far beyond the regulated industry itself into society at large.

124. Initial Statement of Dep't of Justice at 2, submitted in Restructuring Proceedings, supra note 1.
125. Initial Statement of General Services Administration at 3, submitted in Restructuring Proceedings, supra note 1. The State of Michigan Department of Management and Budget, the one state agency to participate in the proceeding, also supported such a view in its Initial Statement at 4, submitted in Restructuring Proceedings, supra note 1.
127. Initial Statement of Dep't of Justice at 6, submitted in Restructuring Proceedings, supra note 1.
DOT called such a view "virtually unchallenged." The criticism of the governmental departments extended also to the classification system itself. The existing classification system was challenged by DOJ, DOD, and FEA. FEA suggested that density-based rates, such as the coordinated freight classification utilized by the New England Motor Rate Bureau in the New England territory, were superior.

GSA cited various service failures which it encountered in the movement of small shipments, but these were no different than those which had been cited by the various shipper representatives. Not surprisingly, because of the amount of traffic controlled by it and the corresponding leverage obtained, DOD indicated that it had received satisfactory small shipment service in the past.

In the area of rates and operations, suggestions were submitted to improve the small shipment situation. DOD voiced approval for the utilization of freight-all-kinds (FAK) rates, noting that it had experience with such rates moving at a reduced level, as is permitted on government traffic by the Interstate Commerce Act. DOJ suggested that flexibility should be permitted carriers to raise and lower rates in accord with short term developments. DOT also proposed greater pricing flexibility, as well as the availability of alternative rates based on differing service. FEA supported the establishment of aggregate tender rates, distribution rates on a FAK basis, and released rates on small shipments.

The possibility of achieving operating efficiencies in the transportation of small shipments was an important part of the departments' submissions. GSA proposed a centralized pickup and delivery on the "cluster concept"
for urban services.\textsuperscript{138} GSA also advanced the concept of utilizing automated equipment in terminal, unitization hardware, and motor vehicles to handle palletized or containerized small shipment loads.\textsuperscript{139} FEA added its support to a pooling concept, the elimination of deadhead miles on backhauls, and the use of transportation facilitation centers (TFC), where one carrier would be assigned the task of performing pickup, delivery, consolidation, and breakbulk for all common carriers operating in a metropolitan area.\textsuperscript{140} FEA was also a proponent of substituted intramodal services in which a common carrier with excess capacity would transport shipments along the same traffic lane for other common carriers encountering equipment shortages.\textsuperscript{141} It was felt by DOT that the Commission should provide some incentive for continued improvements in efficiency in the transportation of small shipments. It proposed that restructuring should be based, at least in part, on efforts by the carriers to improve their efficiency in this regard.\textsuperscript{142}

One of the most novel ideas was that for the establishment of a subsidy revenue fund. DOJ advanced that such a fund should be set up to subsidize shippers directly if a judgment were made that the continued business activity of those shippers would be in the public interest, even though there was inadequate demand for their products to cover the shipment cost. (This assumes, of course, an end to cross-subsidization of small shipments.)\textsuperscript{143} DOT believed that with freer entry, this situation would not exist except in very isolated instances.\textsuperscript{144} The governmental departments generally supported the ICC's examination of the small shipment problem. The Commission was urged to take an activist role in implementing reforms.\textsuperscript{145}

\section*{C. CARRIER REPRESENTATIONS}

Submitting a joint statement were numerous tariff bureaus, including the Central States Motor Freight Bureau, Inc., the Eastern Central Motor

\begin{itemize}
\item \textsuperscript{138} Initial Statement of General Services Administration at 6, \textit{submitted in Restructuring Proceedings}, supra note 1.
\item \textsuperscript{139} \textit{Id.}
\item \textsuperscript{140} Initial Statement of Federal Energy Administration at 8, 19, \textit{submitted in Restructuring Proceedings}, supra note 1.
\item \textsuperscript{141} \textit{Id. at 12.}
\item \textsuperscript{142} Initial Statement of Dep't of Transportation at 13, \textit{submitted in Restructuring Proceedings}, supra note 1.
\item \textsuperscript{143} Initial Statement of Dep't of Justice at 16, \textit{submitted in Restructuring Proceedings}, supra note 1.
\item \textsuperscript{144} Initial Statement of Dep't of Transportation at 6-9, \textit{submitted in Restructuring Proceedings}, supra note 1.
\item \textsuperscript{145} Initial Statement of Federal Energy Administration at 38, \textit{submitted in Restructuring Proceedings}, supra note 1.
\end{itemize}
Carriers Association, Inc., the Middle Atlantic Conference, the Midwest Motor Freight Bureau, the New England Motor Rate Bureau, the National Motor Freight Traffic Association, the Niagara Frontier Tariff Bureau, Inc., the Pacific Inland Tariff Bureau, Inc., the Rocky Mountain Motor Tariff Bureau, Inc., and Southern Motor Carriers Rate Conference (hereinafter the MC-82 Bureaus)\(^{146}\). Submitting separate statements were two other bureaus, the Motor Carriers Traffic Association, Inc., and the Central & Southern Motor Freight Tariff Association, Inc. The Regular Common Carrier Conference (RCCC) of the American Trucking Associations, as well as five carriers individually, also submitted statements in response to the *Ex Parte No. MC-98* proceeding.

The MC-82 Bureaus pointed to numerous problems encountered by them in the transportation of small shipments. It was noted that there was a multitude of individual demands for service. Shippers often possessed outmoded and inadequate loading and unloading facilities, making it difficult for the general freight carriers to provide service. Certain shippers demanded that extra copies be provided of freight bills and other shipping documents, leading to an excessive amount of paperwork on small shipments. General freight carriers encountered single shipment tenders, instead of multiple tenders, on frequent occasions. Poor packaging was another factor cited in the handling of small shipments by general freight carriers. Some shippers insisted that pickups and deliveries be performed at specific times of the day, even down to the exact hour. Other shippers required that appointments be made before pickup or delivery, sometimes as much as 48 hours in advance. Still other shippers refused to receive any freight on one or more days of the week.\(^{147}\)

The heart of the matter, however, from a carrier standpoint, had to do with the pricing of small shipments. As shipper representatives thought that the pricing on small shipments was too high, the carriers were convinced that the converse was true. As was stated by the MC-82 Bureaus,

The basic competitive problem to which the Commission refers does not lie in the maintenance of the classification-based rate structure on LTL traffic. Rather, it lies in the fact that shipments under 500 pounds, as a category of traffic, do not pay their way under the present system of class rates and minimum charges. The consequence is that shipments of heavier weights are required to bear a disproportionate share of the burden for meeting the carrier's need for overall revenues sufficient to enable them to discharge their duty to render adequate service. The unavoidable result of this is the actual or threatened diversion of the heavier weighted shipments to other forms of carriage.\(^{148}\)


\(^{147}\) *A History of Restructuring*, supra note 92, at 6-7.

\(^{148}\) *Id.* at 3.
A similar view was expressed by RCCC, that some shipments produced large deficits while others were burdened with the task of making up for those deficits. Likewise, individual carriers participating in *Ex Parte No. MC-98* echoed the view that there was a need for the cessation of this cross-subsidization.

The agreement ended, though, among the carrier submissions, with regard to the continued viability of the classification system. The MC-82 Bureaus commenced their statement with a defense of the National Motor Freight Classification (NMFC). Their enthusiasm, however, was not seconded by other motor carrier participants. Yellow Freight System, Inc., for example, referred to the existence of truckload classes and minimum weight factors, stating that it was time "to remove the shackles of this historic pitfall... from the National Motor Freight Classification." Jones Transfer Company referred to the existence of flat charges applying on shipments less than 500 pounds, varying with distance and by 50-pound increments and applying on interstate traffic moving within the state of Michigan, as a superior pricing system. Georgia Highway Express, Inc., stated:

That actually up to 500 pounds and even to 1,000 pounds—other than in light and bulky and in high value traffic—there really is very little difference in characteristics, and classification principles have really little to do with the minimum charge for the traffic other than in the amount of weight that moves under the minimum charge. Actually, the number of pieces in the shipment would probably have more cost impact than classification.

Neither were the Central & Southern carriers enamored with the NMFC system. They also urged the establishment of a density-related classification. In addition to a revamping of the classification system, other carriers felt that tariff incentives should be initiated, such as multiple pickup allowances.

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Various tariff incentives were also suggested by the MC-82 Bureaus in their joint statement. They submitted, as Appendix B to their initial statement, a model tariff, denoted "Tariff 499." Tariff 499 is actually the product of the Middle Atlantic Conference. As explained by the MC-82 Bureaus,

It is a small shipments tariff embodying a pricing system of rates, charges, allowances, and discounts which can be tailored to the needs of each individual shipper. Thus, it provides freight-all-kinds rates and charges graduated by weight, number of pieces, and volume. It offers discounts on shipments tendered to the carrier at its terminal, on shipments that are prepaid, on shipments that are tendered in multiples.\(^{157}\)

Crucial to the actual publication of this tariff, however, according to the MC-82 Bureaus, was the receipt of released rates authority from the Commission, pursuant to the terms of the Act.\(^{158}\)

In addition to this innovative tariff, a creative alternative to present pricing systems was submitted by Georgia Highway Express. That carrier urged the adoption of a transaction charge rate structure. Such a rate structure would impose a flat transaction charge to reflect the costs incurred solely because a carrier handled a particular shipment. This would include all costs except those related to the number of pieces in a shipment, weight, and distance.\(^{159}\) Added to the flat transaction charge\(^{160}\) would be a hundredweight rate times the actual weight of the shipment.\(^{161}\) Thus, although the carrier would receive compensation for each additional pound in a shipment, the cost per hundredweight to the shipper would reduce substantially with an increase in weight. This, in the opinion of the proponents, would provide a significant incentive to the shipper to transport larger shipments and to the receiver to order larger shipments.\(^{162}\)

Both the RCCC and the MC-82 Bureaus felt it necessary to defend the Commission's controversial platform study from attack by various shipper interests.\(^{163}\) Yet both groups urged upon the Commission speed in the completion of a new platform study.\(^{164}\) At the same time, the MC-82 Bureaus emphasized that "cost finding is not a science but a constantly evolv-

\(^{157}\) A History of Restructuring, supra note 92, at 5.
\(^{158}\) 49 U.S.C.A. § 10730 (West Supp. 1979) provides that the Commission may authorize or require motor carriers to furnish transportation under limited liability, as opposed to full liability, if the "value would be reasonable under the circumstances surrounding the transportation."
\(^{159}\) Initial Statement of Georgia Highway Express, Inc. at 24, submitted in Restructuring Proceedings, supra note 1.
\(^{160}\) The example transaction charge suggested by Georgia Highway Express was $7.00. Id.
\(^{161}\) Id.
\(^{162}\) Id. at 25.
\(^{163}\) A History of Restructuring, supra note 92, Reply Statement at 3; Reply Statement of RCCC at 4, submitted in Restructuring Proceedings, supra note 1.
\(^{164}\) See note 87, supra.
The MC-82 Bureaus acknowledged their duty to establish rates, but at the same time admonished the Commission that it had the duty to provide guidelines for the carriers.\textsuperscript{166}

The battlelines drawn, then, by the submissions of the parties in Ex Parte No. MC-98 were changed only slightly from the earthworks of earlier skirmishes. The challenge presented to the Commission, in light of this record, was not so much to declare a winner but to prevent, once again, a theoretical stalemate. Only in this manner could progress finally be made toward solving both small shipment problems—the shippers' and the carriers'.

\textbf{D. THE COMMISSION'S DECISION}

The Commission's decision, served March 27, 1978, is comprised of some 136 pages of text with over 100 pages of appendices. Only one Commissioner, of the then seven sitting members, dissented from the issuance of the decision, and that dissent was only a partial one.\textsuperscript{167} The Commission made 16 specific recommendations focusing on the service and rate areas. As a result of the rulemaking, two new proceedings were spawned by Ex Parte No. MC-98, including an investigation into the classification system and a rulemaking proceeding on released rates to be applied to a small shipment tariff. The decision will be discussed in terms of both service and rates, although, again, the two issues are inextricably intertwined, as they have been in prior discussions of the small shipment problem.

1. Service

The Commission, in one recommendation, indicated that it would encourage the specialization of carriers in the transportation of small shipments in the future. The shipper allegations that small shipment service was in any way deficient had been contested strenuously by the RCCC and the MC-82 Bureaus in their evidentiary submissions in this proceeding.\textsuperscript{168} The Commission, however, implicitly found that small shipment service was in fact deficient by its pronouncements on carrier specialization. It is true that the Commission did not state any intention of discouraging general freight carriers from handling small shipments in the future. Rather, the Commission found that small shipments could be handled most efficiently

\textsuperscript{165} A History of Restructuring, supra note 92, at 14.
\textsuperscript{166} Id. at 16.
\textsuperscript{167} Restructuring Proceedings, supra note 1, at 3.
\textsuperscript{168} A History of Restructuring, supra note 92, and Reply Statement of RCCC at 2, submitted in Restructuring Proceedings, supra note 1; Reply Statement.
either through the utilization of carriers specializing solely in small shipments, or by the establishment by general freight carriers of a special division to handle the transportation of small shipments.

As the Commission stated in this regard:

It is not our intention to limit the authority of general commodities carriers. We do intend, however, that more carriers will specialize in the transportation of small shipments. We believe that these specialized carriers, handling the traffic economically and efficiently, will serve as a positive competitive impetus in the trucking industry.169

In order to accomplish this specialization, the Commission stated that it would continue to issue certificates of public convenience and necessity containing weight limitations in the small shipment area.170 The Commission indicated that then if the Applicant can demonstrate that its proposal is responsive to a public need, then the certificates would be granted.171 The Commission made a specific finding that there was a particular need for the transportation of small shipments in the area between the 100-pound-per-shipment weight restriction of United Parcel Service, Inc., and the 500-pound weight cut-off of the small shipment problem itself.172

In encouraging the establishment of small shipment specialists, the Commission explicitly disavowed the view that the transportation of small shipments was inherently unprofitable. Even within the category of shipments weighing less than 500 pounds, the Commission identified the existence of various subgroups, including (1) parcel delivery, comprised of shipments weighing in the main less than 50 pounds; (2) package freight, weighing generally anywhere from 50 pounds to 300 pounds; (3) furniture, appliances, and small machine cartage; and (4) small-shipment pool distribution.173 The Commission commented on these various subdivisions, noting that:

Each of these divisions of small shipments places a somewhat different burden upon the carriers’ vehicles, handling equipment, and terminals. Carriers with profitable LTL and small shipment specialities generally recognize and capitalize on the differences. Such recognition is reflected in the design of and placement of terminals, fleet selection, and in handling equipment and management.

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169. Restructuring Proceedings, supra note 1, at 94.
170. See note 19 supra.
171. The standard utilized by the Commission in issuing common carrier certificates is governed by 49 U.S.C.A. § 10922 (West Supp. 1979), which provides that an applicant must show that it is "fit, willing, and able—(A) to provide the transportation to be authorized by the certificate; and (B) to comply with this subtitle and regulations of the Commission; and (2) the transportation to be provided under the certificate is or will be required by the present or future public convenience and necessity."
172. Restructuring Proceedings, supra note 1, at 92.
173. Restructuring Proceedings, supra note 1, at 90. These same divisions had been first suggested by one authority on the small shipment problem in Wasserman, The Cause of The Small Shipment Problems and An Effective Solution, THE ALPHAN, September, 1976, at 3.
This explains, at least in part, why some carriers complain about inefficiencies associated with small shipments traffic and the comparatively high cost of handling it, while others pursue this traffic. 174

The Commission thus took notice of that which several shippers’ representatives had pointed out, i.e., that numerous carriers specialized in the transportation of small shipments and still possessed extremely favorable operating ratios.

With regard to the service area, the Commission also commented on various other suggestions that had been proposed by the parties in Ex Parte No. MC-98. The Commission stated that it would encourage the computerization of rates, through the use of a mathematical formula, so that it would be possible for shippers to readily ascertain the correctness of any particular rate. (Although this recommendation concerns the actual construction of the rates, many shippers mentioned the complexity of small shipment rates as a service problem, in that it was impossible for them, without extensive calculations, to determine the correctness of rates.) 175 Although it was pointed out that it would be virtually impossible for the Commission to mandate an “efficient” packaging method, as suggested by carriers and shippers, the use of more efficient packaging methods was supported by the Commission. 176

The Commission also informed carriers that they were not prohibited from establishing different types of small shipment service, including expedited, guaranteed, premium, and other special service, by the publication of applicable tariffs. It specifically disclaimed the notion that it had, in a past decision, meant to prohibit the filing of such provisions altogether. 177 The Commission acknowledged that it already could approve pooling arrangements, pursuant to the provisions of the Act, as long as the pooling provisions resulted in better service to the public and would not unduly restrain competition. 178 However, with regard to pooling, the Commission stated that it would urge that the statutory provision be amended, in order that it could provide for the summary informal approval of a substantial proportion of such proposals without engaging in the complex proceedings currently mandated by the statute. Such an amendment, the Commission

175. Id. at 111.
176. Id. at 105.
177. Id. at 102-03. The Guaranteed Service, Pacific Intermountain Express, 351 I.C.C. 90 (1975) proceeding was not meant to be a statement of general disapproval of guaranteed service provisions, the Commission underscored, pointing out that the P.I.E. tariff in question therein did not involve a special service, and the complete refund of rates involved amounted to a rebate, in violation of 49 U.S.C.A. § 11903 (West Supp. 1979).
felt, would allow the expeditious implementation of the energy-efficient pooling arrangements.\textsuperscript{179}

Along a similar line, the Commission referred to the concept of transportation facilitation centers. It found that experiments with TFC’s had failed in the past, so that their future feasibility had not been clearly demonstrated.\textsuperscript{180} Still, the Commission cautiously recommended continued future experimentation with the concept. With regard to loss and damage claims, the Commission indicated that there was a public demand and need for remedial legislation in this area also. It referred to its past efforts in the area\textsuperscript{181} and indicated that it would support remedial legislation. Examining overcharge claims, the Commission noted\textsuperscript{182} that it had commenced its own rulemaking proceeding\textsuperscript{183} because of shippers’ problems with regard to the practices and procedures of carriers. Also, the Commission reiterated that, in order to promote more efficient use of motor carrier equipment, it would support the standardization of size and weight restrictions on the nation’s highways through legislation.\textsuperscript{184}

Moreover, the Commission indicated that, with regard to the service complaints regarding pickup and delivery, the failure of existing carriers to meet the scheduling requirements of shippers and receivers would receive renewed emphasis in all types of proceedings, including operating rights, finance, and rate matters.\textsuperscript{185} Thus, across an extremely broad front, the Commission addressed the problems of shippers with existing service and the suggestions put forth by carriers, shippers, and government departments for the amelioration of the service aspect of the small shipment problem.

2. Rates

The Commission’s treatment of the rate area was no less comprehensive. The Commission began by addressing the suggestion that a moratorium be placed on all rate restructuring and held that there would be no such moratorium.\textsuperscript{186} It confronted the issue of costing, observing that "[c]osting is a developing science, and as such, will continue to progress."

\textsuperscript{179} Restructuring Proceedings, supra note 1, at 116.
\textsuperscript{180} Id. at 126.
\textsuperscript{181} See Ex Parte No. 263, Rules, Regulations and Practices of Regulated Carriers with Respect to the Processing of Loss and Damage Claims, 340 I.C.C. 515 (1972).
\textsuperscript{182} Restructuring Proceedings, supra note 1, at 121.
\textsuperscript{183} Ex Parte No. MC-342, Procedures Governing the Processing, Investigation and Disposition of Overcharge, Duplicate Payment, or Overcollection Claims, 358 I.C.C. 114 (1978). This action has been concluded by the Commission, and new regulations have been promulgated.
\textsuperscript{184} Restructuring Proceedings, supra note 1, at 172.
\textsuperscript{185} Id. at 68.
\textsuperscript{186} Id. at 6. The action of the United States Court of Appeals for the District of Columbia Circuit may have the same practical effect, however. See note 85 and accompanying text. Bu-
Even though present cost analysis can be improved, it is not so invalid as to justify a moratorium on rate restructuring. Yet the Commission recognized the need for more precise costing and, accordingly, required the one-time submission of cost-revenue information from MC-82 Bureaus and adopted the additional reporting requirements of Appendix E. Also on the subject of costing, it was emphasized that costing was not the end-all of the rate-making process, and the parties were cautioned against any adherence to this view.

The Commission faced once again the classification problem. It was pointed out that "[c]lassification, as it was originally conceived, has become somewhat distorted, resulting in the anomaly of having a multiplicity of classes for any one given commodity . . . . Further, innovations in pricing can be, and often are, inhibited by the present classification system." The Commission noted that the Coordinated Classification System, however, as an alternative to the National Motor Freight Classification, had not resulted in an end to the small shipment problem in New England. Further evidence was needed, the Commission concluded, before any ultimate determinations could be made concerning improvements in the present system. Accordingly, it instituted an investigation into the continued validity of the classification system.

Discussing the inclusion in a small shipment tariff of a FAK rate, where rates would include the transportation of any commodity named in a freight classification system, whether in straight shipments of any one commodity or in mixed shipments, the Commission declined to support such a provision. It was stated that such FAK rates would ignore the classification and commodities principles. Those who would be participants in the classification investigation were invited, however, to present proposals concerning the manner in which FAK rates could be utilized without discriminating against shippers of consistently low-rated commodities. The continued authorization of pickup and delivery allowances was supported by the Commission for situations wherein shippers arrange for the separate pickup and/or delivery of their freight. In the future, allowances for pickup and delivery must be increased whenever there is a rate increase, so that the shipper will continue to be compensated for assuming part of the transpor-

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tation service.\textsuperscript{194} Again, the Commission noted that pickup and delivery allowances had been well-established under past Commission precedent.\textsuperscript{195}

The Commission went beyond the mere reiteration of its support for pickup and delivery allowances, however. If the carrier elected not to file pickup and delivery allowances, then the carriers would be required to have small shipment tariffs that set forth two sets of rates. The first set of rates would be for pickup and the second for line-haul and delivery of the shipment. Pickup would be performed at the option of the shipper only. The Commission refused to require the publication of separate delivery allowances; it felt that such a provision might overtax the terminal facilities of carriers, which were not designed for warehousing.\textsuperscript{196}

The Commission believed that its action with regard to pickups and deliveries was significant, since these two elements of a carrier's costs comprised a substantial portion of the total expense of handling small shipments.\textsuperscript{197} Because of the importance of pickup costs, the Commission also indicated its support for aggregate tender provisions. As stated by the Commission, "[i]t is only logical that if a carrier can pickup two or more small shipments at one time rather than making a trip for each, its expenses will be reduced."\textsuperscript{198} The Commission approved of the publication of such aggregate tender rates, which provide an incentive to shippers tendering several shipments to the carrier at one time. The pickup charges published by the carriers should be the same regardless of the amount of shipments tendered at one time.\textsuperscript{199} This is to be the method whereby shippers receive incentive for tendering multiple shipments, as opposed to any allowance system. Again, the Commission noted that it had found in the past that reduced rates based on the ability of the shipper to tender large or aggregate shipments did not discriminate between shippers.\textsuperscript{200}

The Commission also discussed the issue of the propriety of discounts on prepaid shipments. It had, only recently, instructed carriers that no restrictions on C.O.D., freight-collect, and order-notify shipments could be imposed.\textsuperscript{201} However, the Commission clarified that ruling, with regard to the specific issue of prepaid discounts, by stating:

We no longer view such discounts as 'undue' discrimination. There will always be a measure of unfairness or discrimination in the business world, due to

\begin{itemize}
\item 194. Id. at 38.
\item 195. Pickup and Delivery Allowance at St. Louis and Kansas City, 64 M.C.C. 163, 165 (1955).
\item 196. Restructuring Proceedings, supra note 1, at 39.
\item 197. Id. at 45.
\item 198. Id.
\item 199. Id. at 46.
\item 200. Aggregate Class Rates Between Points in the South, Midwest and East, 332 I.C.C. 524 (1968).
\end{itemize}
many factors, economies of scale being only one. It is not the Commission's duty to prevent all discrimination, but only that which is 'unjust' and that prejudice and preference which is 'undue'.

Carriers were cautioned to relate discounts to costs and to provide a significant enough incentive for prepaid or prepayment shipments.

Another important area addressed by the Commission centered on the permissibility of released rates provisions as applied to all small shipments. The Commission felt that, by authorizing released rates, it could make the service of regular route general commodities common carriers more attractive, since lower rates could be offered if carrier liability were limited. The fundamental consideration of the Commission, in determining whether to grant released rates, is "the surrounding transportation circumstances and conditions." The Commission had recognized over 50 years ago that small shipments have traditionally moved in express service on a released-rates basis. Despite the Commission's interest in the utilization of released rates as a device to attract more small shipment traffic to general freight carriers, it did not believe that there was sufficient data, based on the record in Ex Parte No. MC-98, to authorize their institution. Accordingly, it announced that a survey of shippers was to be taken and that a second rulemaking proceeding would be instituted on the subject of released rates for shipments weighing 500 pounds or less in conjunction with a small-ships tariff.

The Commission also encouraged the publication of other kinds of discounts. For example, if a carrier would allow a carrier to pick up its small shipments at any time, or at an odd time, such as at night, the carrier could offer such shippers a discount based on its reduced costs. Similarly, if a shipper required that its small shipments be picked up at a set time, the carrier could impose extra charges based on its increased costs.

One other reporting requirement was also imposed in an amendment to 49 C.F.R. §1104.10. Carriers, in rate proceedings, would be required to provide summaries of what steps had been taken to reduce costs on small shipments within the year prior to the time of filing of the revenue proceeding. Subjects to be included were rate innovations, terminal changes, technology developments, and any other operational improve-

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203. See note 158, supra, and accompanying text.
206. Restructuring Proceedings, supra note 1, at 55. This rulemaking proceeding was docketed as Ex Parte No. MC-98 (Sub-No. 2). It, like Ex Parte No. MC-98 (Sub-No. 1), is pending at this time before the Commission.
207. Id. at 68.
ments affecting small shipment costs.\textsuperscript{208}

Finally, the Commission commended the MC-82 Bureaus and Georgia Highway Express for their tariff submissions. Tariff 499 revisions with regard to FAK rates, as well as released rates, were not approved, pending the Commission’s investigation on both of these issues.\textsuperscript{209} The Georgia Highway Express tariff proposal was not adopted because its transaction charge did not provide for optional pickup and delivery. However, the Commission believed that its separate pickup charges accomplished an end similar to that of the transaction charge recommended by Georgia Highway Express but was more effective.\textsuperscript{210} The Commission also stated generally that both tariff proposals, which provided for allowances, should include alternative charges instead.\textsuperscript{211} Yet, ‘‘[b]oth of these tariffs proposed by the carriers have merit.’’\textsuperscript{212}

V. EFFECTIVENESS OF EX PARTE NO. MC-98

The title of Ex Parte No. MC-98, New Procedures in Motor Carrier Restructuring Proceedings, is a misnomer, because it refers only to motor carrier restructuring proceedings. In fact, this rulemaking proceeding represents one of the most comprehensive efforts to date by the Commission to solve the small shipment problem from the dual aspect of service and rates. It is significant that the title of the proceeding did not dissuade the participants from providing the Commission with evidentiary input, allowing a complete survey of the field. Although generally partisan in tone, the representations of the parties, taken collectively, provided a forward-thinking and creative dialectic aimed at the betterment of the small shipment problem.

This is not to say that Ex Parte No. MC-98 is a radical departure from the history which preceded it, as this examination has shown. For example, in the area of service deficiencies, the Commission in the instant proceeding announced that it would encourage the specialization of carriers in the small shipment field, either through carriers which devote their attention exclusively to the transportation of small shipments or through the establishment by general freight carriers of separate divisions handling small shipments. The Commission’s statement on these topics was strong in tone. They approached, but did not quite reach, the level of a general find-

\textsuperscript{206} \textit{id.} at 79.
\textsuperscript{207} Id. at 28, 39, 127. Participant Jones Transfer Co. had called the Commission’s attention, with regard to FAK rates, to a series of flat charges in effect on Michigan interstate shipments, of course. See note 153, supra, and accompanying text.
\textsuperscript{210} Restructuring Proceedings, supra note 1, at 128.
\textsuperscript{211} Id.
\textsuperscript{212} Id.
ting of need for new carriers in the small shipment field. Yet, as the historical study herein showed, the Commission had, for over twenty years, encouraged the specialization of carriers in the small shipment area. Not only had UPS received a series of grants of authority over the vehement protests of numerous parties, but other small shipment specialists had been successful in obtaining authority to serve the shipping public in this area. Indeed, the Commission had been a sympathetic audience for shippers who wished to support new entrants in the small shipment area.

Thus, the mere support for small shipment specialists is not to be equated with the commencement of a new trend. However, the Commission’s encouragement of specialization can be very significant if the words are followed by action on the part of the Commission. For example, the Commission expressed support for the concept that there was not only the need for specialization in the small shipment area, but the small shipment area itself could be subdivided into four further specialties. If the Commission, in applications for operating authority, recognizes the small shipment specialty and subspecialties, and adds or detracts from the protests of existing carriers, including general freight carriers, based on that recognition, then new entrants may actually be tempted to enter this field. As the Commission pointed out, it is not inherently unprofitable if it is treated as a specialty. Yet, it is submitted that when they were faced with the opposition of general freight carriers, potential entrants in the past may have been deterred from even attempting to enter the small shipment field. This stalwart opposition was by the same general freight carriers that stated that this traffic was unprofitable to them. At the same time, the Commission has encouraged the general freight carriers to set up separate divisions to handle small shipment traffic. Presumably, in this manner, the general freight carriers could establish the same specialized systems that have made the transportation of small shipments profitable for other concerns.

If new entrants are attracted into the field and general freight carriers are persuaded to establish separate divisions for the handling of small shipments, innovations with regard to operations in this field would necessarily follow, improving service and reducing prices. The test of the policy statement will come, however, when the Commission is faced with operating rights applications in the small shipment field. The policy statement must be translated into a working rule of application in operating rights proceedings.

The Commission addressed other service innovations, including such suggestions as pooling, transportation facilitation centers, and the permissi-

213. In Ex Parte No. MC-120, Petition to Relax Entry on the Transportation of Small Shipments Weighing 500 Pounds or Less, the Commission has before it a proposal submitted by a passenger carrier, Trailways, Inc., to make a general finding of public convenience and necessity in the small shipment area. This is now pending before the Commission. 43 Fed. Reg. 37329 (1978).
bility of various levels of service. The Commission indicated that it was receptive to virtually any new ideas to improve service in this area. Legislation was suggested in the area of loss and damage claims, uniform size and weight restrictions on the highways, and pooling, in order to facilitate the remedies in these areas. In the entire service area, however, the most important of all developments is the authorization of new service and the encouragement of general freight carriers to establish separate divisions for the handling of small shipments. The operating efficiencies referred to by the Commission will only be utilized effectively to the extent that carriers do in fact specialize in small shipments—then, the various innovative devices cited by the parties will become meaningful and cost-saving to the motor carrier industry. Similarly, new technological developments for material handling in the transportation of small shipments can be expected to accompany the specialization.

In the rate area, the Commission warned initially, as it had in the past, that it was the duty of carriers to present rate proposals to the Commission. Yet, after making this general statement, the Commission proceeded to discuss specifically the proposals submitted by both carriers and shippers in the rate area, indicating specifically which areas were acceptable to it. This was exactly the leadership which had been requested by the MC-82 Bureaus, and it represents an important step in any solution of the pricing problems that have traditionally confronted small shipments. This lack of leadership, in the past, has slowed a solution to the small shipment problem substantially. The ICC's reluctance to establish any guidelines or guiding principles is perhaps understandable, it should be noted, in light of recent court actions which have specifically nullified attempts by the ICC to be aggressive in this area. Indeed, the courts have seemed only too ready to examine in meticulous detail, not matters of general policy, but minute and detailed economic procedures and judgments made by the Commission.

At the same time, the Commission, in matters such as its controversial platform study, delayed too long in commencing its search for a replacement after it became apparent that the initial platform study was inadequate in several respects. Although costing may not yet be a science, it is impermissible to shrug away costing deficiencies for art's sake.

The Commission, in Ex Parte No. MC-98, did provide some specific guidelines for the motor carrier industry in the area of small shipment tariffs. Specifically, it prescribed the publication of separate pickup rates apart from line-haul and delivery rates. It also supported aggregate tender rates. Moreover, it stated that it would not consider prepaid discounts to be discriminatory, if in fact they are based upon carrier cost savings. These developments, led by the publication of separate pickup charges and line-haul and delivery charges, should have an effect in reducing shippers' cost in
the transportation of small shipments as well as in encouraging carriers to transport their small shipments in a more efficient manner.

As the Commission, in the service area, supported certain legislation, the Commission, in the rates area, instituted two new rulemaking proceedings. The released rates proceeding, specifically related to the issue of released rates in small shipment tariffs, has the promise of allowing service to be provided at still lower cost while providing the shipping public with the alternative of moving their small shipments at full value.\textsuperscript{214} The other investigation, that relating to the classification system, goes to the very core of the construct of a small shipment tariff. The Commission, in denying the FAK rate approach of Tariff 499, indicated its adherence to the National Motor Freight Classification once again. The Commission, it is submitted, did not give due weight to the systems of flat charges that are already in effect today, such as those cited by Jones Transfer. At the same time, the general investigation into the classification system, and the relative merits of the National Motor Freight Classification (as opposed to the Coordinated Freight Classification in use in New England) will provide needed hard data in this area. Also, an opportunity will be presented for parties to present ways in which the use of FAK rates would not discriminate against consistent shippers of lower-rated commodities. Moreover, the Commission's reluctance to eschew the National Motor Freight Classification on all small shipments is understandable in light of the court decision in National Small Shipment Traffic Conference, Inc. v. United States,\textsuperscript{215} in which Judge Friendly redressed the Commission for ignoring, contrary to the dictates of the Act, classification principles.

VI. CONCLUSION

Ex Parte No. MC-98 is by no means a final solution to the small shipment problem.\textsuperscript{216} It does seem, however, to be the most positive step to date in the struggle with this vexing, amorphous problem. It certainly represents, furthermore, a retreat from the narrow, reflexive reaction exhibited by both shippers and carriers in earlier proceedings.\textsuperscript{217} The recommenda-

\textsuperscript{214} The Commission contemplates, in the rate-making proceeding, the establishment of a two-tiered rate structure for small shipment tariffs, with the shipper having freedom to choose lower rates on goods moving at less than full value or higher rates on shipments transported at actual value.


\textsuperscript{216} Ex Parte No. MC-98 is not administratively final. Petitions for administrative review were filed by RCCC, ECMTA, Middle Atlantic Conference, The New England Motor Rate Bureau, and the Rocky Mountain Motor Tariff Bureau, Inc., all five of which are carrier groups.

\textsuperscript{217} This reflexive reaction against change was decried by Commissioner Arpaia (dissenting) when he stated that

[\textquoteleft]there is nothing in the act which permits us to condemn a rate merely because it departs from a tradition. Indeed, we should not be governed by the dead hand of the past, but
tions reached by the Commission in this proceeding are, to a very great degree, the result of the thought-provoking input of the various shipper, carrier, and governmental participants. If these recommendations are in fact utilized by the Commission in its day-to-day decision making, both rate and service problems (from the standpoint of shippers and carriers) should be decreased dramatically. This, perhaps, is the most important qualification of all, for much of what was said in Ex Parte No. MC-98 with regard to both service and rates was merely a reiteration, for both the Commission’s benefit and the benefit of the parties which appeared before it, of past principles, enunciated in a more positive and meaningful way.

should permit the carriers subject to our regulation to initiate departures from the conventional to attain lawful ends. As a matter of fact, if it were otherwise, we would be in the position of the author of the rhyme:

"I do not like thee, Doctor Fell;
The reason why, I cannot tell;
But this I know, and know full well,
I do not like thee, Doctor Fell."

Surcharge on Small Shipments Within Central States, 63 M.C.C. 157, 205 (1954). For many years, it is submitted, shippers and carriers alike were in the position of the author of the poem. The resulting frustration was best expressed in Ex Parte No. MC-98 by Arthur W. Todd:

Once upon a time, when we were very little, there was a small boy (not this respondent) whose manners were impeccable and whose emotions were human who, when he was very angry, could think of no better expletive than "streetcar." Today, perhaps "streetcar" is the only expletive that has not been used by one party or another, with respect to "the small shipment problem."

International Air Transportation: The Effect of the Airline Deregulation Act of 1978 and the Bermuda II Agreement

BENJAMIN A. SIMS

INTRODUCTION

In an effort to assess the future of United States international air transportation, this article will focus upon the historic private, as well as recently enacted statutory and administrative, mechanisms which have brought U.S. international air transportation to its present status. It will be seen that there are a considerable number of often conflicting or competing interests which must be balanced, such as those of the consumer, U.S. scheduled international and domestic air carriers, U.S. charter and cargo air carriers, U.S. foreign policy, foreign air carriers, and foreign governments. The Bermuda agreements between the U.S. and the United Kingdom of Great Britain and Northern Ireland will be studied with emphasis upon Bermuda II,

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1. Though nonexistent at the beginning of this century, the air transportation industry generated passenger revenues on United States international trunk carriers for the 12 months ending in June 1978 of $2,985,000,000, and over 3,927,783 passengers were enplaned. Civil Aeronautics Board, XI-2 AIRLINE INDUSTRY QUARTERLY ECONOMIC REPORT 8 (Sept. 1, 1978); Civil Aeronautics Board, XXIV-6 AIR CARRIER TRAFFIC STATISTICS 15 (June 1978).

which has been characterized as "the greatest step backward in forty years of attempting to bring market-oriented competition to international aviation." Part of the problem will be found to be a result of the changing and often fragmented approach to negotiations by the U.S. Departments of State and Transportation, the Civil Aeronautics Board, and other interested parties. Finally, recommendations will be made to remedy defects in the current structure used for negotiations in the international air arena.

I. HISTORICAL

The establishment of the principle of sovereignty over national airspace has served to check and regulate the admission of aircraft over a state's territory as well as requiring that permission to cross it be obtained. Thus, the establishment of international airways and landing rights has become a matter of negotiation or diplomacy between states and, in a number of cases, between states and private airlines or associations.

In an attempt to reach a multilateral agreement, the United States convened the International Civil Aviation Conference in Chicago in 1944. While the U.S. advocated virtually unfettered freedom of the air through the so-called "five freedoms," only the first and second freedoms were even-


5. U.S. DEPT' OF STATE, 1 PROCEEDINGS OF THE INTERNATIONAL CIVIL AVIATION CONFERENCE (1948) (hereinafter cited as CHICAGO CONFERENCE). The Soviet Union was not represented because Portugal, Spain and Switzerland participated. These countries were accused by the Soviet Union of possessing Axis sympathies. W. O'CONNOR, ECONOMIC REGULATION OF THE WORLD'S AIRLINES 29 (1971).

6. The "five freedoms" were set forth in the International Air Transport Agreement. Under it, each contracting state grants to the other contracting states the following freedoms of the air in respect of scheduled international air services:

   (1) The privilege to fly across its territory without landing;
   (2) The privilege to land for non-traffic purposes;
   (3) The privilege to put down passengers, mail and cargo taken on in the territory of the State whose nationality the aircraft possesses;
   (4) The privilege to take on passengers, mail and cargo destined for the territory of the State whose nationality the aircraft possesses;
   (5) The privilege to take on passengers, mail and cargo destined for the territory of any other contracting State and the privilege to put down passengers, mail and cargo coming from any such territory.

tually adopted because of the regulatory requirements espoused by the Europeans. The Chicago Conference did attempt, however, to partially by-pass the stalemate concerning the third, fourth, and fifth freedoms by promulgating a provisional agreement form to be used by those negotiating these rights bilaterally.\(^7\)

The U.S. proposed that economic decisions as to fares, frequencies, and routes would be left to the will of the affected airlines subject only to restrictions placed on the airlines by their own governments. Aside from the CAB certification to fly a particular route, U.S. international airlines would legally be subject to no economic regulation since the CAB was powerless to control international fares. Although the U.S. envisioned this proposal as the international implementation of the American free enterprise system which provided for competitive pricing and ease of entry, U.S. domestic aviation was heavily subsidized through concealed operating subsidies, and other nations recognized this.\(^8\)

Because the Europeans possessed devastated economies and obsolete aircraft and related equipment, they believed that a competitive market would have meant extinction of their meager aviation resources. Additionally, the Europeans had long resorted to adopting anti-competitive devices as an accepted method of protecting national interests. The British, who then articulated the European position, have remained consistent to the present in demanding a regulatory authority over the control of routes, rates, and schedules.\(^9\)

Although the Chicago Conference did not resolve matters involving economic regulation, it did set up the International Civil Aviation Organization (ICAO) to "study any matters affecting the organization and operation of international air transport, including the international ownership and operation of international air services on . . . routes . . . ."\(^10\) The ICAO has

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\(^7\) CHICAGO CONFERENCE, supra note 5, at 127-129.

\(^8\) Note, The Ins and Outs of IATA: Improving the Role of the United States in the Regulation of International Air Fares, 81 YALE L.J. 1102, 1111 (1972) [hereinafter cited as Ins and Outs of IATA]. The federal government gave Pan American and its subsidiary Pan American-Grace $47,202,000 in subsidy for the 11 fiscal years July 1, 1929, through June 30, 1940. Curiously, the subsidy received by all U.S. domestic carriers during this same period was $59,852,000 even though the domestic carriers had flown eight times the passenger miles that Pan American flew. The federal government had also expended some $126,468,000 on the construction and maintenance of domestic airway facilities. W. BURDEN, THE STRUGGLE FOR AIRWAYS IN LATIN AMERICA 116-17 (1943).

\(^9\) Address by Lord Swinton, Chairman, United Kingdom delegation to Chicago Conference (Nov. 2, 1944), CHICAGO CONFERENCE, supra note 5, at 63-67. Compare Lord Swinton's speech with Bermuda II, supra note 2.

avoided, thus far, any participation in international ratemaking. 11

Because the governments were unable to solve the economic problems, the International Air Transportation Association (IATA) was resurrected in 1944 from its prewar demise. 12 The airlines had originally formed IATA in 1919 "with a view to cooperate to mutual advantage in preparing and organizing international aerial traffic." 13 It originated as a private association of airline operators and remains such today. It must be recognized that most of the airlines in the association are solely or largely owned by their governments. The unwritten reason for the revival of this organization was that IATA would provide informal ratemaking and allocation of the air passenger and cargo market. 14

Shortly after Articles of Association were approved for IATA in April 1945, Pan American Airways announced plans to reduce its transatlantic fares by approximately thirty percent. 15 This act was responsible for consternation on the part of Great Britain, which had been active in lobbying for rate control in international aviation. Pan American’s act provided, in part, the impetus for the first Bermuda agreement. 16

A. Bermuda I.

The first Bermuda bilateral [hereinafter Bermuda I] agreement arose as a result of a conference between the United States and Great Britain in Bermuda in January 1946. 17 This agreement served as a model for most of the bilateral agreements to which the United States has been a party. The significance of this agreement was that the United States agreed to IATA’s economic regulation in return for Great Britain’s dropping of its demand for control over the number of flights over any specific route which would be offered by either party’s airlines. 18 Bermuda I provided, in effect, that each nation’s airlines would be allowed to provide capacity based upon their estimates of traffic demands.

IATA was to be the moving force in the setting of fares in international

13. Historical Survey, supra note 4, at 42.
    tariff negotiations are described in Gazdik, Rate-Making and the IATA Traffic Conferences, 16 J.
    Air L & COM. 298 (1949). See also, Note, Impact of Technology on IATA Ratemaking: Problems,
15. The one-way fare was to be $275.00. See H. J. SMITH, AIRWAYS ABROAD 10-14 (1950).
16. Id.
17. Bermuda I, supra note 2. Bermuda I is actually the Chicago Conference form with an
    "annex" which contains the provisions of the routes and rate controls. In 1948, the U.S. incorpo-
    rated the "annex" provisions involving IATA into a new form currently known as the "Bermuda
    form." Both "Chicago" and "Bermuda" forms can be found at 3 Av. L. Rep. (CCH) ¶ 26,306-
    26,307 (June 9, 1958).
18. Bermuda I, supra note 2, at annex § II.
air travel under the Bermuda I agreement, which was designed in the belief that IATA would normally reach such agreement. Additionally, it was contemplated that the agreed fares would be approved by the governments whose carriers negotiated them. Paragraphs (e) and (f) of Bermuda I reserved to governments party to Bermuda I-type agreements the right to disapprove IATA rate agreements.\(^{19}\) Although these provisions had the effect of allowing party governments to regulate fares directly, the provisions were impractical means of rate setting. In regard to the U.S., these powers were largely meaningless, at least as far as the CAB was concerned, since the CAB has never possessed the power to invoke paragraph (e)\(^{20}\) and has only recently explicitly possessed any power to wield authority concerning the right of summary action under paragraph (f).\(^{21}\)

**B. THE DOMESTIC BACKGROUND**

Before launching into a discussion of the current approach to international air negotiations, it will be helpful to briefly survey the domestic regulatory climate from a historical and current perspective. Such an approach will reveal many of the current conflicting demands which have arisen as a result of past regulatory practices. Until recently, the approach to international aviation regulation stemmed in large part from the economic and political climate of the 1920's and 1930's.\(^{22}\) The Transportation Act of 1920\(^{23}\) shifted the regulatory philosophy toward the encouragement of the orderly development of the air industry and away from attacking concentrated power. The Civil Aeronautics Act of 1938\(^{24}\) arose from the philosophy produced by the forces responsible for the Transportation Act of 1920.\(^{25}\) The purpose of the 1938 Act was to thwart existing competitive forces and limit entry, in addition to fostering orderly promotion and devel-

\(^{19}\) Bermuda I, supra note 2, at annex § II, ¶¶ (e) and (f).

\(^{20}\) This is the view of the CAB and the Department of State. See G. Edles, Legal Bases for Scheduled and Charter Air Transportation and the Future Direction of International Aviation Policy 20 (1975) (unpublished S.J.D. thesis, George Washington Univ.) [hereinafter cited as Edles]; M. STRASZHEIM, THE INTERNATIONAL AIRLINE INDUSTRY 214 (1969) [hereinafter cited as Straszheim]. Some commentators have focused on the lack of this power in the CAB prior to 1972, but have failed to realize that it may reside in either Congress or the Executive Branch, although not delegated. See, e.g., INS AND OUTS OF IATA, supra note 8, at 1145. But see R. BERGER, EXECUTIVE PRIVILEGE 117-62 (1974), where Professor Berger concludes that Congress is the repository of such power. Regardless of who possesses such power, it is clear that the United States does have the power to suspend.


\(^{22}\) Edles, supra note 20, at 22.

\(^{23}\) Transportation Act of 1920, Pub. L. No. 64-152, 41 Stat. 456 (1920).


\(^{25}\) Edles, supra note 20, at 22.
opment of the existing airline industry. The clamor for regulation came surprisingly from the fledgling airline industry and not from consumers or government.26

There were, however, unsuccessful attempts made by Pan American during the 1930's to achieve legislation which would directly or indirectly allow the carrier to possess unregulated control over its international operations.27 Had Pan American's view been accepted it would have burdened the Executive Branch with understandings and agreements between foreign nations and Pan American or other private carriers. Fortunately, the Civil Aeronautics Act of 1938 provided that the CAB must conduct its business in conformity with United States international commitments.28 However, the international airlines were left to their own devices to a much greater extent than domestic airlines since international airlines were not regulated in regard to adequacy of service or fares and rates. Because of the foreign policy implications of international air traffic, the President has ultimate control of entry. This power has been criticized as too broad since the President has not been limited solely to foreign policy considerations.29 In fact, the Standing Committee on Aeronautics Law of the American Bar Association in 1974 supported legislation which would remove presidential review of CAB actions concerning overseas or foreign air transportation based on economic and domestic political considerations.30 Under the ABA proposal the President would retain his "rights and obligations in the fields of national defense and foreign relations . . . .," and a plaintiff would also be assured of the availability of judicial review.31

Although it is reasonable to remove domestic political considerations from the President's decision-making process, removing economic factors is impossible since economic factors are the paramount reasons for bilateral and multilateral agreements. It appears that the ABA did not want economic factors of either domestic or international import to be considered since the resolution speaks of "removing economic and domestic political

26. See, e.g., Letter from Ass't Secretary of Commerce J.M. Johnson to Senator McCarran (Dec. 16, 1936); letter from Postmaster General J.A. Farley to Senator Wheeler (Mar. 11, 1937), both reprinted in Regulation of Transportation of Passengers and Property by Aircraft: Hearings Before the Subcomm. on S.2 and S.1760 of the Senate Comm. on Interstate Commerce, 75th Cong., 1st Sess. 89, 140 (1937) [hereinafter cited as 1937 Senate Hearings]. The War Dep't was neutral concerning the proposed legislation. 1937 Senate Hearings at 47.

27. See testimony of Comm'r Joseph Eastman, id. at 70; testimony of Edgar S. Gorrell, id. at 511.


31. ABA, supra note 30.
considerations..." so only political considerations were limited in a domestic sense. Not allowing the President to consider international economic factors would deny the President the power to consider the single most important element of the decision-making process in international relations. By so limiting his considerations, situations may result in which a foreign flag or U.S. airline would be added to a list of carriers operating between the U.S. and other countries even though the economics dictated otherwise. One such situation arose when Pakistan International Airlines was granted a route between the U.S. and Pakistan solely because the Executive Branch had a bilateral agreement with Pakistan, despite the fact that economic conditions did not support such entry.33

The Airline Deregulation Act of 1978,34 signed by the President on October 24, 1978, has incorporated the provisions of the ABA resolution by use of the following language:

The President shall have the right to disapprove any such Board [CAB] action...solely upon the basis of foreign relations or national defense considerations... but not upon the basis of economic or carrier selection considerations.35

The "economic" statutory limitation appears to be ill-advised and will no doubt be the cause of a great deal of litigation and controversy since foreign policy concerns embrace economic issues as well as narrowly political ones. Additionally, this provision could force the President to use the more cumbersome, and less sure, bilateral negotiating process to accomplish foreign policy objectives based on economic issues. The President could use this authority to negotiate bilateral air transport agreements to circumvent decisions of the CAB involving carrier selection or economic considerations, and the CAB would be obligated to accede to the resulting agreement since it must exercise its duties in compliance with treaties, conventions, or agreements in force between the U.S. and foreign govern-

32. Id. (emphasis added).
33. Pakistan Int’l Airlines Corp., Foreign Air Carrier Permit, 33 C.A.B. 687, 691 (1961). This author does not insist that economic considerations should prevail over other considerations; allowing Pakistan to enter the market may well have been a correct decision in that instance. Although this decision was made at a time when the President was permitted to consider international economic factors, logic dictates that, if economics is not to be considered, the problem will arise much more frequently.
35. Id. at § 34. The "carrier selection" language was added largely due to the controversy surrounding the President’s disapproval of a route award between Dallas-Fort Worth and London by the CAB to Pan American in 1977. President’s Announcement to Expand Air Service between the U.S. and Europe, 13 WEEKLY COMP. OF PRES. DOC. 1910 (Dec. 21, 1977). Pan American argued that the CAB should have allowed a period for reconsideration prior to its order implementing the President’s dictates. Pan American felt that the President had acted on "legally defective data and a misconception of his authority." The CAB denied Pan American’s request for further consideration citing Chicago & Southern Air Lines v. Waterman Steamship Corp., 333 U.S. 103, 109 (1948).
ments. Since the agenda in formal bilateral negotiations cannot be unilaterally determined by the U.S., legislation which forces the President to resort to that mechanism will certainly be more costly to the U.S. than if the problem were resolved in the course of section 801 review of the CAB decision.

Under the President’s review of CAB decisions, where the President disapproves the "issuance, denial, transfer, amendment, cancellation, suspension, or revocation of, and the terms, conditions, and limitations contained in, any certificate authorizing an air carrier to engage in foreign air transportation, or any permit . . . to any foreign carrier . . . ," the President must set forth his reasons in a public document to the extent that national security permits, within sixty days of submission of the CAB’s action to the President. Whereas the previous statute gave the President power over both overseas air transportation (between or within the U.S. and its territories and possessions) as well as in foreign air transportation (between the U.S. and its territories and possessions and any place outside it), the current statute limits the President’s power to foreign air transportation. However, as in the previous statute, foreign air transportation includes U.S. international carriers as well as non-U.S. citizen international carriers.

Normally, judicial review of CAB orders is vested in the federal courts of appeals, upon petition filed within sixty days after entry of the order, by "any person disclosing a substantial interest in such order," or later upon a showing of "reasonable grounds" for failure to file within the required time. An exception is in respect to orders relating to foreign air transportation subject to the President’s approval under 49 U.S.C. § 1461(a). These orders cannot be reviewed unless the CAB action is not disapproved within sixty days and the action takes effect as a CAB action and not one of the President.

38. See Hearing on International Aviation before the Subcomm. on Aviation of the Senate Commerce Comm., 95th Cong., 2d Sess. 11 (1978) [hereinafter cited as Hearing on Int’l Aviation] (statement of Hon. Brock Adams, Sec. of Transp.).
44. Airline Deregulation Act of 1978, Pub. L. No. 95-504, § 34, 92 Stat. 1705 (to be codified in 49 U.S.C. § 1461(a)). A pertinent portion of this provision reads: "Any such [CAB] action not disapproved within the foregoing time limits shall take effect as action of the [CAB], not the President, and as such shall be subject to judicial review as provided in [49 U.S.C. § 1486] of this Act."
This language from the 1978 Act attempts to avoid some of the effects of *Chicago & Southern Air Lines v. Waterman Steam Ship Corporation* by further subjecting certain CAB orders to judicial review. *Waterman* held that orders of the CAB as to certificates for overseas or foreign air transportation are not mature and are therefore not susceptible to judicial review. Also, they are not reviewable after approval by the President since they then embody Presidential discretion beyond the competence of courts to adjudicate. It is significant that the President's powers under 49 U.S.C. § 1461 have remained unchanged from *Waterman* until the 1978 Act. The 1978 Act curiously states that the President "shall have the right to disapprove" CAB actions within his purview, but nowhere does this 1978 Act mention that the CAB action shall be "subject to the approval of the President" as did the 1958 Act. Thus, it could be argued that even if the President approves the CAB action, the action is judicially reviewable as an action of the CAB under a strict reading of the 1978 Act which denies judicial review only to presidentially disapproved actions of the CAB. Such an interpretation would allow virtually every presidential act to be litigated including disapprovals, indirectly, because disapproved CAB actions are normally modified in accordance with the President's desires and will be subsequently approved in modified form. It would appear that such review would be an unconstitutional infringement on the President's foreign relations and national defense prerogatives. At the least, the difference in language between the two acts is striking and further litigation will be necessary to determine proper legal parameters. It is suggested that the proper interpretation of this provision is that judicial review is proper only when no action is taken by the President or the President's approval or disapproval was clearly not based on his foreign relations or national defense powers.

There is also legal authority allowing judicial review of CAB action where it is alleged that the CAB acted in excess of its powers and notwithstanding the President's prior approval.

Under S.3363, a bill introduced by Senators Cannon and Pearson in

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To compound the problem, Executive Order No. 11,920, 3 C.F.R. 121 (1977), issued by President Ford, states in part:

Orders involving foreign and overseas air transportation certificates of U.S. carriers that are subject to the approval of the President are not subject to judicial review when the President approves or disapproves an order for reasons of defense or foreign policy. All disapprovals necessarily are based on such a Presidential decision, but approval by the President does not necessarily imply the existence of any defense or foreign policy reason.

45. 333 U.S. 103, 114 (1948).

46. Id.


1978, the President would have power over only non-U.S. citizen carriers and he would have only ten days in which to disapprove a CAB order in connection with international air transportation. It is not clear whether some portions of S.3363 may be reintroduced in the 1979 session of the Senate. There are, however, some provisions of the Senate bill which the Airline Deregulation Act of 1978 did not address, so it is reasonable to believe that S.3363 is not completely dead.

II. AIRLINE DEREGULATION ACT OF 1978

Certain aspects of the Airline Deregulation Act of 1978 have been briefly touched upon previously. Because it is anticipated that this Act will in the future create significant changes in foreign air commerce and that its effect will no doubt be reflected in bilateral and multilateral negotiations, significant features of this far-reaching Act will be set forth coupled with contrasting aspects of the Federal Aviation Act of 1958 which have been superseded as well as those which survive. Among the major provisions of the Airline Deregulation Act of 1978 [hereinafter 1978 Act] are those eliminating the CAB by 1985 and the move away from economic regulation toward free competition. This sweeping change toward complete competition was apparent even prior to the 1978 Act in actions of the CAB. Such changes may be welcome in the domestic area, but could cause problems in the international area by creating pressures which privately owned and financed U.S. airlines may not be capable of withstanding. This author concludes that although some competition should be the goal in the international sector, close scrutiny of foreign governmental action should be employed during the transitional and later periods.

When Pan American asked for freedom from governmental regulation in the 1940's, that airline was in the preeminent position competitively and could vie effectively with other nations' airlines. By mid-1970, Pan American had been forced to furlough large numbers of its flight crews due to depressed economic conditions and over-capacity created by introduction of the jumbo jets. As of August 1978, despite nearly two years of strong growth in international air transportation, Pan American has been unable to recall forty percent of these flight crews. Also, U.S. airlines' share of in-

49. S.3363, 95th Cong., 2d Sess., § 8 (to amend § 601(a) & (b) of the Federal Aviation Act of 1958, 49 U.S.C. § 1461 (1976)).
52. Hearing on Int'l Aviation, supra note 38, at 152 (statement of Richard Smith, Director of Legislative Affairs, Flight Engineers Int'l Ass'n).
ternational traffic is now down to forty percent. On the other hand, the 
foreign flag carriers across the North Atlantic are subsidized either directly 
or indirectly in the acquisition of equipment and other expenses. In fact, 
almost all European airlines are now state-owned, as are most other airlines 
outside the U.S. The Export-Import Bank also subsidizes competition by 
foreign airlines against U.S. airlines by making available favorable financial 
terms unavailable to U.S. carriers in our own "free market" financial cen-
ters. Other factors which affect U.S. airlines' ability to compete effec-
tively internationally are the relatively higher U.S. labor costs and the 
conscious effort of foreign governments to give their "chosen instru-
ments" the choicest "feed-in" and "beyond" route systems that funnel 
traffic over their transatlantic routes.

An illustration of the situation which existed as of August 1978 be-
tween Germany and the U.S. will show the changing balance. Lufthansa 
provides nonstop service to four German and four U.S. cities. Pan Ameri-
ican provides nonstop service to only one of each. Lufthansa operates 
fifty nonstop frequencies weekly each way compared to only thirteen 
by Pan American, none by TWA, and two by National. The same imbal-
ance exists in a number of other markets. Whether the Airline Deregula-
tion Act of 1978 will ameliorate or exacerbate this problem is as yet 
undetermined. Hopefully, the airline industry will not suffer the fate of 
the U.S. maritime industry.

The statement of the joint House and Senate conferees on S.2493, 
amending the Federal Aviation Act of 1958, indicated that the 1978 Act 
would "encourage, develop, and attain an air transportation system which 
relies on competitive market forces to determine the quality, variety, and 
price of air services . . . ." Specifically, the 1978 Act has added cer-

53. Id. at 2.
54. STRASHEIM, supra note 20, at 19.
55. See Hearings before the Subcomm. on Aviation of the Senate Comm. on Commerce, 
Science and Transp., 95th Cong., 1st Sess. 20-21 (1977) [hereinafter cited as Senate Aviation 
Hearings-1977].
56. Flag carriers owned and subsidized by the state are normally called "chosen instru-
ments."
57. Hearings on Int'l Aviation, supra note 38, at 6 (statement of R. Smith). "Feed-in" normally 
describes traffic ducted into specific routes, while "beyond" traffic, in relation to Country A, for 
example, is that traffic which is being carried on Country B's aircraft to a destination beyond 
Country A.
58. Id. at 7 (statement of R. Smith). TWA operates to Frankfurt via Paris, but is not a real factor 
in the market.
59. Id. at 8 (statement of R. Smith). Airlines which overwhelm the market with more service 
than all U.S. carriers combined are: SAS, KLM, and Swissair.
60. Twenty-five years ago the U.S. merchant marine carried 60% of our national ocean com-
merce whereas today its share is about 5%. See id. at 5.
61. S. REP. NO. 95-1779, 95th Cong., 2d Sess. 53 (1978) [hereinafter cited as CONFERENCE 
REPORT].
tain factors which the CAB shall consider "among other things, as being in the public interest, and in . . . the public convenience and necessity . . . ." 62 By separately setting forth "Factors For Foreign Air Transportation," 63 the 1978 Act indicates the distinctiveness which embraces foreign air commerce. The earlier act as amended in 1977 had no such separate provision. The language in the 1978 Act is designed to promote "adequate, economical, and efficient service . . . at reasonable charges, without unjust discriminations, undue preferences or advantages, or unfair or destructive competitive practices." 64 Competition was apparently believed by the legislation's authors to be needed "to the extent necessary to assure the sound development of an air transportation system properly adapted to the needs of the foreign and domestic commerce of the United States, of the Postal Service, and of the national defense." 65 The significant differences between the domestic portion of the 1978 Act and the foreign air portion are reflected by the fact that the CAB is obligated to consider the following factors, among others, in respect to interstate and overseas air transportation (both considered domestic aspects): (1) availability of adequate, economic, efficient, and low-priced services by air carriers without unjust discriminations, undue preferences or advantages, or unfair or deceptive practices; (2) need to coordinate transportation by air carriers; (3) need to encourage fair wages and equitable working conditions; (4) placement of maximum reliance on competitive market forces and on actual and potential competition; (5) need for prompt decision-making; (6) responsiveness to the public; (7) adaptation to needs of domestic and foreign commerce of the United States, the Postal Service, and the national defense; (8) prevention of unfair, deceptive, predatory, or anticompetitive practices; (9) avoidance of unreasonable industry concentration, excessive market domination, and monopoly power; (10) other (unnamed) conditions that would allow carriers unreasonably to increase prices, reduce services, or exclude competition; (11) reliance on actual and potential competition to provide efficiency, innovation, and low prices, and to determine the variety, quality, and price of air transportation services, and (12) encouragement of entry into new markets, additional markets, and the continued strengthening of small air carriers.

In contrast, the portion of the new legislation regarding foreign air transportation contains less of an emphasis than does the domestic portion on the prevention or avoidance of "unreasonable industry concentration, 66

63. Id. § 3(c) (to be codified in 49 U.S.C. § 1302).
64. Id. § 3(b) (to be codified in 49 U.S.C. § 1302).
65. Id.
66. Id. § 3(a) (to be codified in 49 U.S.C. § 1302(a)).
excessive market domination, and monopoly power..."67 Additionally, there is basically the same emphasis on competition, but with the use of considerably fewer words. The domestic legislation is cluttered with redundancies,68 which may nevertheless be determined judicially or administratively to possess inherent and distinctive meaning. In any event, much litigation will likely ensue over the meaning of the 1978 Act's terminology.

Previous caselaw shows that the courts apply a presumption against competition. It is not clear to what extent the current legislation will revise this presumption. If it is concluded that the legislation, contrary to the caselaw, creates a presumption in favor of competition, then cases such as Continental Air Lines, Inc. v. CAB69 and Big Bear Cartage, Inc. v. Air Cargo, Inc.70 would no longer appear to be dispositive, at least as far as their holdings that there is no presumption in favor of competition. Even if a presumption favoring competition is invoked, it can be rebutted by showing, at least in the international area, that the questioned practice is unreasonable; is unjustly discriminatory; creates undue preferences or advantages; is unfair or destructive; does not contribute to the sound development of air transportation adapted to the needs of the foreign and domestic commerce of the United States, of the Postal Service, or of the national defense; does not promote air safety; does not promote sound economic conditions in air transportation; does not improve relations between air carriers; does not coordinate transportation by air carriers; and does not promote, encourage, and develop civil aeronautics.71

It should not be concluded that even if such a presumption of competition has preeminence in the domestic area that it should also prevail in the foreign air circumstance. Foreign policy, at least at present, requires nations to agree upon a common course to meet problems. Competition is not the only consideration internationally. That is not to say that negotiations should not attempt to create conditions in which legitimate competition can exist. Unfortunately, the present international climate does not allow competition to predominate.72

Aside from pure economic regulation, entry into international air carriage must be "required by the public convenience and necessity" before a

certificate can be issued to a U.S. carrier. In the domestic sector, such transportation must be merely "consistent with the public convenience and necessity . . . ." Thus, the burden under the new law is much greater for a U.S. carrier to prove that it is "required" to enter the foreign market than for it to enter the domestic or overseas market. Although the present administration and the CAB are favorably disposed to freedom of entry into foreign markets, this statute, under less favorable views, could be used to deny entry. Also, this provision favors existing U.S. international carriers by preserving current foreign markets at least for the short term. At the same time, non-U.S. carriers are not required to meet the onerous "required by the public convenience and necessity" order of proof before permits are issued to them. Thus, even currently certificated U.S. international carriers will ultimately suffer due to these differing legal standards of treatment. Realism requires that foreign policy interests be considered in international air traffic; however, it does not appear to be in the best interests of the United States, from both a competitive and foreign policy viewpoint, to impose this additional impediment on U.S. carriers and not on foreign carriers. This disparate standard forces the CAB to discriminate against U.S. carriers in favor of foreign citizens and current international carriers.

U.S. carriers operating in foreign transportation have been subjected to a variety of "discriminatory and unfair competitive practices in their competition with foreign air carriers." Under the International Air Transportation

73. Airline Deregulation Act of 1978, Pub. L. No. 95-504, § 8, 92 Stat. 1705 (to be codified in 49 U.S.C. § 1371(d)(1)(B)) (emphasis added). See, e.g., Pan American-Grace Airways, Inc. v. CAB, 342 F.2d 905 (D.C. Cir. 1964), cert. denied 380 U.S. 934 (1964). However, the "public interest" involved in an obligation under a bilateral agreement between sovereigns cannot be equated with the "public convenience and necessity" which is the criterion for granting air routes to domestic carriers.


75. 49 U.S.C. § 1372 (1976), which pertains to permits to non-U.S. citizen foreign air carriers, provides:

The [CAB] is empowered to issue such a permit if it finds that such carrier is fit, willing, and able properly to perform such air transportation and to conform to the provisions of this chapter and the rules, regulations, and requirements of the [CAB] hereunder, and that such transportation will be in the public interest.


76. 49 U.S.C. § 1159b (1976). Airport user fees are weighted against transatlantic traffic. Great Britain adds on a 15% return in order to provide it a profit. Considering the fact that the British government owns British Airways, its major airline, this fee appears to be particularly discriminatory. In 1974, TWA was charged $4.5 million at Heathrow airport for landing fees, parking charges, and terminal traffic control. In 1978, that charge is estimated to be approximately $7 million. Enroute navigational charges, which are not assessed by the U.S., have been increased 300% by the British. Senate Aviation Hearings-1977, supra note 55, at 25 (statement of C.E. Meyer, Jr., president, Trans World Airlines).
Fair Competitive Practices Act of 1974, the Congress has required the Department of State, the Department of the Treasury, the Department of Transportation, the CAB, and other departments or agencies to review these practices and to "take all appropriate actions within [their] jurisdiction to eliminate . . . discrimination or unfair competitive practices . . . ."

During the latest reported year, the CAB notified Congress, as required by 49 U.S.C. § 1159b(c), of complaints of discriminatory and unfair competitive practices on the part of twenty-one foreign jurisdictions against U.S. carriers. Little was accomplished in response to the complaints due to the inertia of foreign bureaucracies. What is surprising, however, is that there was little action taken other than note passing even in some cases which warranted retaliatory action. For example, an unfavorable competitive position is imposed on Pan American vis-à-vis Aeroflot, the Soviet airline, due to currency and ticketing restrictions imposed by the Soviet Union. Civil negotiations, at the time of the latest report to Congress, had proved unproductive.

In an effort to strengthen U.S. international carriers, the CAB had prior to the 1978 Act granted authority to these carriers to carry domestic passengers on some domestic legs of their foreign flights. In addition, Congress has enacted a broadening of this right by allowing such carriers to transport persons, property, and mail between domestic U.S. points. This legislation will enable Pan American in particular, and other U.S. international carriers in general, to benefit from the additional revenues these domestic passengers and cargoes will provide in filling up previously wasted space. Additionally, travelers will benefit from the anticipated lower fares.

Probably the most significant feature of the 1978 Act is the provision for eventual transfer, on January 1, 1985, of CAB authority over foreign air transportation to the Department of Transportation. The statute provides that this power will be exercised by DOT in "consultation" with the Depart-

78. Id.
79. [1977] CAB ANN. REP. 102-12. Complaints were lodged in fiscal year 1976 against the following countries: Argentina, Australia, Brazil, Canada, Chile, Columbia, Egypt, Federal Republic of Germany, Greece, India, Indonesia, Iran, Italy, Japan, Mexico, Philippines, Poland, Singapore, United Kingdom, U.S.S.R., and Venezuela.
80. Id. at 107. Pan American announced on Oct. 25, 1978 that it had cancelled its flight no. 67 from Moscow. WGMS Radio, Wash., D.C., Oct. 25, 1978. Another example is that although Hungary had agreed in 1975, to act as the sales agent for the U.S. designated airline, Hungary had made not one sale for the U.S. airline even though the U.S. airline had operated out of Budapest during the two years in which no sale had been made. See note from the U.S. Embassy to the Hungarian Ministry of Foreign Affairs, May 24, 1977, T.I.A.S. No. 8617.
ment of State.\textsuperscript{63} One unanswered question is how the DOT will administer its responsibility and authority. It is likely that many of the employees and officers of the CAB will move to the DOT and that, in some respects, the DOT will function much as did the CAB. Close study of the 1978 Act reveals that the DOT will apparently receive considerable authority in regard to foreign air transportation, such as: (1) issuing certificates to U.S. carriers for foreign scheduled and charter air transportation for both permanent and temporary transportation based on the DOT determination that the carrier is "fit, willing and able" to perform such transportation and that the service is required;\textsuperscript{64} (2) designating terminal and intermediate points where it is deemed practicable;\textsuperscript{65} (3) attaching "closed-door restrictions" to certificates;\textsuperscript{86} (4) granting permits subject to Presidential approval to noncitizen foreign air carriers;\textsuperscript{67} (5) rejecting tariffs;\textsuperscript{88} (6) transportation of mail;\textsuperscript{89} and (7) other statutory duties of the CAB.\textsuperscript{90} Significantly, most of the domestic regulatory schemata concerning interstate and overseas air transportation are phased out in the time period between 1979 and 1985 while being retained in the foreign arena. One major easing of restrictions in foreign air transportation is that U.S. international charter carriers will not be barred by statute from carrying foreign charter passengers on the same flight with scheduled passengers.\textsuperscript{91} By January 1981 charter certificate holders may

\textsuperscript{63} Id. \textsection 40(a) (to be codified in 49 U.S.C. \textsection 1551).

\textsuperscript{64} Id. \textsection 8 (to be codified in 49 U.S.C. \textsection 1371(d)(1)(B), (2)(B), (3)(B).

\textsuperscript{65} Id. \textsection 40(a) (to be codified in 49 U.S.C. \textsection 1551).

\textsuperscript{86} Id. \textsection 16 (to be codified in 49 U.S.C. \textsection 1371(e)(7)). Closed door restrictions are defined as "any condition attached to a certificate to provide interstate or overseas air transportation . . . which prohibits such air carrier from providing local passenger service between any pair of points between which it is authorized to operate . . . " (emphasis added). This amendment takes away power to impose "closed door restrictions" on such certificates. Since by definition such restrictions are not legal in foreign air transportation, international carriers must file to remove such restrictions. If competition is truly desired, "close door restrictions" should not be imposed on U.S. international carriers except where exigent circumstances such as bilateral or multilateral agreements require them.

\textsuperscript{67} Id. \textsection 40(a) (to be codified in 49 U.S.C. \textsection 1551).

\textsuperscript{88} Id.

\textsuperscript{89} Id. The 1978 Act does not make clear how much the Postal Service is to participate with the DOT in this area. The Sunset Provisions (Title XVI of the Act, providing for transfer of CAB authority) are ambiguous and any of the following propositions could be argued: (1) the DOT has the complete authority, (2) the Postal Service has the complete authority, or (3) both share the authority in some undefined manner. The question results because section 40(a) of the 1978 Act gives the authority of the CAB to the Postal Service only with respect to "interstate and overseas air transportation." Both are domestic types of air transportation. 49 U.S.C. \textsection 1301(21) (1976).


\textsuperscript{91} See id., \textsection 20. The reader is reminded that "overseas" and "foreign" are not the same. The omission of this provision with regard to foreign transportation appears significant. In any event, even overseas or domestic charter flights will not be limited by this restriction after 1981. Id., at \textsection 40(a).
sell or offer for sale individual tickets for an inclusive tour directly or indirectly to the general public. This is something the Air Charter Tour Operators of America have opposed on the ground that a charter- or airline-controlled tour operator is anticompetitive.\(^2\)

The legislation, although purporting to give all the authority of the CAB to the DOT, recites in a subsequent provision that the authority of the CAB relating to foreign air pooling and other anticompetitive-type practices is transferred to the Justice Department.\(^3\)

The provisions of the 1978 Act relating to pooling and similar anticompetitive agreements require approval by the CAB of any agreement affecting foreign air transportation.\(^4\)

Pooling agreements may be to the benefit of the U.S. in the international sphere especially where without such agreements a U.S. carrier would withdraw from a route leaving only foreign carriers to serve it. Pan American ended its Moscow-New York service on October 25, 1978, after ten years of unsuccessfully attempting to make a profit. Pan American was barred by diplomatic arrangements from selling its own tickets and was prevented by antitrust regulations from pooling its revenues with Aeroflot, the Soviet airline, even though other foreign airlines flying into the Soviet Union engaged in that practice. Pooling arrangements should be allowed in particular situations where without them the U.S. would lose a market.\(^5\) The CAB is empowered to and should approve such agreements where they are not "'adverse' to the public interest."\(^6\)

In contrast, any air carrier entering into an agreement affecting interstate or overseas air transportation is not required to file such agreement before the CAB even though the CAB is required to disapprove such parts which are "'adverse to the public interest, or in violation of [the 1978 Act] . . . ."\(^7\) By placing the mandatory filing requirement only on international agreements, the 1978 Act misplaces the emphasis because there are fewer reasons to disapprove such pacts external to the U.S. This requirement connotes that such pacts affecting foreign air commerce are less fa-


\(^4\) *Id.* § 28(a) (to be codified in 49 U.S.C. § 1382(a)) states that "'every carrier shall file [memoranda, contracts or agreements] affecting foreign air transportation . . . ."' (emphasis added). Pooling is a practice that permits companies to combine passenger revenues to equalize income.


vored than are domestic pacts when the reverse is implied by other provisions of the 1978 Act.\textsuperscript{98}

A third transfer of authority from the CAB concerns mail rates in foreign air transportation. The transfer will be to the DOT since the statute specifically empowers the Postal Service to exercise authority only over interstate and overseas air transportation.\textsuperscript{99} It is not clear why Congress apparently gave the mail rate power over foreign air transportation to the DOT.\textsuperscript{100} It may have been an unintentional omission to exempt mail in foreign air transportation as a Postal Service responsibility especially since the DOT presumably has no particular expertise in postal rate negotiations or competitive bidding. Since the Postal Service currently has developed the procedures and organization to implement the law\textsuperscript{101} concerning interstate, overseas and foreign airmail transportation, it would be wasteful and duplicative to require the DOT to set up an organization and procedures for only the foreign sector.\textsuperscript{102} Since the Secretary of State and the Postal Service currently negotiate with the Universal Postal Union and foreign countries concerning mail rates, it would be preferable not to inject another government agency into the process.\textsuperscript{103}

Congress recognized the revolutionary aspects of the 1978 Act and thoughtfully gave itself an opportunity for retrenchment or revision by requiring periodic assessments and reports by the CAB during a series of dates up through January 1, 1984.\textsuperscript{104} The CAB is required to assess items pertinent to international air commerce, such as competition, pricing, agreements affecting the degree of competition within the industry, the degree to which the administrative process has been expedited under the 1978 Act, the degree to which beneficial or detrimental changes have been made upon the traveling and shipping public, Postal Service, national defense, and air carriers, the impact upon the United States-flag foreign air transportation system, and a comparative analysis of procedures in regard to Presidential approval or disapproval of foreign air routes under 49 U.S.C. § 1461 as amended by the 1978 Act.

Additionally, the CAB must provide the Congress with a "detailed


\textsuperscript{99} Id. § 40(a) (to be codified in 49 U.S.C. § 1551).

\textsuperscript{100} See Conference Report, supra note 61, at 120. The conference report states simply that the "CAB's authority to set mail rates is transferred to the Postal Service."


\textsuperscript{102} The Postal Service could consult with the Department of State just as easily as can the DOT. Thus, where negotiations are required with foreign governments, the Postal Service, which is familiar with the requirements of mail handling, would be the logical choice rather than the DOT.


opinion' as to whether the public interest requires continuation of the CAB beyond its currently scheduled termination in 1985. If the CAB concludes that it should continue to exist, then "detailed recommendations" concerning revisions to the 1978 Act are required by Congress in order to insure "continued improvement of the United States air transportation system." Finally, there are listed a number of procedural elements outlining how the CAB should prepare its submission of the comprehensive review.

It is hoped that before 1985 there will be clarification of how transfer of authority under the 1978 Act will take place, exactly what authority will be transferred, which agency or agencies will wield it, and, procedurally, how airlines and consumers will obtain administrative relief from problems that arise. Nevertheless, the 1978 Act is a good beginning toward fostering the goals of the U.S., and Congress is apparently prepared to revise its method in reaching those goals should conditions so require.

III. FOREIGN POLICY ASPECTS OF AIR TRANSPORTATION

As previously discussed, the current political climate dictates that competition be a paramount aim to the extent compatible with the public interest. An additional element generally not considered in regard to interstate or overseas air transportation is that of foreign policy. The President's power and critical role in this regard has been discussed above,105 and the CAB's limited control over suspension and rejection of rates in international air transportation has been examined. Because of these limitations, the manner in which routes, capacity, and other economic aspects have been decided is through the use of bilateral and multilateral agreements along with IATA agreements. The Bermuda I-type agreement is still the basic agreement between the U.S. and foreign governments even though the Bermuda II agreement has supplanted the original Bermuda I agreement between the United States and the United Kingdom.

A review of statements of international air transportation policies by Presidents during the 1970's reveals that competition among and between U.S. carriers and foreign carriers has been the primary goal. For example, competition,

tends to improve the quality and variety of service to the public, keeps prices reasonable, and enlarges the market for all carriers. The United States should maintain a flexible policy on certificating competition among U.S. carriers on international routes. The policy should also distinguish between point to point competition of U.S. carriers and services to a particular foreign country from different sections of the United States. Within this framework, there may be future route possibilities for new U.S. carriers, as well as the present ones. U.S. carriers should adequately serve their certificated routes and every effort should be made to improve U.S. carrier competitive performance vis-a-vis for-

105. See text accompanying note 35 supra.
eign carriers.\textsuperscript{106}

The U.S. policy for the conduct of international air transportation negotiations has translated goals into negotiating objectives which, although sketchy, provide the negotiator with at least an articulated objective. These objectives will presumably be presented in negotiations as an integrated U.S. position, but it must be recognized that this policy cannot be implemented unilaterally and must be achieved within the international framework:

1. creation of new and greater opportunities for innovative and competitive pricing that will encourage and permit the use of new price and service options to meet the needs of different travelers and shippers;
2. liberalization of charter rules and elimination of restrictions on charter operations;
3. expansion of scheduled service through elimination of restrictions on capacity, frequency, and route and operating rights;
4. elimination of discrimination and unfair competitive practices faced by U.S. airlines in international transportation;
5. flexibility to designate multiple U.S. airlines in international air markets;
6. [encouragement] of maximum traveler and shipper access to international markets by authorizing more cities for non-stop or direct service, and by improving the integration of domestic and international airline service, and
7. flexibility to permit the development and facilitation of competitive air cargo services.\textsuperscript{107}

The latest policy statement was issued partially in response to outrage voiced by carriers, consumers, shippers, and Congress over the Bermuda II agreement. This statement was an effort to tell foreign governments that the U.S. would not be using the Bermuda II agreement as the new model. However, it must be noted that policy statements do not have the binding effect of legislation.

Specifically, Bermuda II did the following:

1. It imposed a restriction on the number of U.S. flag carriers that the U.S. could designate in United Kingdom markets.
2. It established a mechanism that allowed the British government to control increases in frequency—and thus capacity—on the North Atlantic.
3. It sharply limited the beyond points to which U.S. airlines could carry United Kingdom fill-up traffic, including stopover or interline connecting traffic, although the loss of these rights was partially offset by allowing U.S. airlines to carry online passengers to any beyond points.
4. It provided for specific frequency restrictions on certain operations in the Pacific and in round-the-world operations.

\textsuperscript{106} International Air Transportation Policy, 6 WEEKLY COMP. OF PRES. DOC. 804 (JUNE 22, 1970). For earlier policy issues see generally Ryan, Policy Issues in International Air Transportation, 16 GEO. WASH. L. REV. 443 (1948).

\textsuperscript{107} Briefing by President Carter, United States Policy for the Conduct of International Air Transportation Negotiations (Aug. 21, 1978) (press release, Office of the White House Press Secretary).
5. It prohibited nonstop service from a number of U.S. cities.
6. It restricted the ability of carriers to change schedules to meet public demand.\footnote{108}

This agreement represents a substantial departure from the kind of system envisioned by Congress and generally incorporated into other bilateral agreements. President Carter initially lauded the Bermuda II agreement as being "consistent with [the] objective [of] healthy economic competition among all air carriers . . . [and its] quality, its fairness, and its benefits to the consumer and to the airlines should make it last as long as the original 1946 Bermuda agreement."\footnote{109} However, the President later impliedly denounced the Bermuda II agreement in a letter to the Honorable Griffin Bell as Bell was preparing to negotiate with the Japanese, who are extremely protective of their carriers and restrictive in regard to other countries' carriers:

\begin{quote}
We should seek international aviation agreements that permit low-fare innovations in scheduled service, expanded and liberalized charter operations, nonstop international service, and competition among multiple U.S. carriers in markets of sufficient size. We should also avoid government restrictions on airline capacity. While keeping in mind the importance of a healthy U.S. flag carrier industry, we should be bold in granting liberal and expanded access to foreign carriers in the United States in exchange for equally valuable benefits we receive from those countries. Our policy should be to trade opportunities rather than restrictions.\footnote{110}
\end{quote}

Notwithstanding the rhetoric, at least one principal question remains unanswered. Who should be responsible for making, carrying out, and reviewing international aviation policy? The Bermuda II negotiations displayed serious defects in the organization of the U.S. negotiating team, the advice which it received from its advisors, and its actual negotiations with the other government. Alan S. Boyd was detailed as a special ambassador on a short-term basis for the negotiations. Such a practice "is an aberration and should be seen as such."\footnote{111} Generally, such a procedure should be avoided since it can lead to agreements at odds with the overall U.S. policy. Additionally, there were key affected parties, such as the airport operators and charter operators, who were not regularly consulted. As a result, many of the U.S. proposals were "inconsistent with, or contradictory to, existing legal, contractual, historical and practical circumstances . . . ."\footnote{112} As a

\footnote{108. See generally, Bermuda II, supra note 2.}
\footnote{109. Hearings on Int'l Aviation, supra note 38, at 84.}
\footnote{110. Id. at 42-43.}
\footnote{111. Id. at 74.}
\footnote{112. Id. at 55-58, 32-43. The Airport Operators Council International, Inc. adopted the following in response to the Bermuda II negotiations:}

\textit{Policies to be advocated by the U.S. government in bilateral air services agreement negotiations with other governments should only be developed after consultation with AOCl to ensure proper recognition of U.S. airport operator interests. Consultation on policies involving airport user charges and other operational considerations affecting airport eco-}
consequence, Bermuda II may be viewed as creating the potential for the following situations:

1. The restrictions on capacity and number of U.S. carriers able to serve particular pairs of cities constitute a serious reduction in U.S. carrier competitive opportunities which will seriously deteriorate service and market development.

2. Bermuda II may induce other countries to pressure the U.S. to negotiate agreements with them on similar terms.

3. The agreement will decrease U.S. flag carriers’ market share with associated U.S. balance of payments consequences.\textsuperscript{113}

Although it is too early to discover whether the ultimate effect of Bermuda II will be detrimental, the U.S. has recently concluded agreements which have been heralded as “significantly [expanding] the opportunities for low-fare competitive services, both scheduled and charter . . . .”\textsuperscript{114} As an example, the Netherlands agreement generally provides that fares and rates for traffic moving from one country to the other on scheduled air services are subject to the sole control of the first country. The belief is that since presumably there will be a minimum of governmental interference, the “free play of normal market forces [will be] to the benefit of the consumer.”\textsuperscript{115}

It is significant that these agreements have been negotiated with small countries who have much to gain from expanded opportunities in serving the U.S. with its vastly greater traffic potential and multiple gateways.\textsuperscript{116}

In an effort to demonstrate to European nations that airline competition can work in international markets, the CAB recently granted scheduled flight authority to two charter and two scheduled airlines to fly between several U.S. cities and Belgium and Amsterdam.\textsuperscript{117} There is no doubt that all other countries will be watching this experiment to see if it might benefit


\textsuperscript{115} Netherlands’ Press Release, supra note 114.

\textsuperscript{116} As an example, the U.S. will have the right to serve Amsterdam and points beyond, while the Netherlands will be able to serve New York, Chicago, Houston, Los Angeles and another point to be selected by the Netherlands. Id. Thus, the Netherlands’ potential for increasing its share of the traffic market is greatly improved by this agreement while the U.S. appears to gain acceptance of its view that “protectionism and cartelization are anachronisms . . . . and are an inefficient way of achieving [its] national aviation objectives.” Wash. Post, Sept. 6, 1978, at D1, col. 1.

\textsuperscript{117} See id. The article said that the CAB wanted to show that international competition could work as well as domestic competition. Perhaps the CAB was referring to non-price competition.
them. The U.S. must remember in analyzing the results that although competition is desired, such competition must not be accompanied by predatory pricing and other policies which may be instituted by foreign governments on their chosen instruments in an effort to attract a larger share of the market than could be obtained by normal competition.

An additional area of conflict concerns which agency should have primary responsibility for negotiating international air agreements. The recent negotiating team has consisted of a head negotiator from the Department of State, and others from the CAB and DOT.\textsuperscript{118} S.3363 would modify this by establishing within the office of the President an Office of International Aviation Negotiations headed by a Director and Chief Negotiator [hereinafter Director] who would be appointed by the President with the advice and consent of the Senate.\textsuperscript{119} The Director would have the rank of ambassador, thereby avoiding the problem of disparate ranks which forced the President to appoint a special ambassador to the Bermuda II negotiations.\textsuperscript{120}

Assisting the Director would be special counsels appointed by the CAB, the DOT and the Secretary of State. These four parties would be collectively known as the Aviation Policy Committee and would be responsible for formulating a U.S. international air transportation policy which shall "[emphasize] the greatest degree of competition that is compatible with a well-functioning international air transportation system."\textsuperscript{121}

because until recently no price competition existed. Additionally, it is too early to say that domestic competition is working.

\textsuperscript{118} Hearing on Int'l Aviation, supra note 38, at 23.
\textsuperscript{119} S.3363, 95th Cong., 2d Sess. § 9 (1978).
\textsuperscript{120} There were conflicts between agencies within the U.S. delegation and, in fact, within one agency. Joel Biller, chairman of the U.S. delegation, was in the unfortunate position of being out-ranked on the delegation. Those who considered this situation felt that because of the personality conflicts that developed, it would be impossible to hope to reach a reasonable agreement with the then head of the British delegation, and that the only way to effect a change in the constitution of the U.K. delegation was to bring about a change in the constitution of the U.S. delegation. Hearing on Int'l Aviation, supra note 38, at 75.
\textsuperscript{121} S.3363, supra note 119, § 9(g), (h). The proposed statute sets forth the following goals:

(1) freedom of air carriers and foreign air carriers to offer fares and rates which correspond with consumer demand;
(2) the fewest possible restrictions on charter air transportation;
(3) the maximum degree of multiple and permissive international authority for United States air carriers so that they will be able to respond quickly to shifts in market demand;
(4) the elimination of operational restrictions to the greatest extent possible;
(5) the integration of domestic and international air transportation;
(6) an increase in the number of non-stop United States gateway cities;
(7) opportunities for carriers of foreign countries to increase their access to United States points if exchanged for benefits of similar magnitude for United States carriers and the traveling public with permanent linkage between rights granted and rights given away; and
(8) the elimination of discrimination and unfair user fees, unreasonable ground handling requirements, undue restrictions on operations, prohibitions against change of gauge, and similar restrictive practices.
Since Congress has the power under the Constitution to "regulate . . . foreign commerce," 122 S.3363 has provided a means for exercise of this power. In order to insure Congressional oversight, at least one member of each House of Congress can attend international negotiations. 123 This provision is apparently an effort to counteract the thirty-year policy of precluding the Senate from considering executive agreements in international aviation, 124 and it reflects a renewed interest by the Congress in such negotiations.

The Aviation Policy Committee is obligated under S.3363 to "consult on a regular basis" with the International Aviation Advisory Council, which is composed of interested groups, and to "advise the Aviation Policy Committee on both broad policy goals and individual negotiations . . . ." 125

International aviation involves mixed questions of foreign policy and interstate and foreign commerce. Both the President and the Congress share responsibility within the Constitutional framework. Conflicts will arise as to whether the President or the Congress has usurped prerogatives not within the ambit of the asserting party. The Congress has sent a message to the President, in the form of the 1978 Act and S.3363, that his powers will be limited at least to foreign policy and defense considerations and that the Congress plans to play a more active role in regulating foreign commerce. If

123. S.3363, supra note 119, § 9(i).

Pending in the Senate Foreign Relations Committee presently are Montreal Protocols 3 and 4 of 1975, which would incorporate the Guatemala City Protocol to the Warsaw Convention pertaining to liability of the carrier for damages to international passengers.

When President Truman submitted the Chicago Convention to the Senate for ratification, his accompanying message acknowledged that other civil aviation agreements—including Bermuda I—had been consummated "under authority vested in me" but without submission to the Senate for ratification. International Civil Aviation Conference, message from the President, 92 CONG. REC. 6661-62 (1946).

125. S.3363, supra note 119, § 9(G). "[These groups] shall include representatives of the President's Domestic Council, the Department of Commerce, the Department of Defense, airport operators, scheduled air carriers, charter air carriers, airline labor, consumer interest groups, travel agents and tour organizers, and any other groups, institutions, or interest groups which the Director deems appropriate."
Congress intends to play this part, the first step should be for it to enact clear legislation setting forth the goals to be achieved in international air commerce. S.3363 does this. Additionally, Congress should be consulted before negotiations begin and observers should attend these negotiations on a regular basis. Although the Congress desires to be consulted, the Senate may require that it ratify any executive agreement, especially if another agreement similar to Bermuda II results. However, the President’s responsibility for foreign policy and national defense must be given deference by the Senate and the Courts in order to preserve the delicate balance between the branches of government. Foreign policy will contain economic elements which are inseparably intertwined and a recognition of that fact must exist. It is legally permissible for the Congress to deny the President the right to consider economics solely without regard to foreign policy, but the Congress cannot deprive the President of the right to consider the economic implications of foreign policy.

IV. OTHER CONSIDERATIONS AFFECTING FOREIGN POLICY

The Bermuda I-type bilaterals have relied on IATA to perform ratemaking functions since 1946. The IATA arrangement has been accepted largely because, until 1972, the CAB claimed that this arrangement was "the only opportunity available to it under existing legislation."\textsuperscript{126} Since 1972, the CAB has had the power to suspend and reject international fares.\textsuperscript{127} In 1978, after urging by the U.S. Department of Justice, the CAB began an appraisal of IATA carrier agreements when it issued an Order to Show Cause why the CAB should continue to approve such agreements.\textsuperscript{128}

One of the reasons that the CAB had approved previous agreements even though it disagreed with them was an effort "to avoid an open rate situation."\textsuperscript{129} "Open rate" is the term used for a situation where there is no agreement on rates, and the CAB feared that the result could be "an intergovernmental confrontation which could lead to a cessation of air services."\textsuperscript{130}

An illustration of a recent potential "open rate" situation occurred in mid-1972 which eighteen IATA North Atlantic carriers could not reach a consensus on revised fares, and intergovernmental consultations similarly did not result in an accommodation generally acceptable to all govern-

\textsuperscript{126} IATA Traffic Conference Resolution, 6 C.A.B. 639, 645 (1946).
\textsuperscript{128} Agreements Adopted by the Int’l Air Transport Ass’n Relating to the Traffic Conference, Docket No. 32851 (CAB Order 78-6-78, June 9, 1978).
\textsuperscript{130} Id.
ments.\textsuperscript{131} As a result, major foreign carriers filed individual tariffs reflecting the sharp fundamental disagreement on scheduled airline rate policy which had stalemated the multilateral negotiations. Because these tariffs were unacceptable to the CAB, it exercised its newly-granted statutory power\textsuperscript{132} to suspend the tariffs, finding that they bore little or no relationship to cost and would have a deleterious effect on carrier yield. Consequently, tariffs filed by Pan American, TWA and National were protested and rejected by several European governments pursuant to their respective bilateral agreements with the U.S. After consultation with the foreign governments, the CAB concluded that no agreement was possible and the failure of the CAB to approve the IATA carriers' agreement to extend the status quo through 1973 would create an unacceptable condition.\textsuperscript{133} The CAB then approved the North Atlantic rate agreements, dismissed a complaint against the fare structure and declined to institute an investigation into the rate structure of North Atlantic air fares. As a result, a petition was brought by users of transatlantic air services who were connected with the Aviation Consumer Action Project.\textsuperscript{134} The Court which reviewed the CAB action held that vague and unsubstantiated CAB fears anticipating chaos resulting from an open rate situation were insufficient to warrant automatic approval of unjustified IATA price hikes.\textsuperscript{135} The holding of the Court was based on the lack of "substantial evidence" that an "open rate" situation could cause significant harm to support the CAB order.\textsuperscript{136} Also, the Court felt that if the CAB's decision was adverse to foreign policy, the President could act under 49 U.S.C. § 1461 to set aside the CAB's suspension of any foreign airline's tariffs or landing rights in the United States.\textsuperscript{137}

A more recent case reflects the authority of the CAB to issue directives in respect to conduct of foreign nations in a foreign country, where such

\textsuperscript{131} Id. at 3.


\textsuperscript{133} Id. See also Pillai v. CAB, 485 F.2d 1018 (D.C. Cir. 1973). See generally 47 TEMP. L.Q. 620 (1974).

\textsuperscript{134} A non-profit public interest group formed by Ralph Nader.

\textsuperscript{135} See Pillai v. CAB, 485 F.2d 1018 (D.C. Cir. 1973).

\textsuperscript{136} In the year 1972, 582,411 United States citizens flew United Kingdom aircraft across the North Atlantic; U.S. passengers on the airlines of Germany, France, the Netherlands, Italy and Switzerland in the North Atlantic ranged from 364,803 to 214,520 passengers each. Two-thirds of the passengers on all eighteen carriers on the North Atlantic route are U.S. citizens. In these foreign countries the stake of the tourist industry—hotels, restaurants, bus and tour services, etc.—in addition to the U.S. passengers carried by their national airlines, is enormous.

\textsuperscript{137} Id. at 1024.

\textsuperscript{137} Bilateral negotiations might well be preferable from the United States' point of view. Along any single given route, the net amount of tourist travel and spending flows from the U.S. to the foreign country. In addition, the overall importance of foreign tourist dollars probably in each instance represents a much greater percentage in the economy of the foreign country than in the U.S.
conduct impinges upon commerce to or from the United States. In *Civil Aeronautics Board v. British Airways Board*, the suit arose when the United Kingdom Civil Aviation Authority (CAA), the equivalent of our CAB, directed British Airways to charge certain rates notwithstanding the CAB’s suspension of the rates. British Airways argued that the Federal Aviation Act should not be construed to apply extraterritorially to the charging of rates “in Britain by British Airways at the direction of the British Government...” It also argued alternatively that international law precluded the U.S. court “from enjoining conduct of foreign nationals in a foreign country which is required by the foreign sovereign.” Superficially, it appears that British Airways had been given a “Hobson’s choice” of either charging rates not approved by the CAB or of violating the directive of the British CAA. However, since British Airways is an instrumentality of the British government there was a unity of interest and not simply a situation of a private independent carrier being ordered to do something by its government. The U.S. District Court judge ruled that the British CAA directive could not “relieve British Airways from the generally recognized rule that one wishing to take advantage of the facilities of the United States commerce ‘must be willing to comply fully with United States law.’” It is thus clear that Congress could delegate, under the Commerce Clause, to the CAB, power to make extraterritorial application of the Federal Aviation Act.

These CAB powers of course do not extend to control of U.S. airlines landing or traversing a foreign country to the extent that foreign law governs. The case points out the difficulties inherent in international aviation

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138. This principle is well recognized. See, e.g., Deutsche Lufthansa Aktiengesellschaft v. CAB, 479 F.2d 912 (D.C. Cir. 1973).
139. 433 F. Supp. 1379 (S.D.N.Y. 1977). The CAB had rejected the British tariffs which proposed lower, discount rates in certain circumstances. Among other reasons given, the CAB stated that the tariffs violated its “seven cities” order which determined that a system of add-on charges to New York rates was an improper mode of arriving at rates for shipments destined for other U.S. cities. The CAB preferred a system of mileage-related charges which was designed to avoid shipper discrimination against certain less economical destination cities from the point of view of overall transportation costs.
141. Id. at 32.
and relations with governing bodies, and it indicates that foreign airlines generally have three options: (1) compliance with the laws of this country; (2) foregoing the pursuit of commerce with the U.S., \textsuperscript{146} or (3) its government can renew diplomatic efforts to achieve a mutually satisfactory agreement.\textsuperscript{147} U.S. carriers are faced with the same choices in regard to foreign countries. The meaning of this is clear—foreign diplomacy may be the only practical means to achieve a satisfactory solution to international aviation problems, especially if organizations such as IATA are unable to function.\textsuperscript{148}

**CONCLUSION**

The United States has long espoused competition under the free enterprise system. In practice, however, U.S. international carriers have operated under the aegis of IATA which has set fares and has been described as a "cartel."\textsuperscript{149} Although there has been some justification for this organization to set fares by private agreement which could not be legislated unilaterally, there is now some question whether IATA can continue to act in this manner. The CAB is investigating this IATA function, and if IATA ratemaking does not survive, then the U.S. will be forced into active international ratemaking by negotiation.

U.S. airlines will be competing more openly with foreign airlines. However, foreign airlines in most cases are government-owned or subsidized, so U.S. airlines will have difficulty if foreign governments choose to infuse money into their airlines in a predatory or uneconomical manner in order to drive U.S. carriers out of the market. As U.S. markets are opened to foreign airlines, the domestic consumer will benefit, at least during the short term, from decreased fares and greater availability of flights. Since the U.S. market is the largest in the world in terms of number of air travelers, the U.S. stands to lose its market share to other countries. The result may be a further decrease in U.S. carrier capacity in relation to foreign airlines. The balance of payments will likely be more adversely affected.


\textsuperscript{147} Cf. Kerr Steamship Co. v. United States, 284 F.2d 61 (2d Cir. 1960) (ICC inquiry into secret foreign contracts).

\textsuperscript{148} The Wall Street Journal reported that the airlines have approved a reorganization of IATA that would allow them to set their own fares. Under the new regulations, which still have to be approved by the respective governments, members will be required to adhere to standards of aircraft safety, baggage processing and interairline financial transactions, but participation in faresetting, called "tariff coordination" by IATA, would be on an optional basis. Wall St. J., Nov. 15, 1978, at 4, col. 3.

\textsuperscript{149} Hearings on Int'l Aviation, supra note 38, at 5 (statement of Aviation Consumer Action Project).
In any event, the Airline Deregulation Act of 1978 reflects the current mood that economic regulation over air transportation should be relaxed and that true competition should prevail. The international market is much different from the domestic market, and true competition will not be possible in the current international arena. In order to avoid complete economic decimation of our private international carriers, close scrutiny must be maintained over this situation to avoid predatory and detrimental practices by foreign governments. At the same time, we must recognize the legitimate aims asserted by other countries. The coming years will show whether international aviation will become a “free enterprise” arena or whether it will be forced to continue to reflect the economics of IATA.
The Scheduling and Route Impacts of Increased Fare Flexibility*

Mahlon R. Straszheim**

I. INTRODUCTION

On August 25, 1978, the Civil Aeronautics Board adopted modifications to its policies developed in the Domestic Passenger Fare Investigation (DPFI) which allow increased pricing flexibility to scheduled air carriers.¹ This article will discuss the likely effects of the enacted rule on route abandonment and service.

Airline fare regulation has historically limited the range of price and service options² and has resulted in costly competition in schedules and amenities.³ The new rule offers the promise of significant benefits to travel-

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* This article was originally commissioned by the Public Interest Economics Center (PIE-C) on behalf of the Federal Trade Commission (FTC), and was submitted as an appendix to an FTC report presented to the Civil Aeronautics Board on May 10, 1978. It does not necessarily reflect the views of the PIE-C or FTC.

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ers in the form of lower air fares and services more closely aligned with consumer preferences. The introduction of fare flexibility under the rule will increase the number of passengers carried and result in changes in schedule frequency in a number of markets. The nature of the changes will depend on the elasticities of demand, carrier costs, and carrier route network adjustments. Changes in capacity and service frequency in particular markets are the logical consequences of instituting fare competition and airline service more responsive to passengers' preferences.

It has been argued that permitting more fare competition and the associated changes in schedules is potentially harmful to the public interest. The often-voiced concern is that destructive price competition will undermine service and lead to much route abandonment, particularly to small communities. The CAB correctly minimizes this risk in discussing its enacted rule, for the evidence presented below suggests there is little risk of a substantial loss of air service to small communities as a result of the rule. The principal arguments of this article, developed in the four sections which follow, can be briefly summarized.

The second section of the article outlines the basic rationale of the rule in the context of the current market regulatory environment. In introducing a "suspend-free" zone as a means for permitting fare flexibility, the CAB properly notes that an industry-wide fare formula cannot properly reflect all the special features of costs or market potential which will differ among carriers and markets. Carrier managements are best capable of making accurate predictions of consumer preferences in different markets. The rule is therefore an important and timely step toward a more rational airline system, allowing carriers to introduce fare changes when they think consumers' preferences favor this type of service.

The third section of the article reviews the recent experience of route changes under CAB regulation. The issues are whether the objective of assuring service to small communities is well served by a continuation of present CAB rate, entry, and subsidy policies, and whether service quality to smaller communities under the rule would be worse than under present CAB entry and fare regulation. It will be shown that CAB regulations have done relatively little to assure the continuation of air service to small communities which could not be achieved by fare flexibility under the rule. The exit of local scheduled carriers from small community service has been quite dramatic in the last decade under CAB regulations. This has been accompanied by a very considerable increase in scheduled service provided by commuter carriers.

The fourth section of the article analyzes the argument that carriers currently "cross-subsidize" low-density routes in small communities, and that fare reductions in denser markets will therefore undermine service in less-dense markets. This argument is suspect on both theoretical and em-
pirical grounds. The fourth section of the article discusses the theory of cross-subsidy as it relates to airline network configurations and pricing and scheduling decisions in particular submarkets. There is no economic justification for carriers cross-subsidizing unprofitable routes under the current price and entry regulations or in an unregulated market environment. Because airline route systems consist of many independent subnetworks, changes in rates, revenues, or schedule frequency in many submarkets will have no impact on the profitability of other components of a carrier’s route system and hence will not affect carriers’ decisions in those markets. The principal conclusion is that the current pricing regime does not “cross-subsidize” low-density routes serving small communities.

The final section analyzes what types of service changes might occur under a regime of fare flexibility represented by the rule. Most of the fare reductions will likely be concentrated in denser markets. To the extent that scheduled carriers reduce service in selected smaller markets, commuter carriers will be quick to enter. There is little basis for concluding that major cutbacks in service will result.

II. THE RATIONALE FOR THE RULE

The introduction of fare flexibility by creating a “suspend-free” zone is an important step in making the airline system more responsive to underlying consumer preferences. Major consumer benefits in the form of lower fares are likely to result. The disadvantages of an industry-wide fare structure when differences exist among markets in traveler preferences are evident. The responsibility for tailoring fare and service to consumer preferences is most appropriately placed with carrier managements, who have both better information than regulators to make such decisions and a very direct stake in the outcome of their decisions.

The introduction of price competition through a “suspend-free” zone will encourage experimentation and the generation of information needed to formulate optimal fare and service levels. There is necessarily some uncertainty about consumer preferences. Absent such experimentation in the market, administrative decisions over fare and service options must be made with too little information. Permitting carriers to adjust prices based on their expectations of financial profitability for different types of service in particular markets is the best means for determining underlying consumer preferences.

The CAB’s proposed criteria for suspension are an important dimension which will increase the likelihood of successful fare and service innova-

4. A “suspend-free” zone is a range of fares within which carriers are free to lower or raise fares without submitting economic data otherwise required by the CAB economic regulations, supra note 1.
tion under the rule. The opportunity for carriers to change fares without submitting the economic data presently required by the Board’s Economic Regulations\(^5\) gives carrier managements considerably more flexibility. The CAB in its discussion properly notes the burden of these submissions and their inhibiting effect on fare experimentation.

The new rule’s provisions for suspension of a proposed fare require that complainants make a strong showing that a fare reduction is unlawful, predatory, and would cause irreparable harm if enacted.\(^6\) Placing the burden of proof on complainants reflects a balancing of the possibility that the alleged harm would in fact occur with the offsetting injury to the traveling public that would be deprived of lower fares if an unnecessary suspension occurred. The CAB’s position in this regard reflects the view that the public benefits of lower fares under the rule are substantial, that the opportunity for fare reductions is unlikely to result in destructive competition or predatory prices on any significant basis, and that the usual basis for injunctive relief provides adequate protection for complainants.

III. SERVICE AND ROUTE CHANGES UNDER CAB REGULATION

Service to small communities has historically been affected by CAB regulation of entry and fares and the subsidy payments to local service carriers. The payment of subsidy is intended to finance local service airline operations in low-density markets, and the CAB’s control over entry and exit decisions has the potential of influencing service levels. Concern has been voiced that service to small communities will be much worse under the rule, and that retaining present CAB policies with respect to fares, entry, and subsidy is vital to the continuation of air service to small communities. A review of the history of service under CAB policies suggests that prevailing policies have made very little contribution to air service to small communities.

Regulation of the airline industry by the CAB under the Federal Aviation Act as amended\(^7\) has pursued several objectives, including promotion and regulation of the industry to “‘foster sound economic conditions’” and to provide for “‘competition to the extent necessary to assume the sound development of an air transportation system properly adapted to the needs of the foreign and domestic commerce of the United States . . .’”.\(^8\) Service to small communities in which traffic levels would not sustain profitable operations has been subsidized by the CAB under the statute, beginning in 1945.\(^9\) In 1955 permanent certificates were granted to local service carri-

\(^{5}\) 14 C.F.R. § 221.165 (1978).
The CAB's entry and subsidy policies appear to have yielded only marginally more scheduled service to smaller communities and lower-density routes than would exist in the absence of CAB regulation. The CAB's policies with respect to entry by trunklines might best be described as a cautious policy, permitting entry when the harmful effects on an incumbent carrier's profitability would not be significant, and allowing exit when carriers could show the service to yield sub-normal rates of return. Growth of traffic has, however, permitted some increase over time in the number of markets with more than one carrier. The share of revenue passenger-miles in 1972 in monopoly markets has declined over time to 23.2%. A large number of willing applicants for entry to particular markets exists at all times. The CAB has been relatively lenient in allowing exit, and has no statutory authority to impose restrictions on the type of equipment or service frequency if carriers provide minimum service. Trunk carriers serve only a fraction of the possible city-pair markets within their route authority; trunks have also exited from many markets when profit prospects have been unsatisfactory. A summary of these route changes appears in Table 1. As indicated, trunk carriers served only 180 points in the 48 contiguous states in 1975, versus 210 in 1970 and 315 in 1960.

**TABLE 1**

Points Served by Certificated Carriers
48 Contiguous States

<table>
<thead>
<tr>
<th>Year</th>
<th>Trunk Carriers</th>
<th>Local Service Carriers</th>
<th>All Carriers</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>Points Authorized</td>
<td>Points Suspended</td>
<td>Points Served</td>
</tr>
<tr>
<td>1955</td>
<td>376</td>
<td>27</td>
<td>349</td>
</tr>
<tr>
<td>1960</td>
<td>328</td>
<td>13</td>
<td>315</td>
</tr>
<tr>
<td>1965</td>
<td>231</td>
<td>8</td>
<td>223</td>
</tr>
<tr>
<td>1970</td>
<td>228</td>
<td>18</td>
<td>210</td>
</tr>
<tr>
<td>1971</td>
<td>228</td>
<td>18</td>
<td>210</td>
</tr>
<tr>
<td>1972</td>
<td>222</td>
<td>15</td>
<td>207</td>
</tr>
<tr>
<td>1973</td>
<td>221</td>
<td>19</td>
<td>202</td>
</tr>
<tr>
<td>1974</td>
<td>208</td>
<td>16</td>
<td>192</td>
</tr>
<tr>
<td>1975</td>
<td>198</td>
<td>18</td>
<td>180</td>
</tr>
</tbody>
</table>

1. As of December each year.
2. Includes points served jointly with local service carriers.
3. Includes points served jointly with trunk carriers.


10. A local service carrier is one that provides "air service of a short-haul, low-density nature operated generally between smaller outlying communities and major traffic hubs." **G. EACOS,** supra note 3, at 3. Trunk carriers, on the other hand, serve principally long haul markets and heavily traveled segments between major cities. **W. JONES, CASES AND MATERIALS ON REGULATED INDUSTRIES** 1087 (1976).

11. CAB SPECIAL STAFF REPORT ON REGULATORY REFORM 47 (1975).
Local service carriers' networks have also changed quite substantially in recent years. Local service carriers served 380 points in 1975, versus 433 in 1970 and 459 in 1960. There are two principal causes of these changes. The CAB has attempted to limit the size of subsidy to local service carriers by allowing carriers to exit from low density routes. Under the CAB's "use it or lose it" policy, many cities were deleted from the local service carriers' networks when traffic levels fell below established minimums. Second, local service carriers' managements have redefined their objectives in recent years; most appear to seek entry into trunk markets of medium density and to become small trunk carriers. The conversion to jet aircraft is both a cause and a reflection of this change in objectives. Efficient use of jet aircraft requires longer-haul, denser routes than characterized the local service carriers' networks in 1960. The CAB has allowed local service carriers to enter denser routes, in many instances replacing service of trunk carriers, and has permitted exit from more marginal routes. As the local carriers' fleets become more dominated by jet aircraft, the scheduling problems of efficiently using smaller aircraft are accentuated. Local service carriers appear destined in many instances to virtually complete exit from very low density service which they traditionally provided. This reduction in service by local service carriers to smaller communities has occurred under existing CAB regulation.

The exit of local scheduled services has been accompanied by a very considerable growth in service by commuter carriers. Commuter carriers operate under part 298 of the CAB's Economic Regulations. Commuter carriers' operations are neither subsidized nor regulated, with carriers free to enter and charge any price. The exemption from certification under section 401(a) of the Federal Aviation Act enjoyed by commuter carriers derives from the requirement that commuter carriers operate aircraft with a maximum passenger capacity of thirty passengers and a maximum payload of 7,500 pounds. The commuter carriers have in some instances received permission under the exemption authority vested in the CAB to operate larger aircraft. Most of the commuter carriers' fleets are comprised of small aircraft, in the fifteen to nineteen seat range.

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12. The evaluation in local service carriers' route and investment decisions and its interrelationships with CAB regulation is described in G. Eadz, supra note 3.
13. Commuter air carrier is defined in the economic regulations as "an air taxi operator which (1) performs at least five round trips per week between two or more points and publishes flight schedules which specify the times, days of the week and places between which such flights are performed, or (2) transports mail by air pursuant to contract with the United States Postal Service. 14 C.F.R. § 298.2(f) (1978).
The market opportunity to which commuter carriers have responded is the willingness of travelers in small communities to pay for high frequency service on small aircraft. In a number of instances, local service carriers have contracted with commuter carriers to provide 'replacement service', allowing the local service carrier to meet its obligations under its route certificate in the market in question in this fashion. Allegheny has pioneered this approach. In some cases, the local service carrier has a financial obligation under the agreement. These arrangements reduce subsidy costs to the taxpayer, and also provide a more frequent service to the cities in question than the local service carrier could provide with larger aircraft. As of July 26, 1977, agreements at 53 replacement points in 23 states and involving 24 carriers had been approved by the CAB.\textsuperscript{16}

Commuter service has grown considerably more rapidly than scheduled local or trunk service. In 1976, 85 commuter carriers served 300 airports and 746 city-pairs, carrying 7.3 million passengers. This represents a 9.4% annual rate of growth since 1970, versus 5.0% annually for the scheduled domestic carriers over this same period.\textsuperscript{17}

The majority of commuter service is to small communities, of less than 75,000 people. Table 2 summarizes growth in service by type of carrier and city size for 1970 to 1975.

<table>
<thead>
<tr>
<th>TABLE 2</th>
</tr>
</thead>
</table>

Service to Communities under 100,000 Population, Points Served and Weekly Flights by Type of Carrier

<table>
<thead>
<tr>
<th>Size of Community</th>
<th>1970—</th>
<th>1975—</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>Trunk</td>
<td>Local</td>
</tr>
<tr>
<td>1970 Population</td>
<td></td>
<td></td>
</tr>
<tr>
<td>0—25,000</td>
<td>17</td>
<td>126</td>
</tr>
<tr>
<td>25,000—50,000</td>
<td>18</td>
<td>80</td>
</tr>
<tr>
<td>50,000—75,000</td>
<td>3</td>
<td>12</td>
</tr>
<tr>
<td>75,000—100,000</td>
<td>6</td>
<td>16</td>
</tr>
<tr>
<td>Total</td>
<td>44</td>
<td>234</td>
</tr>
</tbody>
</table>

Percent Change: 1970 to 1975

<table>
<thead>
<tr>
<th>Size of Community</th>
<th>1970—</th>
<th>1975—</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>Trunk</td>
<td>Local</td>
</tr>
<tr>
<td>0—25,000</td>
<td>-29.4</td>
<td>-11.9</td>
</tr>
<tr>
<td>25,000—50,000</td>
<td>-11.1</td>
<td>-17.5</td>
</tr>
<tr>
<td>50,000—75,000</td>
<td>-33.3</td>
<td>-8.3</td>
</tr>
<tr>
<td>75,000—100,000</td>
<td>-16.7</td>
<td>-6.3</td>
</tr>
<tr>
<td>Total</td>
<td>-20.4</td>
<td>-13.2</td>
</tr>
</tbody>
</table>

\textsuperscript{17} Id. at 7-8.
Weekly Flights

<table>
<thead>
<tr>
<th></th>
<th>1970-</th>
<th></th>
<th>1975-</th>
<th></th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>Trunk</td>
<td>Local</td>
<td>Commuter</td>
<td>Trunk</td>
</tr>
<tr>
<td>0–25,000</td>
<td>583</td>
<td>3,911</td>
<td>4,025</td>
<td>256</td>
</tr>
<tr>
<td>25,000–50,000</td>
<td>556</td>
<td>3,464</td>
<td>2,282</td>
<td>603</td>
</tr>
<tr>
<td>50,000–75,000</td>
<td>161</td>
<td>409</td>
<td>560</td>
<td>132</td>
</tr>
<tr>
<td>75,000–100,000</td>
<td>458</td>
<td>865</td>
<td>613</td>
<td>373</td>
</tr>
<tr>
<td>Total</td>
<td>1,758</td>
<td>8,849</td>
<td>7,480</td>
<td>1,364</td>
</tr>
</tbody>
</table>

Percent Change: 1970 to 1975

<table>
<thead>
<tr>
<th></th>
<th>Trunk</th>
<th>Local</th>
<th>Commuter</th>
</tr>
</thead>
<tbody>
<tr>
<td>0–25,000</td>
<td>-56.0</td>
<td>-22.2</td>
<td>36.3</td>
</tr>
<tr>
<td>25,000–50,000</td>
<td>-8.4</td>
<td>-30.7</td>
<td>20.0</td>
</tr>
<tr>
<td>50,000–75,000</td>
<td>-18.0</td>
<td>-22.7</td>
<td>42.9</td>
</tr>
<tr>
<td>75,000–100,000</td>
<td>-18.6</td>
<td>-16.5</td>
<td>36.4</td>
</tr>
<tr>
<td>Total</td>
<td>-22.4</td>
<td>-25.0</td>
<td>31.8</td>
</tr>
</tbody>
</table>

Source: U.S. Dept. of Transportation, Service to Small Communities 28 (1976).

In communities of less than 100,000 population, the trunks have reduced scheduled flights by 22.4% in the period 1970 to 1975, the local service carriers reduced flights by 25.0%, while commuter carriers have added 31.8% to their flights. In 1974 commuter carriers provided more than half of their service in routes with less than ten passengers daily. Average stage length is much smaller than for scheduled carriers. (See Tables 3 & 4).

TABLE 3

Distribution of Passenger Markets by Mileage

<table>
<thead>
<tr>
<th>Mileage</th>
<th>Number of Markets</th>
<th>Percent</th>
<th>Number of Markets</th>
<th>Percent</th>
</tr>
</thead>
<tbody>
<tr>
<td>Less than 100</td>
<td>514</td>
<td>40.9</td>
<td>63</td>
<td>2.4</td>
</tr>
<tr>
<td>100-200</td>
<td>460</td>
<td>36.6</td>
<td>306</td>
<td>11.7</td>
</tr>
<tr>
<td>200-300</td>
<td>190</td>
<td>15.1</td>
<td>374</td>
<td>14.2</td>
</tr>
<tr>
<td>300-400</td>
<td>58</td>
<td>4.6</td>
<td>287</td>
<td>10.9</td>
</tr>
<tr>
<td>Over 400</td>
<td>35</td>
<td>2.8</td>
<td>1,595</td>
<td>60.8</td>
</tr>
<tr>
<td>Total</td>
<td>1,257</td>
<td>100.0</td>
<td>2,625</td>
<td>100.0</td>
</tr>
</tbody>
</table>

* The data refers to markets with single plane service. Markets where connecting service only is offered were excluded in order to make the data more comparable with commuter operations. Source: U.S. Dept. of Transportation, Service to Small Communities 34 (1976).
TABLE 4
Distribution of Passenger Markets by Passengers per Day

<table>
<thead>
<tr>
<th>Passengers per Day</th>
<th>Number of Markets</th>
<th>Percent</th>
<th>Number of Markets</th>
<th>Percent</th>
</tr>
</thead>
<tbody>
<tr>
<td>Less than 10</td>
<td>969</td>
<td>77.0</td>
<td>286</td>
<td>10.8</td>
</tr>
<tr>
<td>10-20</td>
<td>103</td>
<td>8.2</td>
<td>578</td>
<td>21.9</td>
</tr>
<tr>
<td>20-30</td>
<td>50</td>
<td>4.0</td>
<td>351</td>
<td>13.3</td>
</tr>
<tr>
<td>30-40</td>
<td>31</td>
<td>2.5</td>
<td>219</td>
<td>8.3</td>
</tr>
<tr>
<td>Over 40</td>
<td>104</td>
<td>8.3</td>
<td>1,204</td>
<td>45.6</td>
</tr>
<tr>
<td>Total</td>
<td>1,257</td>
<td>100.0</td>
<td>2,638</td>
<td>100.0</td>
</tr>
</tbody>
</table>

* The data refers to markets with single plane service. Markets where connecting service only is offered were excluded in order to make the data more comparable with commuter operations. Source: U.S. Dep't of Transportation, Service to Small Communities 33 (1976).

In the shortest-haul, low-density markets in which commuter carriers have been successful, the cost and scheduling advantages associated with smaller aircraft are very considerable. Miller and Laney’s study of fares suggest that commuter fares are below local service carriers’ fares in the very-short-haul markets. Local service carrier fares are based on a formula in which fares are set by a fixed charge plus a mileage charge; in addition, local service carriers may establish fares up to 130% of the CAB’s coach formula if no trunk carriers participate in the market. As a result, the local service carriers’ fares are high for very short stage lengths, whereas commuter carriers’ fares are higher at longer stage lengths. The other important characteristic of commuter fares is the absence of significant differences in fares between monopoly and non-monopoly routes which commuter airlines serve. The threat of potential entry restrains any tendency for commuters with a monopoly to raise prices. In summary, commuter carriers enjoy cost economies in using small aircraft in short stage lengths, which are reflected in the commuter air fare structure.

These statistics clearly reveal the contribution being made by air commuters to small communities and the reductions in service from local service carriers at small communities. The local service carriers have exited from the small community as rapidly as CAB regulations will permit. Many

19. Id.
smaller communities have seen their scheduled service switch from local service carriers to commuter carriers in recent years. In brief, pressures to keep the direct subsidy to a minimum have limited the degree to which the Congress has been willing to subsidize service by local service carriers at low-density points. Consumer satisfaction with commuter air service, largely the result of its rapid growth and the financial success of commuter carriers, is one reason why it has been possible politically to reduce the subsidy of local service carrier operations at low-density points.

The fortunes of air service at small communities lies with the commuter carriers, regardless of pricing changes which will result from the rule. The local service carriers have no comparative advantage at this stage to re-enter the small community market. Commuter service will expand at routes from which local service carriers exit.\textsuperscript{20} The routes from which local service carriers exit have longer stage lengths and higher densities than are typical for commuter carriers, making these routes especially attractive.

IV. SCHEDULING DECISIONS AND CROSS-SUBSIDY: SOME THEORETICAL OBSERVATIONS

Fare flexibility will result in changes in service in certain markets. Some concern has been voiced that massive reductions in service will result. It will be shown below that in order to predict the nature of changes in schedule frequency it is necessary to analyze the rationale for carriers' scheduling decisions. The extent to which fare reductions will require changes in schedule frequency depends on cost functions and the elasticity of demand. Service adjustments should be viewed as the natural consequence of achieving a more efficient outcome in which service is more closely aligned with consumer preferences.

The second argument analyzed below is the extent to which carriers "cross-subsidize" low-density markets with profits from high-density routes. The importance of this issue derives from a concern that reductions in fares and profits in high-density routes will undermine service throughout an airline's route network. It will be argued that this viewpoint is incorrect.

In considering first the adjustments of schedules, the interrelationships between fares and schedule frequency must be analyzed. Lower fares require higher load factors to cover costs and hence a tradeoff exists between the level of fares and the level of capacity.\textsuperscript{21} Greater capacity, or lower load factors, implies higher schedule frequency and convenience and a

\textsuperscript{20} Department of Transportation, Service to Small Communities 26 (1976).
higher probability that a seat is available at the desired departure hour. However, more capacity may require higher fares. The possible choices of fare and schedule frequency will depend on both fare and schedule elasticities of travelers and carriers’ cost functions. Travelers will differ in their preferences regarding the optimal fare-schedule frequency combination, with business travelers preferring lower load factors while tourist travelers likely will prefer lower fares at the expense of lower schedule frequency.\textsuperscript{22} Even within a city-pair market, passenger preferences will vary substantially. The optimal choice of fare and load factor in any city-pair will therefore depend on the mix of travelers by trip purpose, and also on the stage length and route density. The latter will be relevant in passengers’ valuations of the benefits of more- versus less-frequent service.

The choice between lower fares and more frequent service has been made by the CAB in its prevailing fare regulation, which has attempted to establish fares consistent with a 55% load factor. Price flexibility under the new rule allows carriers to test market responses to lower fare service. Carriers’ willingness to experiment with alternative price-service options may in turn result in adjustments in schedule frequency.

The effects of fare flexibility on capacity will depend both on the elasticity of demand and airline cost functions. Fare reductions which stimulate demand will entail additional costs to carry the additional traffic even if aircraft seat miles are held constant. Douglas and Miller estimate that the marginal costs of carrying additional passengers are well below the costs of providing capacity for most aircraft and under most load factors.\textsuperscript{23} The demand elasticity must be well above unity (about -1.3) if the increased traffic associated with a fare reduction is to provide sufficient revenues to cover the added costs of carrying the additional passengers. If the elasticity is less than -1.3, the carrier must reduce frequency, i.e. increase the load factor, when fares are reduced.\textsuperscript{24}

To conclude this argument, it should be stressed that service or frequency changes, including reductions in frequency, which will occur as a result of the rule should be viewed as the natural consequence of realigning service with consumer preferences. Such adjustments in frequency are a necessary part of a process of obtaining an economically efficient outcome, which is the appropriate objective of the change in the fare regulations.

The argument that the airlines now cross-subsidize low-density routes with profits from higher-density routes is inconsistent with the economic theory of the firm. That fares diverge from marginal costs in particular markets

\textsuperscript{22} Douglas and Miller developed a theoretical model relating the value of schedule delay to passengers’ valuation of time. Business travelers likely place higher values on time. G. DOUGLAS & J. MILLER, supra note 3, at 82-94.

\textsuperscript{23} Id. at 8-26.

\textsuperscript{24} Id. at 57-60.
is not in itself evidence that cross-subsidy occurs. A brief theoretical discussion of the concept of cross-subsidy will usefully focus the issues which arise in assessing the impacts of the rule.

Cross-subsidy exists when outputs and prices are such that prices differ from marginal costs among markets, assuming all cost functions are characterized by constant costs and all costs are assignable. Markets in which prices are below marginal cost are being subsidized. It is difficult to envision circumstances when firms would willingly choose to cross-subsidize one market by revenues from another if cost and demand functions in each market were independent. Sellers would have no incentive to use profits from one market to subsidize output in another market in these circumstances. Regulation of markets is the one circumstance in which cross-subsidy is often created; as a condition of participation, firms may be required to establish output and price levels across markets which cross-subsidize certain markets. Certain types of postal service illustrate a market subsidized in this fashion.

There are a variety of circumstances in which prices diverge from marginal cost but no cross-subsidy occurs. For example, if sellers had some degree of market power and entry were precluded by entry barriers or entry controls, firms would have incentive to set prices and outputs such that prices diverged from marginal cost by varying amounts, the amounts dependent on the elasticity of market demand curves. No price would lie below marginal cost, but prices could diverge from marginal costs in particular markets even if the firm’s cost function was characterized by constant costs and all costs were assignable. No cross-subsidy would exist.

Other circumstances in which prices diverge from marginal costs in particular markets involve considerations of decreasing costs, non-assignable common costs, and the interdependencies between markets. For example, the firm may perform activities where there are significant common or non-assignable costs. Several types of users may share a facility, but all of the facility costs cannot be traced to the use of individual users. Or, a firm may produce many products with a given production process, with some common or overhead costs non-assignable to particular products. The airlines are by no means unique in confronting the problem of recouping overhead or common costs.

“Cross-subsidy” is a misnomer to describe the situation in which different markets make different contributions to overhead costs. In these circumstances there is no basis on economic efficiency grounds in support of any particular assignment of common costs to different products. (Efficiency requires marginal cost pricing, with lump-sum taxes used to finance non-assignable costs.) In practice a variety of procedures are employed by firms to “assign” common costs to particular markets. The most common procedure is a constant markup of costs of particular products. Much of
the retailing sector uses markups of this sort to recoup overhead or common costs. Another procedure often used by firms in recouping common costs is to price discriminate, assigning differential amounts of common costs to products based on differences in demand elasticities.\textsuperscript{25}

In the case of the airlines the principal issue in interpreting fares in different markets stems from the existence of common costs associated with operating networks comprised of more than one city-pair route. A route system will include both common costs and costs traceable to operations in each link. These common costs arise from indivisibilities in the production process. Station expenses are not proportional to output at low levels of output since a minimum level of station facilities must be provided even at low passenger demand levels. Some portion of station expenses cannot be directly assigned to output levels in any given city-pair link.\textsuperscript{26} (Overhead costs also are unassignable to particular routes.)

The size of aircraft used on a network also creates an indivisibility which affects the definition of cost functions in particular city-pair sub-markets. Aircraft represent an input available in discrete sizes, and which cannot be varied continuously by city-pair market. Costs do not vary proportionally with output at small levels of output due to aircraft sizes available and the economies associated with larger aircraft. The fact that it is most efficient in most circumstances to schedule a given aircraft over a linear route system comprising several city-pair markets creates an indivisibility. The least-cost choice of aircraft will depend on the network over which it is to be flown, including the stage length and traffic density in each route. The most efficient means of serving a network may entail scheduling an aircraft over a network so that revenues are below assignable marginal cost in a subportion of the network.\textsuperscript{27}

In pricing service over a network comprising many route segments, and in which some portion of costs are non-assignable to particular segments, an allocation of common costs is necessary. In particular sub-markets, prices may bear different relationships to assignable costs. In this circumstance it is inappropriate to label these differences between prices and costs cross-subsidy. Even in the situation when prices fall below assignable marginal cost in one submarket it may be inappropriate to suggest that this one submarket is being subsidized by others. For example, it may

\textsuperscript{25} The opportunity to price discriminate requires that separate markets be identified, resale be prohibited, and differing elasticities of demand exist. The elasticity of demand for products will depend on the degree of competition in the market and the availability of substitutes. The existence of competitors or the threat of entry limits the degree to which firms may charge prices well in excess of costs in any given market.

\textsuperscript{26} The author found significant cost economies associated with greater route density in the international airline industry. M. Straszheim, supra note 3, ch. 4.

\textsuperscript{27} Positioning flights illustrate this phenomena. M. Straszheim, supra note 3, at 72-82.
be that service in each individual city-pair market in a subnetwork is unprofitable if operated individually, i.e. revenues would fall below costs in each individual market. Yet when operated as a network of city-pairs, common costs can be assigned to various submarkets so that the entire network is profitable. If omitting service in one submarket results in separate subnetworks each of which is unprofitable, or in which costs are now higher (e.g., due to lesser utilization of equipment and personnel), the connecting market should be included even though prices fall below assignable cost. It would be inappropriate to label this a cross-subsidy of the connecting market since the existence of the latter provides cost savings and service benefits to other markets.

It must be stressed that it is only the existence of indivisibilities arising from station expenses or aircraft size, or cost or demand interdependencies among city-pair submarkets in a network, that creates a situation where price-marginal cost relationships could vary among submarkets even in a purely competitive market environment. Were productive inputs completely divisible in all markets, firms would have incentive to offer that output where price (equal to marginal revenue in the competitive case) equaled marginal cost in each market.

To summarize, there is no theoretical argument in support of the thesis that carriers cross-subsidize certain markets. That city-pair markets make different contributions to overhead or common costs is not evidence by itself that cross-subsidy exists. In addition, scheduling competition is such that load factors approach break-even levels in most markets.\(^\text{28}\)

While cross-subsidy is not relevant in predicting the effects of fare changes under the rule, the potential role of network effects on carriers’ decisions in individual markets must be recognized. Airlines are providing service over networks of cities, with the financial returns on components of these networks interrelated. Much air carrier service is conducted on route systems, in which aircraft are routed along a series of city-pair markets. That such subnetworks are a cost-efficient means of providing service over a larger route system creates interdependencies between outcomes in particular submarkets. In a connecting service A to B to C, there may be insufficient traffic from A to B, A to C, or B to C to cover costs if each were served individually. Yet service A to B to C is profitable. The nature of service which can be provided between any two cities may depend in part on service and traffic levels in other markets.

As a result of these network effects, changes in pricing under the rule and changes in revenues in one submarket would in principle alter an airline’s incentive to offer service in an entire subnetwork of routes. However,

\(^{28}\) Douglas and Miller argue that very little excess profit exists in any market due to scheduling competition. G. DOUGLAS & J. MILLER, supra note 3, at 97.
these direct effects would only be felt in routes in which there were production interdependencies arising from the use of common station facilities, common aircraft, and personnel inputs, or demand interdependencies. Service in the rest of the airline’s operations should be unaffected; changes in profits in links unrelated in a production or cost sense to other links should not directly alter carrier’s decisions in these latter markets. Changes in revenue associated with fare changes in any given market under the rule would not affect decisions regarding entire carriers’ route system. It will be argued in the next section that these network interdependencies are likely small.

V. FARE AND SERVICE CHANGES

The opportunity afforded carriers to change prices in markets under the rule will result in fare and service changes in a number of markets. The nature of these adjustments is discussed below. The fare reductions are likely to be concentrated in the denser markets, but these are not likely to lead to major cutbacks in service in low-density markets.

The discussion of these service adjustments is based on limited empirical evidence, since there inevitably remains considerable uncertainty about passenger preferences and their reactions to various fare-service options before the fact. The CAB properly notes the difficulty of anticipating what is an optimal fare and service configuration. Carriers are best suited to making these predictions. In some instances experimentation will be needed to determine the outcomes consistent with consumer preferences.

The best assurance of continued service in markets derives from the fact that the industry is a constant-cost industry. Changes in fares which increase break-even load factors will result in lower schedule frequency. The important questions revolve around the types of service changes likely in particular markets and the role of “network effects” in firms’ decisions to offer service in particular submarkets.

Predicting the most likely service changes under the rule involves an examination of the structure of fares under the previous DLPFI regulations. In the past, prices were established to yield a normal rate of return for carriers experiencing costs equal to the average costs of industry participants at a load factor of 55%. The fare structure was designed to reflect differences in costs associated with varying stage lengths but not varying traffic density. Carrier incentives under regulated prices were to expand service and frequency until actual load factors approximated break-even levels. In actual practice, market load factors have been inversely related to stage length and density,

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29. id. at 91-92.
Carriers’ response to the opportunity to introduce fare reductions will reflect their sense of passenger preferences with respect to lower fares versus lower quality service. Carriers may choose to reduce on-board amenities or terminal facilities. The principal service dimension at choice is schedule frequency. In most instances, demand elasticities are not sufficiently high that lower fares will increase revenue per seat-mile of service. The markets in which passenger preferences most likely favor lower fare service are those with major tourist markets and/or high traffic density. Theoretical markets of passenger demand and schedule convenience suggest that traffic density and schedule convenience implied by any given level of flights are positively-related variables.\(^\text{30}\) In denser markets with more frequent departures, less waiting time is incurred before another flight in the event that any given flight is fully booked. For any given probability distribution of planned departure times, average schedule delay time will be less if more flights are available. Schedule frequency being higher in denser markets, the inconvenience of higher load factors is less; this is the circumstance in which a lower-fare service is likely the most attractive to passengers. High-density markets are therefore the markets which will most likely be the target for fare reductions.

The mix of tourist and business travel will also influence carrier decisions, with tourist-dominated markets the likely target of low-fare experimentation. Since demand elasticities are less in markets with more business travel, less fare cutting is to be expected here. Finally, fare reductions are more likely in markets with more carriers, where tacit collusion on prices is perhaps less easily achieved. There also may be instances in which carriers reduce prices in an attempt to increase market share, either in a market which they now serve or one in which they have chosen to begin service again. This motive is not synonymous with a motive of predatory pricing. Since some entry controls remain, and many markets have only one or two carriers, it is quite possible that price cutting may not be prevalent in these markets, but would rather be substantially concentrated in the larger, more competitive markets.

It is possible that more than one type of service may be offered in certain markets, especially for short periods of time. Some carriers may provide only peak-hour service, at low fares and high load factors in a few high-density markets. In these latter markets some carriers may continue to offer conventional service at higher fares. The carrier with higher fares may have the advantage of feeder traffic. Whether fare differentials can exist within a given market over the long run is not obvious on \textit{a priori} grounds. Intrastate service at lower fares has operated in competition with higher-fare

air service in some markets.  

If only small adjustments in capacity are required as a result of any fare flexibility downward that increases break-even load factors, these adjustments might be made gradually through time. Capacity adjustments could be made by increasing capacity less rapidly than the normal growth in demand that would occur in the absence of price changes. Individual carriers can also adjust capacity downward more quickly, by selling or leasing equipment or deferring new equipment deliveries. Past experience has shown the airlines to be quite reluctant to reduce their capacity commitments, though they will make such adjustments if financial circumstances require it.

It is possible that fare reductions and higher load factors in denser, more competitive markets will encourage carriers to shift capacity to less-dense markets or those with fewer carriers, where they feel additional schedule frequency may be a more effective competitive strategy than price cutting. A carrier might judge that such additions to frequency in these latter markets would preempt entry or service frequency expansion by other carriers. Of course, if one carrier in such a market judges itself to be disadvantaged competitively in scheduling competition, it has the opportunity to reduce fares under the rule. Thus, while some tendency may exist to transfer capacity away from markets in which fare reductions are occurring, there are clear incentives for fare cutting to spread to other markets as well, especially if one or more carriers considers there to be excess frequency in these other markets.

The discussion in Section IV noted that city-pair markets are in some instances interrelated by network considerations. In principle, some service changes traceable to airline network configurations may occur. As noted earlier, fare reductions and lower revenues could in principle affect the decision to offer service in feeder markets. Lower profits might result in exit from a network of several city-pair markets in the absence of opportunity to increase fares in these markets. The reverse might also occur; lower fares might increase demand and induce carriers to increase frequency throughout a subnetwork.

These types of network effects leading to service reductions are not likely to be large. In practice, airline networks are comprised of many “independent” subnetworks, in which demand and cost functions are unrelated from one subnetwork to another. Outcomes in any one city-pair should only affect outcomes in related city-pairs. Also, it is not evident that

32. Straszheim, Airline Demand Functions in the North Atlantic and Their Pricing Implications, J. TRANSP. ECON. AND PUB. POL’Y (forthcoming).
common costs are allocated among airline city-pair submarkets in a highly unequal manner (i.e., that realized load factors are such that there exist significant variations in the contributions of different markets to overhead costs). As noted earlier, competition among trunks, local service, and, recently, commuter carriers is such that airlines' ability to recoup additional profits from particular submarkets is limited.

It is not evident on a priori grounds whether more or less limited types of networks will prove the more cost-efficient means of providing air service in the future. It is possible that much more "limited" route networks will prove most efficient. Carriers may find it cheapest to schedule high-density turnaround service rather than the use of multiple-stage linear route systems. The latter create potential scheduling problems; delays in some portion of the network may affect on-time performance. But the reverse is also possible. More competition in denser markets may shift the advantages in favor of multi-stage systems, with feeder links providing additional traffic to denser links of a system. Carriers may seek to expand their route systems under the new pricing rules rather than contract them.

The small-community markets in which the local service carriers provide monopoly scheduled service (or in competition with commuter carriers) will not likely be significantly affected by increased fare competition in competitive markets. The profitability of much of the small-community market is unrelated to outcomes in denser, more competitive markets. To summarize this discussion, lower-density markets are less likely to experience significant fare reduction or to be affected by fare competition in denser markets.

VI. CONCLUDING OBSERVATIONS

The new rule allowing fare flexibility is an important step in creating more price competition and in encouraging an economically efficient outcome in which price and service in the airline industry are more closely aligned with consumer preferences. The introduction of fare competition will necessarily entail some changes in schedule frequency. These adjustments are the natural result of adjusting service to consumer preferences.

There is no evidence that service changes under the rule will result in significant service abandonment to small communities or that small communities will receive any less service than if prevailing CAB entry, fare, and subsidy policies were continued. Under previous policy, local service carriers have exited from small-community service at a rapid rate, with these markets being subsequently served by commuter airlines. Based on the high rate of growth of commuter service, travelers apparently place very considerable value on commuter air operations. The future of air service to small communities lies largely with the commuter carriers.

The effects of the rule will likely be most evident in the denser markets.
Load factors are inversely related to density. Consumers will likely be most responsive to lower fares even at the expense of less-frequent service in the denser markets, where schedule frequencies are such that the scheduling inconvenience of increasing load factors is least. Tourist markets are also candidates for fare reductions. Denser markets with more than one carrier are the market structures in which price competition is most likely. Major fare reductions in smaller markets and significant reductions in service are unlikely.
The Impact of Section 13(c) of the UMTA on Labor-Management Relations at BART*

JOHN G. KILGOUR**

The San Francisco Bay Area Rapid Transit District (BART) was the first new mass transit system in the United States in sixty years that was more than a reorganization or expansion of existing systems.\(^1\) Consequently, almost everything that was done broke new ground and set example and precedent for the industry of the future. There was more than the need to develop new concepts and technology. BART, for the first time in the industry, encountered the problems and opportunities of large-scale federal assistance to urban transit and the frustrations of dealing with numerous political jurisdictions, high rates of inflation, and concerns of equal employment opportunity, environmental protection, and the elderly and the handicapped. The application to transit of a job-protection concept drawn from the railroad industry was also new. It is this last problem and the developments that surround it that are the main topics of this article. As will be seen, the expansion of this concept and its application to an entirely new

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* The author is indebted to Mr. Paul L. Cooper, BART Employee Relations Manager; Mr. Gordon B. Olsen, Former BART Director of Personnel; Mr. Charles A. Simon, BART Manager of Labor Relations; and Mr. Lary F. Yud, Chief, Division of Employee Protections, U. S. Dep't of Labor, for the information, material and cooperation provided.

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1. SAN FRANCISCO BAY AREA RAPID TRANSIT DISTRICT OFFICE OF PUBLIC INFORMATION, A HISTORY OF BART 7 (November 1976). BART is actually an interurban transit system. However, the distinction is unimportant for the present discussion.
system are disturbing demonstrations of the influence of organized labor in the public sector.

The idea of linking the East-Bay communities with San Francisco was first formally discussed in 1947 as an approach to the problem of traffic congestion caused by heavy post-war migration to the Bay Area. In 1957, the California legislature formed the San Francisco Bay Area Transit District. Construction officially began on June 19, 1964, and revenue service commenced on September 11, 1972. By 1977, the District was operating 450 cars over 71 miles of track with 34 stations and had an average daily ridership of 133,000.² Besides these aspects of the development of BART there were many political, administrative and legal controversies, including those related to labor-management relations.

BART's development took place against a backdrop of important changes in the transit industry. Total passenger rides for the industry declined from 23 billion in 1945 to 7 billion in 1976,³ while transit employment declined from 242,000 to 162,000.⁴ During the same period, transit revenue increased from $1.3 billion to $2 billion,⁵ while total operating expenses went from $1.2 billion to $4 billion.⁶ The difference between revenue and expenses was largely offset by various local, state and federal subsidies.

Throughout this period, many privately-owned transit systems found themselves in economic difficulty and facing the probability of going out of business. Since urban transit services have long been thought of as essential, the fact that they were going out of business was politically unacceptable. The result was that one company after another passed from private to public ownership. By 1976, 375 systems, 39% of the total, had become publicly owned, but these systems generated 88% of the operating revenue and carried 91% of the passengers.⁷ Thus, almost without notice, and entirely without socialist or conservative rhetoric, an important American industry became government owned.

Although the shift from private to public control usually prevented the termination of service, it seldom provided the financial support needed to cope with the industry's fundamental problems, which were attributable mainly to the inherently superior personal transportation provided by the automobile. As the move to the car continued throughout the post-war pe-

² Id. at 4.
⁴ Id. at 34. Public transit systems are defined as systems "owned by municipalities, counties, regional authorities, states or other governmental agencies including transit systems operated or managed by private firms under contract to governmental agency owners."
⁵ Id. at 22.
⁶ Id. at 23.
⁷ Id. at 19.
riod, service levels were reduced, equipment was allowed to deteriorate and technical innovation was ignored. The industry was in trouble.

The decline of the industry naturally made the labor unions very conscious of job security. The transit industry had long been about 95% unionized. The main labor organizations involved in the industry are the Amalgamated Transit Union (AFL-CIO) and the Transport Workers' Union of America (AFL-CIO). In 1975, the ATU had 140,000 members and the TWU 150,000. The ATU, or the Amalgamated as it is often called, is most closely identified with the industry in most cities.

**FEDERAL ASSISTANCE**

Given the plight and social importance of urban mass transit, it was inevitable that the federal government would become involved. However, that involvement was not simple or unopposed. Because of the inherently local character of urban transit, it has historically been outside of the national transportation policy of the United States and beyond the scope of federal regulation or support. Yet conceptually, it has been viewed as an extension of railroad passenger service.

As various railroads abandoned commuter service in the course of that industry's post-war decline, cities began to press Washington for aid to urban mass transit. This was considered a big-city problem and was opposed by Southern Democrats and Northern rural and suburban Republicans, and until the late 1960's progress was slow. By then, however, it was realized that problems of pollution, traffic congestion and mobility were spreading to the suburbs, and positions changed.

The first federal support of urban transit was authorized by the Housing Act of 1961, which made money available for transit demonstration projects. Other transit-support bills were introduced and reported in both houses of Congress in 1962 but not enacted. Legislation was reintroduced in 1963 and 1964 which eventually became the Urban Mass Transportation Act of 1964. Under this law, federal funds are granted through the Urban Mass Transportation Administration to local transit districts and agencies for construction and operating purposes.

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Privately-owned transit systems with an annual gross revenue of $25,000 or more had long been under the jurisdiction of the National Labor Relations Board for collective bargaining purposes. As mentioned, the industry was almost completely unionized and collective bargaining, including the right to strike, was widely accepted. In 1962, a large transit system in Dade County (Miami), Florida, shifted from private to public ownership. As a result, the workers involved became public-sector employees and therefore exempt from the federal collective bargaining law. In spite of the efforts of the Amalgamated Transit Union they lost all collective bargaining rights.14 Given the large number of transit systems that were then in financial difficulty and were thus in the process of shifting from the private to public sector, this was an ominous development for the unions.

Labor responded by lobbying successfully to add a provision to the proposed transit legislation designed to protect existing employee rights.15 After revision and amendment, this became section 13(c) of the Urban Mass Transportation Act of 1964 and is now section 1609(c) of the Urban Mass Transportation Assistance Act of 1970 as amended in 1974.16 The wording has remained unchanged, and the agreements entered into under its provisions are referred to as "section 13(c) agreements."

Section 13(c) requires an employer seeking financial assistance under the Act to enter into an agreement acceptable to the Secretary of Labor to protect the interests of employees affected by such assistance. The agreement is to include:

1. the preservation of rights, privileges and benefits . . . under existing collective bargaining agreements or otherwise;
2. the continuation of collective bargaining rights;
3. the protection of individual employees against a worsening of their positions with respect to their employment;
4. assurances of employment to employees of acquired mass transportation systems and priority of reemployment of employees terminated or laid off; and
5. paid training and retraining programs.17

The section further provides18 that such protection of rights and benefits shall in no event be less than that established pursuant to section 11347 of the Interstate Commerce Act.19 The latter reference locks 13(c) agreements into the railroad industry's Washington Job Protection Agreement of

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15. Barnum, supra note 8 at 170.
17. Id.
18. Id.
19. 49 U.S.C.A. § 11347 (Supp. 1979). This section requires the ICC, as a condition of approving a coordination, to provide fair and equitable arrangements to protect the interests of
May 21, 1936, as expanded upon by various Interstate Commerce Commission decisions.\textsuperscript{20}

**BART’s 13(c) Agreement**

Although the original impetus for section 13(c) was the protection of employee rights (especially collective bargaining rights) when existing transit systems became public utilities, the language of the section makes it a condition of “any assistance” that the recipient enter into a 13(c) agreement.\textsuperscript{21} Thus when BART, a brand new transit system, sought federal funds, it was required to negotiate such an agreement.

As early as October 1966, the U.S. Department of Labor assumed that BART would negotiate a 13(c) agreement.\textsuperscript{22} In a capital grant received from the Urban Mass Transportation Administration in the spring of 1967, BART agreed that if any employees were adversely affected by the grant, “appropriate protective arrangements for such employees would be made as required by Section 13(c) . . . .”\textsuperscript{23}

During 1967 a series of meetings was held in Washington between representatives of BART, various labor organizations, and the Department of Labor.\textsuperscript{24} Drafts were exchanged, and by leaving unresolved the critical issue of the degree to which BART would give “priority employment” to employees of existing transit systems, an agreement was reached. It was signed by 23 labor organizations, was ratified by BART’s Board of Directors, and took effect on January 25, 1968.\textsuperscript{25}

BART’s 13(c) Agreement dealt with two important concepts. One was “adverse effect,” which relates to those employees whose employment positions were worsened because of the construction or operation of BART. This part of the Agreement\textsuperscript{26} closely followed the requirements of section

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affected railroad employees. Such employees may not be placed in a worse position with respect to their employment for a period equal to their length of service up to a maximum of four years.

\begin{itemize}
  \item 20. Stern, supra note 14, at 80-81.
  \item 22. Letter from James J. Reynolds, Assistant Secretary of Labor, to Leo P. Cusick, Director, Urban Transportation Administration, Dep’t of Housing and Urban Development (October 19, 1966), directed to R. B. Stokes, General Manager of BART by David J. Speck, Counsel, Urban Transportation Administration (in possession of the author).
  \item 23. Urban Mass Transportation Capital Grant Contract between the San Francisco Bay Area Rapid Transit District, California, and the United States of America (Dep’t of Housing and Urban Development, Urban Transportation Administration) Project No. CAL-UGT-6, Contract No. H-794 (1967).
  \item 24. The main labor organizations involved were the ATU, TWU, and the railroad unions.
  \item 25. Agreement Pursuant to Section 13(c) of the Urban Mass Transportation Act, as Amended [hereinafter cited as 13(c) Agreement]. BART signed a new 13(c) agreement for capital grants in 1976 and also signed the National Model 13(c) Agreement for operating grants. These matters lie beyond the scope of this paper. All references hereafter refer to BART’s 1968 13(c) agreement.
  \item 26. 13(c) Agreement supra note 21, at 3.
\end{itemize}
13(c) of the Urban Mass Transportation Act\textsuperscript{27} and section 5(2)(f) of the Interstate Commerce Act\textsuperscript{28} as expanded by the so-called "New Orleans conditions."\textsuperscript{29} BART now has an estimated adverse-effect liability of about $5.4 million,\textsuperscript{30} but this part of the Agreement was not then controversial; BART claimed that it would have no adverse effect on employees of existing systems, and the unions were concerned with more immediate matters. Although not developed in the present discussion, this potential liability should be kept in mind when evaluating the overall impact of section 13(c).

The second and more controversial concept contained in BART's 13(c) Agreement was that of "priority employment" for employees of existing transit systems, a concept independent of proven adverse effect.

In section 1 of the 13(c) Agreement, the parties recognized that "some form of priority employment is appropriate for employees of existing mass transportation systems in the area to be served by BART."\textsuperscript{31} The details were left for negotiation between BART and the unions of such employees. Section 2 stated that, pending the completion of negotiations, such employees would be given the "first opportunity to fill all non-supervisory, non-professional, non-construction jobs" under conditions to be agreed upon by the parties.\textsuperscript{32} If no such agreement was reached, the matter was to be submitted to binding arbitration as provided for later in the Agreement. Section 3 required that if no agreement was reached on the extent and scope of priority employment by March 1, 1968, these matters were also to be submitted to arbitration.\textsuperscript{33}

This was the first application of the concept of priority employment independent of adverse affect in a 13(c) agreement. It was to have an important impact on future labor-management relations at BART. From the unions' point of view, priority of employment was the only effective way of dealing with BART, since no adverse effect would occur until after the system went into operation and long after it was staffed; to limit their efforts on behalf of their members to compensation of those displaced by BART was viewed as inadequate. BART management was very unhappy with the in-

\begin{itemize}
\item \textsuperscript{27} 49 U.S.C. §§ 1601-13 (1976).
\item \textsuperscript{28} Recodified in 49 U.S.C.A. § 11347 (Supp. 1979).
\item \textsuperscript{29} 13(c) Agreement, supra note 25, § 5. New Orleans Union Passenger Terminal Case, 282 I.C.C. 271 (1952). This case extended the benefit period for employees dismissed as a result of a coordination from four years from the effective date of the ICC order to four years from the date of the adverse effect. It also reduced the coordination payments by income earned from all employment during the period, instead of just from railroad employment.
\item \textsuperscript{30} F. Siskind & E. Stromsooper, The Economic Cost Impact of the Labor Protection Provision of Section 13(c) of the Urban Mass Transportation Act of 1964, 155-56 (1978).
\item \textsuperscript{31} id. § 2.
\item \textsuperscript{32} id. § 3.
\end{itemize}
clusion of the priority employment concept in the Agreement. BART's representatives at the original 13(c) negotiations were apparently unaware that priority employment had not been included in other 13(c) agreements. It is claimed that had they known the implications of what they were doing, they never would have signed.34 This may be somewhat unrealistic; BART needed federal funding for its completion. The unions were in a position to delay, if not stop, that funding. In addition, there was a certain logic to the unions' contentions that would have found a sympathetic ear in the Department of Labor. Hindsight suggests that BART would have been better off negotiating for a specified degree of priority employment and the conditions under which those employees would begin employment at BART rather than leaving such an important question unanswered.

Section 14 of the Agreement established an arbitration procedure to resolve disputes between BART and the signatory unions in regard to application, interpretation, and enforcement. Sam Kagel, a highly respected labor arbitrator, was specifically named as the permanent arbitrator for the Agreement.35

The parties were unable to reach an agreement on priority employment by the March 1, 1968 deadline or thereafter. Although BART had agreed that some priority employment was in order, there was a standing disagreement among the parties as to the degree and conditions of such employment. On February 8, 1968, two weeks after signing the 13(c) Agreement, the BART Board of Directors issued a policy statement which noted the District's responsibility to hire from (minority) community groups and stated that any preferential hiring arrangements would not be exclusive. Further, it was stated that any agreement negotiated pursuant to section 13(c) would not be binding on the District until approved by the Board of Directors.36

On March 20, 1968, a negotiating session was held between BART and a number of labor organizations. The unions continued to demand 100 percent priority employment. BART continued to offer 10 percent beyond any arrangements made for employees of existing transit systems who actually suffered adverse effect. No agreement was reached. The parties did agree to a follow-up series of meetings to examine the impact of BART on existing transit systems on a run-by-run basis. Upon reflection, BART management and counsel concluded that the unions were attempting to

34. F. SISKIND & E. STROMSDORFER, supra note 23, at 163, 168.
35. In the event Kagel was unavailable or unwilling to serve, Benjamin Aaron was to arbitrate. In the event that neither was available, an arbitrator was to be chosen from a list furnished by the Federal Mediation and Conciliation Service.
expand the concept of adverse effect and cancelled these meetings. On April 4, 1968, BART unilaterally established a procedure to offer available jobs—on a right-of-first-refusal basis—to qualified employees of existing transit systems pending the outcome of the stalled priority-employment negotiations.

The priority-employment talks remained deadlocked for the next two years. The unions made an unsuccessful attempt to pressure BART into a higher degree of preference by making the public claim that they were "following their work." Although various proposals to reopen negotiations were made and discussed, the matter was eventually to be decided by arbitration. Meanwhile, BART notified the signatories to the 13(c) agreement of job openings as they occurred and hired employees as needed at terms established by management. Few employees came from existing transit systems; those that did joined BART as new employees and gave up any accrued rights with their former employer. By the time the matter went to arbitration, there was a large number of employees at BART who had been hired on a non-priority basis and a smaller number who had some claim to preference but had accepted BART's terms.

**THE BARGAINING-UNIT DECISION**

The 13(c) agreement was not the only important labor-relations matter pending at this time; a decision concerning the determination of the appropriate bargaining unit(s) for the new system was also at issue. Transit districts in California are created and governed by individual enabling statutes. Chapter 4 of BART's statute, titled "Labor Provisions," serves as a labor law for the District. California Public Utilities Code section 28851 provides that in a question of representation, the matter will be submitted to the State Conciliation Service, which "shall promptly hold a public hearing and may, by decision, establish the boundaries of any collective bargaining unit and provide for an election to determine the question of representation." When the Conciliation Service received the BART case, it named Sam Kagel, the same person named as the permanent arbitrator in the 13(c) agreement, as its hearing officer.

Mr. Kagel conducted thirteen days of hearings on the representation

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37. BART Inter-Office Communication from Director of Personnel to Assistant General Manager (June 14, 1968).
39. Open letter from E. A. Cordeiro, Business Agent and Vice President ATU Division 192, sent to various state and national legislators (April 22, 1968), in TRANSIT, May, 1968; BART Inter-Office Communication (June 14, 1968).
41. Id. § 28851.
issue during 1971, which generated over 1,500 pages of transcript. Most of the signatory unions to the 13(c) agreement plus other labor and community organizations were represented. The Listing of Appearances contains 79 entries.\textsuperscript{42}

BART contended for a large bargaining unit exclusive of security guards, while the various unions sought different arrangements designed to protect and promote their particular positions and jurisdictions. The details of this matter, which involved exclusion of supervisory and confidential employees, as well as the lateral dimension or scope of the unit, lie beyond the limits of this discussion.

Mr. Kagel made his recommendation to the Director of the Department of Industrial Relations (within which the Conciliation Service is housed) by letter dated February 26, 1973. It called for: (1) a supervisory unit, (2) a security unit, and (3) a comprehensive "umbrella" unit containing three subunits for (a) transportation, (b) clerical, and (c) maintenance employees. The subunits were to have separate status for election purposes but were to bargain jointly as a single unit with BART after the election. In the event that more than one union won representation rights within the comprehensive unit, they were to work out their own internal arrangements for collective bargaining. The determination was based on BART's "unique characteristics," the community of interest of the employees, and the essentiality of the service provided by the system.\textsuperscript{43}

The Department of Industrial Relations adopted Mr. Kagel's recommendations on March 6; a pre-election conference was held on March 14; and the election discussed later was conducted on April 18, 1973.

\textbf{INTERPRETATION OF BART'S 13(C) AGREEMENT}

Soon after the completion of the representation hearings, but before Mr. Kagel made his recommendations to the State Department of Industrial Relations, the parties conducted a closely-related set of hearings on the interpretation of BART's 13(c) agreement. These hearings began on November 15 and ended on December 21, 1971. The issues of the representation hearings and the 13(c) hearings tended to overlap: the 13(c) award would, to some extent, determine which employee-union members would staff and eventually vote in the bargaining units to be determined. On several occasions, the representation hearings got into 13(c)-related matters, and the 13(c) proceedings and exhibits were formally incorporated

\begin{footnotes}
\item[42] Representation Proceedings Before Impartial Hearing Officer Under Provisions of Section 28851 of the California Public Utilities Code, in the Matter of Representation Hearing to Present Representation Claims on San Francisco Bay Area Rapid Transit District (June 21-October 14, 1971) [hereinafter cited as Representation Proceedings].
\item[43] Letter and attachments from Sam Kagel to H. Edward White, Director, Department of Industrial Relations (February 26, 1973).
\end{footnotes}
into the representation case to the extent relevant.\textsuperscript{44} The 13(c) case distilled the basic question of whether the term "employees affected" referred to the potential effects of BART on a general body of employees, as the unions contended, or whether it referred to particular employees who had to be identified as having suffered a worsening of their employment condition, as BART contended. No stipulation was possible on this basic question.\textsuperscript{45} If the union position was adopted (as it later was), then the important issues became the degree and allocation of priority employment among the employees of existing transit systems and the appropriate wages, hours and conditions of these employees who came over.\textsuperscript{46} It should be noted that there were numerous related and incidental questions that are not central to this discussion.

Mr. Kagel's 13(c) priority employment award was issued as three partial decisions dated June 20, July 15, and July 24, 1972, and as an amendment to the basic June 20 decision dated December 20, 1972.\textsuperscript{47} It will be recalled that the bargaining-unit recommendation was dated February 26, 1973.\textsuperscript{48}

The highlight of the 13(c) award was that BART was directed to interview and offer employment for presently available jobs to interested employees of five existing transportation systems by specified order and on the basis of the employees' seniority with the existing company. The priority employees were to bring with them their former wage rate (when higher than BART's the wages would be red circled),\textsuperscript{49} certain benefit rights, and their old seniority dates. The award was not to affect the non-13(c) employees presently at BART, except that those who had already come over from existing transit systems were to retain their old seniority dates. Table 1 presents the companies in order of priority, the number of applications and hires from each, and the main labor organization on the property from which they came. It shows that the overwhelming majority came from systems in which the Amalgamated Transit Union was the main, although not the only, bargaining agent.

\textsuperscript{44} 13(c) Proceedings, supra note 24, at 309.
\textsuperscript{45} Id. at 169-73.
\textsuperscript{46} Id. at 21.
\textsuperscript{47} In the Matter of Controversy between the Signatory Unions to the Agreement Pursuant to Section 13(c) of the Urban Mass Transportation Act, As Amended, January 25, 1968, and San Francisco Bay Area Rapid Transit District (BART), Re: The Application and Interpretation of the 13(c) Agreement, Partial 13(c) Decision of Sam Kagel, Arbitrator, San Francisco, California (June 20, July 15, July 24, 1972); and Amendment to Partial 13(c) Decision of June 20, 1972 (December 22, 1972). [hereinafter referred to as Partial 13(c) Decisions].
\textsuperscript{48} Supra note 43.
\textsuperscript{49} When a wage rate of an employee or group of employees is "red circled" it remains unchanged until the rates of others employed in the job classification catches up with it.
Table 1. Origin and Number of BART's Priority Employees

<table>
<thead>
<tr>
<th>Company</th>
<th>Number of Applicants</th>
<th>Number of Hires</th>
<th>Labor Organization</th>
</tr>
</thead>
<tbody>
<tr>
<td>Peerless Stages</td>
<td>17</td>
<td>4</td>
<td>ATU, Division 1225</td>
</tr>
<tr>
<td>Greyhound Lines West</td>
<td>441</td>
<td>90</td>
<td>ATU, Division 1225</td>
</tr>
<tr>
<td>AC Transit</td>
<td>214</td>
<td>41</td>
<td>ATU, Division 192</td>
</tr>
<tr>
<td>San Francisco MUNI</td>
<td>126</td>
<td>14</td>
<td>TWU, Local 250A plus various craft unions</td>
</tr>
<tr>
<td>Southern Pacific</td>
<td>237</td>
<td>9</td>
<td>Various railroad unions</td>
</tr>
<tr>
<td>Total</td>
<td>1,035</td>
<td>158</td>
<td></td>
</tr>
</tbody>
</table>

Source: Information provided by BART.

UNION ORGANIZATION AND REPRESENTATION ELECTION

A theme that ran through the representation and 13(c) proceedings was that the employees in existing transit systems had a right to "follow their work." There was also an implication that the unions involved would follow their members. Neither was an unreasonable expectation. The 13(c) agreement defined BART as a "coordination" as the term is used in the railroad industry. In transportation this term usually refers to the voluntary or compulsory integration of rates, services or operations by carriers or modes. Coordination often involves questions of through rail rates, joint rail-water rates or the use and operation of common terminal facilities by several carriers. It is difficult to see how BART constitutes a coordination in any operational sense. In the opinion of the author, the use of the term in the 13(c) agreement was an oversight on the part of BART management.

In the railroad industry the employees affected by a coordination would usually be absorbed by the surviving carrier(s). In the BART context, this translated into priority of employment. If the unions had succeeded in attaining their 100 percent priority objective at an early enough date to significantly influence the staffing of BART, this would almost guarantee that the organizations with representation rights on the properties from which they came would win the representation election at BART. However, with one exception, this was not to be.

While the unions with bargaining rights with existing transit companies were busy with the negotiation and litigation surrounding the 13(c) agreement and the representation proceedings, the United Public Employees’ Union, Local 390 (hereinafter referred to as Local 390) of the Service Employees’ International Union (AFL-CIO) was busy organizing existing BART employees. Local 390 began organizing BART’s office staff in 1968 when BART’s offices were still in San Francisco. This was before any transportation employees had been hired and long before any priority employees
came over from existing systems. By July 1972, when the representation hearings were in progress, Local 390 claimed to represent 350 of the 550 non-managerial and non-professional employees then on the BART payroll.

Local 390 had not been a party to the 13(c) agreement because it did not represent employees in existing transit systems; however, it did participate in the representation and 13(c) hearings in a minor way. Its main concern was the protection of the employees then at BART. Mr. Kagel's initial 13(c) award was viewed as a threat to those employees. After Local 390 threatened court action and a strike on their behalf, the award was clarified to the effect that it was not "to affect or place limitations on the relationship between BART and its present non-13(c) employees with respect to wages, hours and working conditions."

By the time the representation and 13(c) proceedings were complete, BART had been fairly well organized by a union that had not been heavily involved in the legal events that led up to the election. Alternately, the unions that were involved in the litigation would be sending their members into an already partially unionized situation.

Local 390 did an effective job in organizing the priority employees as they came into BART. When the representation election was held on April 18, 1973, in the units and under the procedures recommended by Mr. Kagel, Local 390 won the clerical and maintenance subunits of the comprehensive bargaining unit. Division 1555, a newly-chartered division of the ATU, won the transportation subunit which had been largely staffed with priority employees. However, even here, Local 390 made a respectable showing. The details of the representation election are presented in Table 2.

The apparent effect of the comprehensive "umbrella" unit with its three subunits was to protect the position of the ATU among the priority employees concentrated in the transportation subunit. Although one can never say with certainty who would have won an election had the choices been different, given its late start, it is clear that the ATU would have had little chance of winning the whole comprehensive unit. Local 390, on the other hand, would have had a good chance of picking up enough votes to win the larger unit had the election been on that basis and a very good chance of winning a run-off election had no union received a majority on the first ballot, as would have been required.

50. Interview with Paul T. Cooper, BART Employee Relations Manager (May 25, 1968).
51. CAL. PUB. EMPLOYEES REL., NOV. 1972, at 42.
52. Partial 13(c) Decisions, supra note 47.
53. No records are available on which priority employees went into which units and subunits. However, the timing of the hiring and the skills involved, as well as the outcome of the election, strongly suggest that the transportation subunit was staffed mainly with priority employees.
Table 2. Results of Representation Election, April 18, 1973.

<table>
<thead>
<tr>
<th>Unit</th>
<th>Ballots Counted</th>
<th>No Union</th>
<th>Local 390</th>
<th>Local ARSA 1</th>
<th>ATU 2 Division 1555</th>
<th>BPOA Unions</th>
<th>Craft 3</th>
<th>Other</th>
</tr>
</thead>
<tbody>
<tr>
<td>Supervisory Unit</td>
<td>39</td>
<td>15</td>
<td>9</td>
<td>9</td>
<td></td>
<td></td>
<td>6</td>
<td></td>
</tr>
<tr>
<td></td>
<td>(38%)</td>
<td>(23%)</td>
<td>(23%)</td>
<td></td>
<td></td>
<td></td>
<td>(15%)</td>
<td></td>
</tr>
<tr>
<td>Security Unit</td>
<td>53</td>
<td>2</td>
<td>2</td>
<td></td>
<td></td>
<td>49</td>
<td></td>
<td></td>
</tr>
<tr>
<td></td>
<td>(92%)</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Clerical Subunit</td>
<td>147</td>
<td>57</td>
<td>87</td>
<td></td>
<td></td>
<td></td>
<td>3</td>
<td></td>
</tr>
<tr>
<td></td>
<td>(38%)</td>
<td>(59%)</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Transportation</td>
<td>210</td>
<td>20</td>
<td>45</td>
<td>143</td>
<td>(10%)</td>
<td></td>
<td>2</td>
<td></td>
</tr>
<tr>
<td></td>
<td>(10%)</td>
<td>(21%)</td>
<td>(68%)</td>
<td>(21%)</td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Maintenance</td>
<td>555</td>
<td>34</td>
<td>305</td>
<td></td>
<td></td>
<td>191</td>
<td>25</td>
<td></td>
</tr>
<tr>
<td></td>
<td>(6%)</td>
<td>(55%)</td>
<td></td>
<td></td>
<td></td>
<td>(34%)</td>
<td>(5%)</td>
<td></td>
</tr>
<tr>
<td>Total</td>
<td>912</td>
<td>111</td>
<td>437</td>
<td></td>
<td>143</td>
<td>191</td>
<td></td>
<td>30</td>
</tr>
<tr>
<td>Comprehensive</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
</tbody>
</table>

Source: State of California, Dep't of Industrial Relations, Conciliation Service, Results of Bay Area Rapid Transit Election, April 18, 1973. Percentages do not sum because of rounding.

1 American Railway Supervisors Ass'n.
2 This was a new Division of the ATU chartered for BART.
3 Transport Council of Bay Area Craft Unions.
4 Excludes six unresolved challenged ballots.

It will also be noted in Table 2 that the security unit was overwhelmingly won by the BART Policy Officers' Association. This union became Local 1008 of the Service Employees' International Union (SEIU), the same international union with which Local 390 is affiliated.54

Although a majority of the employees involved voted, no union received a majority of the votes in the supervisory unit. A run-off election was held on May 17, 1973, in which the supervisors chose to remain unrepresented.55 Three years later, on June 19, 1976, the supervisors voted to be represented by the BART Supervisory and Professional Association (BART-SPA).56

Consequences and Evaluation

By the summer of 1973, BART employed about 1,000 non-managerial, non-professional persons, over 900 of whom were in the three subunits

55. STATE OF CALIFORNIA, DEP'T OF INDUSTRIAL RELATIONS, CONCILIATION SERVICE, RESULTS OF BAY AREA RAPID TRANSIT ELECTION. (April 18, 1973).
56. Agreement between San Francisco Bay Area Rapid Transit District and BART Supervisory and Professional Association (effective January 8, 1977 through December 31, 1979), § 4 at 3.
of the large comprehensive bargaining unit (see Table 2). Over 150 had come from other transit systems on a priority basis that provided that they retain their former wage rate and their old seniority date for benefit purposes (See Table 1). Thus, a large number of employees scattered throughout BART, and especially throughout the comprehensive unit, were receiving as much as $2 per hour more than their fellow employees who were doing the same work.57 This naturally resulted in feelings of inequity and introduced a major emotional issue into the negotiation of the first labor agreement between the parties.

When formal negotiations for the comprehensive unit began in early May 1973, the unions (Local 390 and Division 1555) demanded that BART equalize wages between priority and non-priority employees.58 No agreement was reached on this issue through May and June, and the unions struck BART at 12:01 a.m. on July 2. During the strike, the definition of "parity" changed from that of equalizing the wage rates of the people employed by BART to bringing BART's wages into line with those of other transit systems in the Bay area.59 The strike lasted until August 1, during which time the system was entirely shut down. When a settlement was finally reached, it included an agreement that inequities would be eliminated during the three-year life of the agreement. It also included a generous (uncapped) cost-of-living allowance, various fringe benefits, a union-shop provision, and a no-strike clause.60

In retrospect, the 1973 strike appears inevitable. It may also have been constructive from an industrial relations point of view. In addition to the usual problems of a newly-recognized union and its leadership having to prove its militancy to the membership and the company, BART had two special problems that reduced the chances of a peaceful settlement. One was the existence of two separate, and until then competing, unions negotiating jointly for the first time. No doubt there were communication and leadership problems that had to be worked out in the course of negotiating a first agreement that was to cover three different employee groups. This, in itself, would have made a settlement without a strike a major accomplishment.

The other special problem was, of course, a phenomenon of the wage and benefit disparity between priority and non-priority employees. The only way management could correct this problem was to spend a large amount of money. It is doubtful that BART's Board of Directors would have, or

57. CAL. PUB. EMPLOYEES REL., August 1973, at 45.
58. Letter from James E. Terry, Director of Employee Relations (BART), to Ernst Stromsdorfer, Deputy Assistant Secretary of Policy Evaluation & Review, U.S. Dep't. of Labor (August 26, 1976), reprinted in F. Siskind & E. STROMSDORFER, supra note 30 at 189.
59. Id.
60. CAL. PUB. EMPLOYEES REL., December 1973, at 47.
politically could have, accepted such a settlement without a reasonable show of determination for the sake of the public and, especially, for Sacramento.

Once both sides had shown themselves and their respective constituencies that they could strike or take a strike, the relationship between BART and the two unions in the comprehensive unit seems to have quickly improved. The eventual elimination of the 13(c)-related inequities, the high wage rates, and generous fringe benefits also helped that relationship.

In July 1976, upon the expiration of the first agreement, BART, Local 390 and Division 1555 reached a second three-year labor agreement without a work stoppage and without much recrimination. In addition, this settlement called for no wage increase beyond cost-of-living adjustments, a 25 percent reduction in entry-level rates for certain new employees, and a 15 percent reduction for certain promoted employees during a 90-day probationary period.\textsuperscript{61} The author is informed that, while there are still some problems to be worked out, relations between BART and Local 390 and Division 1555 are now on a sound and professional level.\textsuperscript{62}

Of course this does not mean that new controversies have not and will not emerge from time to time. On July 8, 1977 a one-day surprise strike occurred when Division 1555 claimed that the manning of two control room electronic consoles with one rather than two persons was unsafe. An agreement was signed at 11:00 a.m. to the effect that BART would go back to using two persons temporarily and if the matter was not resolved by July 22, it would be submitted to binding arbitration. The State Public Utilities Commission subsequently told BART to use two employees on the consoles.\textsuperscript{63}

Another dispute between the District and the BART Police Officers' Association (Local 1008 of the SEIU) resulted in a 13-day strike upon the expiration of their first agreement in August 1977. The dispute ended in a Memorandum of Understanding which established that police officers may not honor the picket lines of other BART employees, but they may refuse to do non-police work during a strike.\textsuperscript{64} A question of amnesty for the strikers was left unresolved with 20 police officers facing possible contempt of court penalties pending litigation.\textsuperscript{65}

The economic impact of BART's 13(c)-related experience is more difficult to determine. In a study reported on April 4, 1978, BART compared its

\textsuperscript{61} CAL. PUB. EMPLOYEES REL., September 1976, at 106.
\textsuperscript{62} Interview with Charles A. Simon, BART Manager of Labor Relations (May 19, 1978).
\textsuperscript{63} CAL. PUB. EMPLOYEES REL., September 1977, at 40.
\textsuperscript{64} CAL. PUB. EMPLOYEES REL., December 1977, at 24.
\textsuperscript{65} Id.
wages and benefits with those of other organizations. Table 3 presents some wage data extracted from that study; it shows that BART's wage rates are substantially above those of other employers in the area and other systems in the industry. In addition, BART's benefits and cost-of-living allowance equal or exceed those in any of the organizations surveyed.

Table 3: Comparison of BART Wage Rates with Other Organizations for Selected Classifications, December 1977. (Percent figures indicate percentage by which BART rates exceed those of other organizations surveyed.)

<table>
<thead>
<tr>
<th>Classification</th>
<th>All Organizations</th>
<th>Local Organizations</th>
<th>Transit Organizations</th>
</tr>
</thead>
<tbody>
<tr>
<td>Clerk Typist</td>
<td>+23%</td>
<td>+22%</td>
<td>+19%</td>
</tr>
<tr>
<td>Storekeeper</td>
<td>+19%</td>
<td>+31%</td>
<td>+10%</td>
</tr>
<tr>
<td>Janitor</td>
<td>+26%</td>
<td>+36%</td>
<td>+21%</td>
</tr>
<tr>
<td>Senior Electrician</td>
<td>+10%</td>
<td>+6%</td>
<td>+11%</td>
</tr>
<tr>
<td>Train Operator</td>
<td>+17%</td>
<td>—</td>
<td>+17%</td>
</tr>
<tr>
<td>Bus Operator</td>
<td>+20%</td>
<td>+17%</td>
<td>+21%</td>
</tr>
<tr>
<td>Station Attendant</td>
<td>+44%</td>
<td>—</td>
<td>+44%</td>
</tr>
</tbody>
</table>


Obviously, BART's labor costs are high. Whether or not they are higher than they would have been in the absence of its 13(c) agreement is an interesting but unanswerable question. BART would have been under strong pressure to approximate the wage and benefit levels of other transit systems in the Bay Area regardless of which union or unions ended up representing its employees and regardless of the way in which those employees were hired. In the Bay Area, the San Francisco Municipal Railroad (MUNI) sets the pattern for other transit systems. Rates at the MUNI are required by charter to be as high as the two highest transit systems in the United States in cities of over 250,000 population with 400 or more operators. In recent years the comparison has been made with two systems in New York City. Thus, it is likely that BART's labor costs would have been just as high in the absence of section 13(c), priority employment, the particulars of the bargaining-unit decision, and the outcome of the election. To say that the elimination of the inequities caused by the priority employment concept was expensive assumes either that the pre-strike wages and benefits established by management were "appropriate" or, that in the absence of the priority employees, the unions would have held out for less. Neither assumption is easy to accept. BART's pre-1973 wage rates had been based on a survey that included non-transit employers in the area and were

67. 13(c) Proceedings, supra note 20, at 436, 553.
admittedly low.\textsuperscript{68} It is highly probable that the wage and benefit levels at BART would have approximated those of other transit systems in the Bay Area in a short time independent of the events discussed in this paper. However, it is possible that these levels would have been attained without the cost and benefit of the strike of 1973.

The probable high cost of the priority employment concept results from the fact that the employees who came from other transit systems brought with them their old seniority date for benefit purposes in addition to their former higher wage rate. As of June 30, 1973, the 73 priority employees who had joined BART had an average seniority of about six years. This resulted in an extra 126 weeks of vacation and 393 days of sick leave.\textsuperscript{69} No doubt some of this cost was offset by the acquisition of a partially-trained, stabilized, and industry-committed work force. Counter to this, it has also been argued that in the absence of priority employment, BART would have been faced with an even larger number of adverse-effect claims.\textsuperscript{70} This too would have offset some of the cost directly associated with the priority employment part of the 13(c) agreement.

\textit{Conclusion and Comment}

What is the importance of BART's 13(c) experience? Obviously, it was and is of considerable importance to BART management and to the unions and employees involved. It may also be of some financial importance to the BART District taxpayers who pay an additional one-half of one percent sales tax to support the system and, less directly, to the taxpayers in the rest of California and the rest of the United States. However, there is also a more general, non-financial lesson to be drawn from the events outlined in this article.

The centerpiece of BART's industrial relations development was its 13(c) agreement. Once this had been agreed to, everything from Mr. Kagel's interpretation of that agreement to the strike of 1973 was all but programmed. Given the unique fact situation, the language of the Urban Mass Transportation Act\textsuperscript{71} and BART's 13(c) agreement, and the established practices and interpretations in the railroad industry, it is unlikely that the award of any qualified arbitrator would have been substantially different from Mr. Kagel's. Regardless of what bargaining-unit structure was

\textsuperscript{68} Letter from James E. Terry, Director of Employee Relations (BART), to Ernst Stromsdorfer, Deputy Assistant Secretary of Policy Evaluation & Review, U.S. Dep't of Labor (August 26, 1976), reprinted in F. Siskind & E. Stromsdorfer supra note 30 at 190.

\textsuperscript{69} BART, "Comparative Benefits of 13(c) Priority Hires Contrasted With Those Non-13(c) Personnel Hired From Other Sources," reprinted in F. Siskind & E. Stromsdorfer, supra note 30 at Appendix A-9.

\textsuperscript{70} F. Siskind & E. Stromsdorfer, supra note 30 at 179.

adopted, the existence of the priority employees and the attending wage and benefit inequities would have made it most unlikely that a first agreement could have been arrived at without a strike.

The history of section 13(c) and its ancestral statutes, agreements, decisions, and interpretation over the past 40 years has been one of continual expansion and elaboration. What started as a simple concept to protect employee interests during railroad consolidations has grown into a monster when applied to the urban mass transit industry.

There is nowhere else in American industry, other than the railroads (which stand as a very poor example for the rest of the economy), where employees are statutorily given such job protection. It may be argued that all employees are due a degree of job security, but it is difficult to accept the idea that railroad and transit employees have a special claim to such protection.

The application of the 13(c) concept to transit is an historical accident resulting from the shift from private to public ownership of much of the industry. The initial arguments were in the nature of protecting collective bargaining rights under such conditions. Job protection, as developed in the railroad industry, was an afterthought and more reflective of the political muscle of organized labor at the national level than a reasoned approach to any problems that might have been caused by UMTA\textsuperscript{72} funding. The expansion of that concept to include priority employment in a newly-constructed system was especially questionable.

It may be argued that BART willingly entered into the 13(c) agreement and, therefore, no recriminations are in order. It may be that BART’s management and counsel were less alert than they should have been. It may also be that the unions took advantage of an opportunity to advance the interests of their members and/or that the Department of Labor failed to exercise the leadership and balance that it should have. But that is not enough.

The tragedy in BART’s 13(c) experience is that it is only one example of a much larger and continuing problem. That problem centers on the interaction of public ownership, control, and/or support of various activities and the political influence and expertise of organized labor.

American labor unions are among the greatest institutions in the free world and their political involvement is an integral and important part of the democratic process in the United States. However, the character and personality of the labor movement developed, and to a great extent continues to develop, in the private sector. There the companies have traditionally been relatively free of the need to placate Washington and the state capitals. Indeed, they have considerable political influence and have

\textsuperscript{72} Urban Mass Transportation Administration.
tended to counter what might otherwise have become a serious political imbalance. In public transit and other similar situations, however, the "company" is dependent upon governmental decision for its very existence. This dependence, which is not limited to UMTA grants, presents the labor lobby with many opportunities to apply the pressure of an organized interest group pursuing a limited purpose. Examples include the addition of section 13(c) in the Urban Mass Transportation Assistance Act and the inclusion of priority employment in BART's 13(c) agreement. No doubt the reader can think of many others.

None of these events is particularly newsworthy. Yet, when we step back and survey the 40-year development in the railroad and transit industries, we are confronted with a powerful, almost glacial, evolutionary force. To this observer, the overall development is most disturbing.

While job protection and priority employment may be to the advantage of some employees and their unions, it is to the disadvantage of others. If it were measurable, the net benefit would approach zero.

The direct impact of section 13(c) on the management of a particular transit system may be negligible or, at least, acceptable. In addition to the reasons for this developed above, transit systems are almost always subsidized monopolies. As such, they can shift additional cost either forward to the rider in the form of higher fares or poorer service or backward to the taxpayer. However, the costs of job protection and priority employment to the economy are considerable. In addition to the direct expense of adverse effect and priority employment touched upon in this paper, most economists would agree that there are important, but subtle, costs associated with the misallocation of resources whenever economic decisions are made for non-economic reasons. In the immediate example they would include the additional replacement and training costs to the companies from which the priority employees came and the administrative and legal expenses of processing them and the other employees who may claim to be "affected." They would also include the cost to BART of having had restricted its recruitment pool to a small fraction of the potential applicants available, which presumably results in a poorer average quality of employee hired.

This is not a call to return to pure competition. In public transit that would be especially inappropriate. It would quickly eliminate most of the industry and deny the country the social and indirect economic benefits of urban mass transit. However, it must be remembered that job protection and priority employment are not "free goods;" they cost money. The fact that the cost may be shifted forward in the form of higher fares or poorer service or backwards in the form of higher taxes may make it more palatable to transit management and the labor organizations with which it deals. This only disperses the problem; it does not eliminate it.

The railroad and transit industries have set a bad example by agreeing
to the unions’ demand for job security, and they are less efficient because of it. Unfortunately, it would be politically impossible to reverse this development for these industries. The best that can be hoped for is that its expansion can be arrested. However, it is not too late to prevent the extension of these concepts to other industries, especially other transportation industries.
Price Competition and the Role of Rate Bureaus in the Motor Carrier Industry*

A. DANIEL O'NEAL**

The trucking industry has experienced phenomenal growth since the enactment of the Motor Carrier Act in 19351 and the passage of the Reed-Bulwinkle Act in 1948. In 1947 the industry earned freight revenues of $2.2 billion; by 1975, that figure had increased to $21 billion. By 1976 intercity trucking (excluding private carriage) accounted for $56 billion out of $98 billion earned by all intercity freight carriers. Investment in trailers in 1947 was $2.8 billion; by 1975 that had increased to $41.8 billion.3

The trucking industry’s dramatic rise from an adventurous band of one-truck companies in the 1930’s to its present prominent status and the contribution of that industry to the nation bears witness to the environment within which the industry has functioned. Regulation has been a major part of that environment. The swift growth of the industry also suggests that yesterday’s solutions may not fit today’s problems.

Indeed, we have evidence that the trucking industry has grown so fast

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* Statement presented before the Subcommittee on Antitrust and Monopoly of the Senate Committee on the Judiciary, April 26, 1978.

** Chairman, Interstate Commerce Commission.


that the changes in the regulatory system have not completely kept up. The sale on July 9, 1976, of the operating certificates of two affiliated bankrupt motor carriers—EasternFreightways and Associated Transport—for $20.5 million dramatized the high market value of many certificates today. It indicates that the obligations imposed upon the industry—the duty to provide common carrier service—at present do not appear to constitute an economic burden to the industry commensurate with the economic benefits it receives from limited entry and antitrust immunity for collective ratemaking.

We need either to assert more forcefully the common carrier responsibilities of the industry or to reduce the economic benefits of regulation. We need to achieve a better balance of the two. Our legislative mandate supports that approach. The Interstate Commerce Act provides for a system whereby resources in the trucking industry are allocated not only in response to market forces but also in part pursuant to the judgment of a group of people appointed by the President, confirmed by the Senate, and charged with responsibility of assuring that this vital industry operates in the public interest. These people have historically discharged their responsibilities in the light of broad consideration of social policy, including—but not limited to—purely economic factors.

The specific means which the Commission may pursue to keep regulation current with the present needs of the public deserve mention. Limited entry and collective ratemaking provide the industry with a measure of protection from pure competition, although a measure of competition—in the form of the entry each year of new carriers into the industry, the entry of existing carriers into new markets, and the exercise by the carriers of their right of independent action to set rates individually—has always existed in the motor carrier industry.

The basic premise of surface transportation regulation is that some restraints were placed on competition in transportation so that competition could flourish among non-transportation businesses, individuals and communities throughout the country. We are currently examining whether the restraints should be loosened in the motor carrier industry. As you know, a Staff Task Force has presented the Commission with a list of 39 recommendations to liberalize motor carrier entry and to streamline the Commis-

4. Eastern Associated is not the only example of a certificate being sold for a great deal of money; the situation is widespread, a subject of an ongoing Commission analysis, and a matter of serious concern.
6. It is important to note that for purposes of this analysis we are contrasting the existing system with "pure" competition—which in theory would drive prices down to long run marginal cost. However, the market is an imperfect mechanism, and we do not have sufficient knowledge to be able to say whether or to what extent the prices resulting from the operation of market forces in the trucking industry would tend toward long run marginal costs.
vision's regulatory procedures. One of these recommendations—which I discussed in my testimony in October—is now a rulemaking proceeding. On February 8, 1978, the Commission voted to approve its Notice of Proposed Rulemaking and Order in Ex Parte No. MC-116, *Consideration of Rates in Operating Rights Application Proceedings.* In that rulemaking we will be considering the feasibility of authorizing entry into the motor carrier industry based on the commitment to publish and maintain lower rates. This is a concept with substantial implications for the future of competition and regulation in the motor carrier industry, and we will give it our closest attention.

The Commission's Task Force made a number of other recommendations which, if adopted, would ease entry into the industry. We are moving ahead on these recommendations, and I hope we have action on many of them completed by later this year.

The Commission's actions in the area of motor carrier entry are not limited to the Task Force recommendations. As we noted in open conference on February 21, 1978, we are looking for a test case to review current restrictions placed on contract carriers, and at the conference on January 17, 1978, we took up the subject of limitations placed on private carriage. And in its adjudications of individual cases, the Commission has taken some substantial steps. For example, in *Toto Purchasing & Supply Co., Common Carrier Application,* decided March 10, 1978, the Commission struck down a 40-year-old prohibition against granting operating authority to private carriers.

The Commission is also reevaluating its regulations concerning motor carrier rate bureaus. Last October I noted that the Commission would consider whether or not the 4-R Act's new *rate bureau regulations for railroads should be applied to motor carriers.* On December 30, 1977, the Commission instituted a rulemaking proceeding in Ex Parte No. 297 (Sub-No. 3), *Modified Terms and Conditions for Approval of Collective Ratemaking Agreements Under Section 5a of the Interstate Commerce Act.* There we will consider whether the Commission should (and whether we can) apply the 4-R Act's prohibition against bureau members voting on single line rates or interline rates in which they do not participate, and the 4-R Act's ban on bureau protests of the filings of non-member carriers, to the motor carrier industry.

Now that the Fourth Circuit Court of Appeals has upheld the Commission's order in Ex Parte No. 297, we have set a schedule to review all the

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motor carrier industry's outstanding rate agreements in the light of the new Ex Parte No. 297 requirements, and the National Transportation Policy.

These are some of the actions which would increase competition and strengthen the impact of market forces in the trucking industry. We feel that as the trucking industry has grown, it needs protection from these forces less than it did during the period of its growth to its present level of maturity.

But we also feel just as strongly that increased reliance on the market is not the only course of action which we should pursue to assure the continued operation of this industry in the public interest. The Interstate Commerce Act—and the tradition of common carriage upon which it is based—allocates resources on the basis of considerations which differ somewhat from those dictated by the market. Common carriage imposes social responsibilities on carriers, and establishes pricing patterns based on social decisions which can be fairly debated but should not be dismissed out of hand. It requires that whoever holds himself out as a common carrier provide service within the scope of his authority on reasonably equitable terms to all comers.

A key element in this system of government enforcement of common carrier obligations is the prevention of unjust discrimination by carriers among shippers and among communities. Congress felt sufficiently strong about this issue, that, while it gave the railroads substantial ratemaking freedom under the 4-R Act, it kept intact the Commission's authority to police unjust discrimination and undue preference and prejudice.

The marketplace allocates resources without regard to popular notions of equity. In a pure market system, without any economic regulation, a large and powerful shipper could obtain price concessions and preferential service which carriers would not make to smaller shippers. By establishing a system of regulated collective ratemaking, Congress has provided a means by which individual carriers may resist the pressure of powerful individual shippers to establish lower rates on their behalf.\(^\text{11}\)

This is not to say that the existing system offers complete protection to

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\(^{11}\) Mr. Shenefield took note of the anti-discrimination function of the current regulatory system, albeit in a rather backhand way, in his testimony before the Subcommittee last October. He noted, "Finally, it might be asked, if the system is so bad, why aren't the shippers screaming for relief? After all, they deal directly with the trucking industry, paying those inflated rates. One short answer is that many shippers are more interested in seeing that their competitor doesn't get a better rate than they are in the level of the rate. In other words equal rates are more important to many shippers than lower rates." Mr. Shenefield suggests that lower rates are better than equal rates. Perhaps from a purely antitrust viewpoint that is so. But American society has also favored dispersing economic power among a large number of firms, even where that means foregoing some price reductions which could result from allowing large firms to exploit their scale economies. Total deregulation in the trucking industry would mean one less protection which small shippers have against the economic power of their larger brethren. Perhaps lower consumer prices (if they do in fact occur and continue) would justify that action; perhaps not.
small shippers. The really big shippers have established sophisticated physical distribution systems employing private carriage and thus haul their own products effectively at cost. Independent actions allow some shippers to exert power on certain carriers, though the fact that the rates are subject to shipper protest and usually are not published to apply specifically to one shipper minimizes the potential for discrimination.

I do not suggest that the Commission should—or could—regulate motor carrier rates so as to equalize the price of motor carrier service among all shippers and among all communities. There is a limit to the extent to which we should go in foregoing real economic benefits in order to serve social ends. This is an area where intelligent tradeoffs must be made.

Perhaps when all is said and done, the American public will prefer to take its chances with the potential for increased concentration of economic power among shippers and carriers created by deregulation in its desire to pocket whatever reduction in consumer prices the development of market competition would yield. If the public makes that decision on the basis of reliable information and following an enlightened discussion of the issue, so be it. The point to be noted is that change brings both benefits and draw- backs, and a major drawback of increased competition is the increased potential for discrimination.

The potential for discrimination among shippers carries the threat of increased economic concentration. The potential for discrimination among communities carries the potential for adverse economic and social consequences for the communities which would be subject to discrimination—and, of course, benefits for those communities preferred.

Some care should be taken with this discussion, especially with respect to the use of the term discrimination. What is unjust discrimination to one person is social justice or economic sanity to another.

I doubt that the motor carrier industry carries goods at a rate below the actual costs of transporting the goods to any great extent. But it also appears that carriage to some communities is more profitable than to others. In theory, licensed carriers operating under a common carrier injunction to provide service within the scope of their authorities, and given a certain amount of protection from the rigors of total competition, will not seek to maximize profits on each unit of service. The carriers will tolerate a level of profit on the less lucrative routes which falls below the return the carriers could earn if they invested elsewhere the money needed to provide the service.

That is the theory, and it raises two issues. Is it actually operating and, whether it is or not, should it be?

We know from the fact that dormancy is an issue in many motor carrier finance cases that there are carriers which are not providing service within
the full scope of their authorities. On the other hand, a number of factors—including the concern that dissatisfied shippers will support the applications of new carriers for grants of authority which might embrace desirable as well as undesirable hauls—indicate that carriers are not totally ignoring the obligations of their certificates either. The information which the Subcommittee and the Commission gather from the Continuous Traffic Study\(^\text{12}\) ought to shed some light on this issue.

Even if it were assumed that carriers were largely ignoring their common carrier obligations to provide reasonably adequate, non-discriminatory service within the scope of their certificates, that situation would not necessarily suggest a need to deregulate: it can be argued that the more appropriate solution would be to enforce the existing service obligations.

But the issue of whether or not motor carriers are providing nondiscriminatory service to small communities does not get to the more important question: Should small communities—any more than small shippers—have recourse to a regulatory agency to establish their freight rates on some basis other than the market? Why should the shippers and consumers living in Podunk get protection not afforded to the citizens of New York City? On the other hand, the Nation has always asserted that it is in the public’s interest that all parts of the country enjoy certain minimum service levels in key areas—power, communication, transportation, etc.—regardless of market considerations. How would service levels to small towns differ under a free market system than under the current system? Would there be any significant difference? A move to uninhibited reliance on the market would be easier to make if we had answers to these questions.

The above concerns—together with our existing statutory mandate—indicate that the Commission needs to take a hard look at whether carriers are meeting their common carrier obligations, and to define those obligations so that they can be practicably enforced. One example of a current Commission initiative in this area is our investigation into discrimination by carriers in their credit practices in Ex Parte No. MC-73, Regulations for Payments of Rates and Charges.\(^\text{13}\) Another is Ex Parte No. MC-77 (Sub-No. 2), Regulation Governing Restrictions on Service by Motor Common Carriers.\(^\text{14}\) The Commission is also undertaking new initiatives in the enforcement area, for example, through its actions against weight bumping in the household goods area and by the prosecution of carriers who retain duplicate payments by shippers. We are also reducing the Commission’s protectionist role in the enforcement area by advising carriers complaining

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\(^{13}\) 350 I.C.C. 527 (1975).

\(^{14}\) 129 M.C.C. 71 (1978).
about unauthorized carrier operations that their appropriate remedy is self-help.

Another characteristic of motor carrier pricing behavior resulting from regulation is the measure of stability introduced into the process of establishing and maintaining levels of carrier services and rates. While carrier support for such stability can be attributed to the desire to avoid competition, the basis for shipper support must lie elsewhere. Shipper support for a measure of stability in levels of rates and services does exist; Commissioner Clapp and I both heard such views expressed during the field hearings which we conducted on the Staff Task Force recommendations. It seems to be based on a desire by the users of the motor carrier system to be able to make plans for using it with a degree of certainty that it will not exhibit substantial price and service changes within a short period of time.

The desire of carriers and users for a measure of stability is not, however, reason to discourage marketing innovations by aggressive carriers. That sort of initiative ought to be encouraged. For example, we supported the publication of alternative rates for different levels of service—premium, regular and standby—in our report in Ex Parte No. MC-98, New Procedures in Motor Carrier Restructuring Proceedings.15

As I noted in my testimony last October, the Commission's mandate under the Interstate Commerce Act is to balance the goals of antitrust policy—market competition—with the achievement of the other social policies embodied in the Act. The motor carrier system at present is providing good service to the satisfaction of most of its users. That fact must be given some weight.

But the maturity of the trucking industry and the growing complexity of the demand for motor carrier service dictates that increased reliance be placed upon competition as a tool to assure that the industry performs in the public interest.

We should not move so fast in that direction that we forfeit the opportunity to learn the practical consequences of each step in that direction. And we need to move affirmatively to remedy the scarcity of useful data on the motor carrier industry, in order to enable us to monitor the industry's responses to the changes that lie ahead.

The following sections set forth a discussion of Commission rate regulation in the motor carrier area. They include a review of the history of and current practices of motor carrier ratemaking, with particular focus on cost finding.

II. HISTORY OF MOTOR CARRIER RATEMAKING

A. INTRODUCTION

When the bill that was later to become the Motor Carrier Act of 1935 was submitted to the Senate for vote, it was accompanied by a report by Senator Burton Wheeler, the Chairman of the Committee on Interstate Commerce. The report stated that passage of the bill was required due to the conditions in the motor carrier industry, which were described as follows:

In recent years there has been an extraordinary growth of highway transportation. Thousands of miles of hard-surface highways have been developed and are teeming with millions of automotive vehicles. Motor carriers for hire penetrate everywhere and are engaged in intensive competition with each other and with railroads and water carriers. This competition has been carried to an extreme which tends to undermine the financial stability of the carriers and jeopardizes the maintenance of transportation facilities and service appropriate to the needs of commerce and required in the public interest. The present chaotic transportation conditions are not satisfactory to investors, labor, shippers, or the carriers themselves.\textsuperscript{16}

Thirty years later the Committee on Commerce conducted an evaluation of the 1935 Act. In the report of that evaluation, Edwin C. Johnson, former member and chairman of the Interstate and Foreign Commerce Committee, recalled his preregulation experience as a motor carrier owner. The Senator observed that, prior to the passage of the act, the operation of interstate motor transportation was a "homeless and precarious" business; equipment was undependable due primarily to unprofitable operations. The rate structure was "what you could get" and the business was a "gamble with the odds against you."\textsuperscript{17}

Commenting on the effect of the 1935 Act, Senator Johnson went on to state:

No one could have guessed that the passage of this act could have straightened out this frustrated business so completely. The 1935 act brought order out of chaos and did it almost overnight. I know of no single statute on our books that did quite so much for American transportation or business progress generally as did the Motor Carrier Act of 1935.\textsuperscript{18}

Today, even some of the severest critics of regulation concede that the United States has, judged by almost any standards, the best and most comprehensive domestic transportation system of any country in the world, and that it is probably the most efficient.\textsuperscript{19} The regulated Motor Carrier industry is the backbone of this transportation system. The time since the passage

\textsuperscript{18} Id.
\textsuperscript{19} Pergum, Should the ICC be Abolished?, in G. Davis, Transportation Regulation: A Pragmatic Assessment 51 (1976).
of the 1935 Act has witnessed giant strides in industrial and commercial development with concomitant demands on the motor carrier industry to meet growing transportation needs. Those changes indicate the need for a fresh look at motor carrier regulation.

B. Rate Regulation Provisions of the Act

In reviewing the legislation we find that the regulation of rates is an important part of it. In particular the Act provides:

1. Publication of rates and fares is required and there must be strict observance of tariffs.
2. Rates and fares are to be reasonable and not unjustly discriminatory.
3. Carrier practices and regulations relating to fares and charges are to be just and reasonable.
4. Notice of at least 30 days is required for changes in rates and fares.
5. Proposed rates and fares may be suspended by the Commission for a period not exceeding seven months.
6. The Commission has power to prescribe the maximum, minimum, or actual rate to be charged in lieu of a rate found unreasonable or otherwise unlawful.
7. The Commission has the power to hear complaints and institute investigations pertinent to its Congressional mandate.

These provisions reflect specific objectives of motor carrier rate regulation. For example, the requirement that carriers establish, observe and enforce just and reasonable rates and practices and the prohibition of discrimination among shippers reflects the intention that shippers will pay, and that carriers will receive, a rate that fairly reflects the service rendered regardless of competitive conditions. Undue discrimination against different shippers, points, and territories has historically been proscribed in the transportation field. The antidiscrimination provisions prohibit a carrier from unduly favoring one party or segment of traffic to the detriment of others. The emphasis is on "undue;" a mere difference in rates, standing alone, does not constitute undue discrimination and prejudice.

Small shippers are particularly susceptible to rate discrimination. Through our present system of published rates and antidiscrimination provisions, the small shipper is able to know the transportation situation of its competitors and enforce upon carriers a duty of equitable treatment. Thus, at least insofar as transportation services are concerned, the small shipper is enabled to compete with the assurance that the economic leverage of others, or its lack of it, will not be permitted to unduly prejudice its business endeavor.

The Commission's suspension and investigatory powers and its jurisdiction to hear complaints reflects in part an attempt to encourage rate stability. A stable rate structure is desired by both carriers and shippers. Carriers desire a stable rate structure for business planning purposes, so
that over time they can be reasonably sure of the level of revenues they will receive. A rate structure that is not subject to radical fluctuations and which provides carriers a fair return fosters financially responsible and stable carriers. Shippers find unstable rates to be a disconcerting element in business transactions. For example, future sales often involve calculation of existing freight charges or those expected in the near future. Such calculations are not possible, absent a reasonably stable rate structure.

It should be noted that the Act’s rate provisions are concerned primarily with common carriers. Contract carriers are required to publish their rates, and are required to adhere to their published rates. (This is a result of a 1957 amendment. Under the original act they were only required to publish their minimum rates.)

The Act gives the Commission power to prescribe minimum rates for contract carriers. The fact that the Commission cannot prescribe maximum rates and the lesser requirements placed on contract carriers indicate that contract carriers, defined as carriers providing service to a limited number of persons, do not have common carrier obligations to the general public.

Predictably, the question of the proper relationship between common and contract carrier rates arose. Although numerous states, by statute or by policy, require contract carriers to maintain rates no less than those charged by common carriers, this has not been the Commission’s policy. The Interstate Commerce Act, amended by the Transportation Act of 1940,20 as a declaration of policy, requires the Commission to administer the Act so as to recognize the inherent advantages of the various modes of transportation. By being able to select the shipper it will serve and the traffic it will carry, the contract carrier is able to provide service at a lower rate in many instances. This is an inherent advantage of contract carriage, and the Commission, recognizing it as such, has declined to hold contract carrier rates up to the level of common carrier rates.

C. Broad Trends in the Rate Environment

Under the Motor Carrier Act of 1935,21 which became Part II of the Interstate Commerce Act, motor carriers were required to file their initial tariffs and schedules on or before April 1, 1936. The initial tariffs filed by many motor carriers were almost reproductions of the then effective tariffs of the rail carriers.

These initial publications of motor carriers reflected many differences in rates between operators for like services in the same territory. It was only

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after the initial filing of schedules that carriers became aware of the rates and charges of their competitors. In an effort to bring about a more uniform rate structure, a number of carriers voluntarily equalized their rates. This equalization was generally toward lower rates, and ultimately, a number of rate wars commenced.

Consistent with the protectionist philosophy of the time, the Commission stepped in and conducted a number of investigations which resulted in the establishment of minimum rate orders. These orders prescribed a level of rates below which motor common carriers should not go, and produced the desired result of the financial improvement of the motor carrier industry. Minimum rate orders were entered in: (1) Middle Atlantic Territory, (2) Central Territory, (3) New England Territory, (4) Midwestern Territory, and (5) Trunk Line Territory. The Commission’s order provided for modifications through petitions, and in fact many such petitions were filed by shippers and carriers alike. These minimum rate orders discouraged rate cutting and made it mandatory for motor carriers to obtain approval of the Commission before the publication of rates lower than the minimum rates prescribed.

 Immediately prior to World War II, motor carrier traffic increased, the industry improved financially, and the minimum rate orders were vacated.

 The post World War II period has been marked by a growing, rapidly expanding economy and accompanying moderate to severe inflation. The motor carriers have sought to keep up with industrywide cost increases—especially those involving labor—through general rate increase proceedings.

 A request for a general increase is based on systemwide revenue needs as opposed to those concerning only particular movements, commodities, or segments of traffic. Unlike ordinary rate proposals, a general increase is normally sought as a percentage increase applicable to all or nearly all rates maintained within a ratemaking territory. In approving or disapproving a request for a general increase the Commission has cited the "rule of ratemaking," which maintains first, that carriers be permitted to charge rates sufficient to meet their revenue needs and to enable them to fulfill their service obligations at the lowest cost consistent with the furnishing of the service.22

 In 1970 the Commission established formal procedures and evidentiary requirements for general rate increases in Ex Parte No. MC-82, Proposed New Procedures in Motor Carrier Revenue Proceedings.23 This process will be discussed at greater length in Part IV of this testimony.

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III. COMMISSION RATEMAKING IN THE MOTOR CARRIER INDUSTRY—POLICY AND PRACTICE

A. RATEMAKING PROCEDURES

The system of ratemaking prescribed by Congress places the initial responsibility upon the carriers to set rates.24 The regulatory role of the Commission is basically that of a check on carrier ratemaking designed to safeguard the public against unjust and unreasonable rates and practices, unjust discrimination, undue preference or prejudice, and destructive or unfair competition.

Carriers initiate rates by publishing them in tariffs which are filed with the Commission at least 30 days (45 days for general commodities carriers general rate increase proposals) prior to the date they are to become effective, unless a shortened period is authorized by special permission. The rates to be published by the carriers may be agreed upon jointly through the carrier's rate bureau activities or by independent action of the carrier. A protest challenging the lawfulness of the proposed rate may be filed by any person, except that a rate bureau may not protest their carriers' independent actions. Many shippers subscribe to tariff watching services or join associations such as the National Small Shipments Traffic Conference in order to more effectively monitor and/or protest rate actions which affect them.

At this stage of the ratemaking process (i.e., prior to the effective date of the tariffs), the Commission analyzes informally the lawfulness of the protested rate proposal. In the case of a rate proposal that is not protested the Commission may initiate this analysis on its own. In addition, all tariffs are examined for conformity with the Commission rules and regulations pertaining to the filing of tariffs; the Commission's general review of tariff filings is discussed later in this section.

The carrier is given the opportunity to justify the proposal in either event. If it appears that the proposed rates are reasonable and otherwise lawful, they are permitted to become effective without formal investigation. On the other hand, if the opinion is reached that the tariff schedules would result in unlawful rates, we subject them to an investigation. Ordinarily, in such cases, the operation of the investigated schedules would be suspended for the 7 months permitted by law. As an alternative, a rate may be investigated without suspension. Where a proposed increase is not suspended but is investigated and later found unlawful, it is ordered cancelled. The Interstate Commerce Act does not authorize the Commission to require refunds with regard to motor carrier rates.

The initial decision whether to suspend and/or investigate is usually

made by Commission staff experts, members of the Suspension and Fourth Section Board. An additional safeguard is that in every case there is provided an opportunity to appeal this determination to a division of the Commission. Some of the more complex cases, such as motor carrier general increase proceedings, are decided initially by the Commission. In any event, the entire process is completed within 30 days.

After a decision to suspend and/or to investigate, the merits of the tariff are examined in an evidential hearing. In some instances this can be accomplished by the submission of verified statements by the parties and the issuance of an employee board report setting forth findings of fact and conclusions of law. The employee board's findings and conclusions are subject to appeal to the division. Other cases may be assigned for oral hearing before an Administrative Law Judge, although concurrent verified statements may also be required under special procedures. The Administrative Law Judge's decision is also subject to appeal.

After a rate has been allowed to become effective (i.e., not suspended) and not investigated, shippers can challenge its lawfulness by filing a complaint. Such proceedings may result in a finding that the rate is shown to be unlawful and an order requiring its cancellation.

B. Tariff Review

Through its power to examine tariff filings and to suspend and investigate those that appear contrary to law,25 the Commission provides a considerable measure of protection for the many smaller interests that simply do not have the resources to analyze and protest rate proposals that adversely affect them. These powers permit the Commission to protect the interests of the public in its largest sense, without relying on action by someone immediately affected by a given proposal.

The Commission expends substantial resources in the review of carrier rate filings. All the tariffs filed (approximately 360,000 in fiscal year 1977)26 are examined for compliance with statutory provisions, Commission orders and tariff filing regulations. All motor carrier general increase proposals are examined in detail and subjected to full review and determination of lawfulness on the merits.

Beyond this, there is a substantive review of all the tariff filings of the major rate bureaus, the specialty carrier bureaus, and individual publications of major carriers. This review of the substance of proposed changes in rates, rules or provisions is effected through the consumer-oriented tariff examination program. The program is designed to compress the Commission's limited tariff expertise resources and focus it on the publications.

25. Id. § 10704.
which have the broadest application over the traffic moving in the regulated carrier system. This concentration of review recognizes that the individual publications of several thousand small motor carriers have no significant impact on the traffic departments of the thousands of shippers which might utilize their services. The small carrier is in no position to influence the financial stability of a shipper, large or small; the shipper might negotiate price (rate) adjustments with a small carrier, but taken individually or collectively, the tariff publications of the small carriers are simply not significant or influential enough to warrant in-depth examination of each publication. This frees the Commission to focus its tariff examination resources on the rate bureaus and large carriers, as is done via the consumer-oriented tariff examination program. There, the emphasis is on seeking out proposed changes which will increase the tariff users' costs.

The review includes, but is not limited to the following:

*High less-than-truckload rates* that have the economic effect of an embargo on small shipments. Also rates that are of such a high level that they will not move the traffic involved, and thus in effect embargo that traffic.

*Minimum charges* at high levels require justification. These high minimum charges also have the effect of placing an embargo on the affected traffic.

*Exception ratings and commodity rates* of motor carriers that result in charges that exceed the classification basis must be accompanied by justification when filed with the Commission.

*Pickup or delivery charges* that apply only to selective named points.

*Arbitrary charges* that apply only to selective points.

*Joint rates restricted* to named points.

*Surcharges of any nature* that have the effect of increasing the cost to the shipper.

*Limitations of liability.* Tariff provisions which attempt to relieve the carrier of responsibility for loss or damage.

*Additional liability provisions.* Tariff provisions which provide that carrier will accept additional liability depending upon payment of additional charges.

*Cancellation or increasing* of rates to small communities.

*Increased rates filed under authority of section 15(8)(b) and 15(8)(c) of the Interstate Commerce Act (Yo-Yo Filing).* Verification that the increases do not exceed the increases authorized.

During Fiscal Year 1977 the consumer examining staff reviewed 202,401 publications. Of that number 1,084 were rejected and 3,293 were criticized, *i.e.*, a letter was sent out informing the carrier that the tariff is offensive and asking correction of the offending provision or cancellation
of the tariff. The criticisms also led to 1,182 publications either voluntarily cancelled or amended by affected carriers, among which were 236 publications that involved reductions in motor common carrier service. The staff referred to the Commission's Suspension and Fourth Section Board 405 publications for its consideration and possible suspension. Of that number, 142 were placed under suspension and/or investigation. A number of cases were also referred to the Commission's Bureau of Operations for possible investigation. Finally, 2,752 letters, in addition to the 3,293 criticisms mentioned above, were written to motor carriers requesting justification of proposed cancellations of joint routing provisions, i.e., a reduction in service.

The Commission's tariff review helps to protect the public against unjustifiable charges that would otherwise inflate the rate structure. Obviously, the value of this activity extends beyond the specific tariff filings that are ultimately found unjust and unreasonable. Knowledge by the industry that this monitoring program exists certainly has an inhibiting effect on the filing of tariffs which cannot be justified.

I mentioned that one of the items the consumer unit looks for is additional charges for pickup and delivery service at certain points. Both large urban areas as well as remote locations are often the victims of such charges. At issue here are those methods or devices used by carriers to increase their charges for shipments to and from particular points or areas other than straight forward increases in rates per 100 pounds. Three such devices are often employed by carriers: arbitraries, pickup and delivery charges, and surcharges. Each of these varies slightly in definition, but all result in increased rates for service to and from a particular point by the imposition of charges to be added to class rates without an increase in service. It has been the Commission's view that a proposal to establish charges in addition to class rates without an increase in service is absent convincing, well supported, special justification—unlawful. The Commission invariably suspends such proposals.

Whether or not a given proposal constitutes new or reduced rates is a matter of tariff interpretation. Under some circumstances, however, pub-

27. Id. Some figures were compiled by the Bureau of Traffic, Section of Tariffs, from internal reports and records.

28. In Docket No. 36654, Boyle Brothers, Inc., Petition for Clarification, initial decision served January 13, 1978, pending possible action on appeal, the Commission has decided that in the future it will consider that arbitraries, pickup and delivery charges, and surcharges are illegally filed unless they apply in connection with specifically named points, with the publication itself in a tariff that is used to determine class rates. A proposal to establish "delivery charges," for example on all shipments to points in Vermont (by a script clause rather than by reference in connection with the individual points), would be therefore "illegal" and considered for possible rejection. This should more or less eliminate the wholesale application of such charges often called "area arbitraries."

29. Tariff technicalities are significant particularly in the determination of whether or not arbitra-
lication of arbitraries can be clearly determined to be a proposal to establish rates lower than an existing basis.

Unless the proposal appears to be unjust and unreasonable, because of the level of the rates, the Commission generally does not suspend arbitraries that result in genuinely reduced rates, or in rates for application where no current basis of rates exists, simply because of the manner of publication.

When the Commission votes to suspend an arbitrary, a pickup or delivery charge, or a surcharge, it does so because the suspended charge plus the currently existing charge appears above a just and reasonable level.

C. REASONABleness of RATES

Since the Interstate Commerce Act does not define just and reasonable rates, the meaning of these terms must be found in decisions of the Commission and the courts. No precise formula has been devised for determining the reasonableness of a given rate on particular traffic; the question is one of fact which calls for the exercise of the Commission's informed judgment. The courts have acknowledged that the Commission has wide latitude and flexibility in judging the reasonableness of rates.

A reasonable rate is one that falls in the "zone of reasonableness," a concept that originated in the field of rail regulation. Thus, one of the most oft-quoted descriptions of the zone of reasonableness is that of Justice Cardozo in United States v. Chicago, M., St. P. & P. R.R.

A zone of reasonableness exists between maxima and minima within which a carrier is ordinarily free to adjust its charges for itself . . . . We lay to one side cases of discrimination or preference or rivalry so keen as to be a menace to the steady and efficient service called for by the statute . . . . Those tendencies excluded, "a carrier is entitled to initiate rates and, in this connection, to adopt such policy of ratemaking as to it seems best." 30

The zone of reasonableness concept places a check on the Commis-

sion’s regulatory authority. The zone of reasonableness delineates an area where the market forces and the judgment of management rule. It is only when a rate falls outside the zone that the regulatory authority is permitted to interfere with the normal ratemaking process.

The zone of reasonableness cannot be effectively defined in terms of fixed percentage points in a way that will be applicable to all cases. The zone of reasonableness concept, as applied by the Commission, provides the carriers with broad pricing flexibility which may be even more necessary under present economic conditions than in the past. The Commission’s approach has permitted and encouraged the introduction of innovative approaches to ratemaking. While the Commission does have the power to prescribe just and reasonable maximum or minimum rates following a finding that any rate is or would be unlawful, the burden is on the carriers in the first instance to publish their own rates and most go into effect as a matter of course. In order that rate regulation may be responsive to changing economic conditions, the applicable statutory provisions are drafted in general terms. As the Commission stated in the early days of transportation regulation, "[t]he words just and reasonable imply the application of good judgment and fairness, of common sense of justice to a given condition of facts. They are not fixed, unalterable, mathematical terms." ^31

Because of the impracticality of developing a definition of a just and reasonable rate that will fit all situations, the Commission is faced with the task of applying general standards to specific facts. The fundamental principle underlying this function is the protection of the public interest. The term "public interest" in this sense means not only the protection of the public against unreasonable and discriminatory charges but also the interest of the public in the maintenance of an adequate, efficient, and dependable system of transportation.

Although, as previously stated, the determination of the bounds of the zone of reasonableness does not lend itself to mathematical formulas, there are certain indicators of reasonableness which the Commission has employed, including rate comparisons, competitive conditions, and cost of service.

Cost has become an increasingly more significant factor in ratemaking. It used to be said that "value of service"^32 determines the maxima of the zone of reasonableness; cost, the minima; and competition determines the rate to be charged. Increased competition, however, has produced a trend toward cost-oriented pricing. The extent to which the price of a service exceeds its cost is an indicator of whether a rate is too high and exceeds

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31. In re Investigation and Suspension of Advances in Rates for the Transportation of Coal by the Chesapeake & O. R.R., 22 I.C.C. 604, 624 (1912).

32. A rate just below a level that would dry up demand for the service.
the bounds of reasonableness. The Commission’s role in developing improved cost finding is discussed more completely in part IV.

D. ENTRY CONTROL

The Commission has recently given increased attention to the potential of liberalized entry as a means to improve motor carrier regulation. The recent staff task force study completed July 6, 1977, contained 39 recommendations for improvements in the regulation of interstate trucking. The task force’s recommendations covered four broad areas: (1) recommendations involving the application and application proceedings, (2) recommendations directed at facilitating entry by expanding exemptions or easing evidentiary burdens, (3) recommendations which are primarily procedural or are directed at internal Commission operations, and (4) recommendations for further study and analysis including a study of independent truckers and a comprehensive study of motor carrier entry. As of January 31 of this year some action had been taken on 35 of the 39 proposals. Final action on ten of the proposals has resulted in much expedited processing of application proceedings and several legislative proposals. In addition, a number of rulemaking proceedings have been instituted in regard to other proposals to explore their feasibility and to develop standards for their implementation.

One of the task force’s proposals related to the introduction of cost/price evidence in application cases and is probably of particular interest to this subcommittee. In response to the task force’s recommendation the Commission instituted on February 8, Ex Parte No. MC-116, Consideration of Rates in Operating Rights Application Proceedings. Through the proposed rulemaking in Ex Parte MC-116, the Commission intends to develop guidelines for considering rates where the new rates may be the main advantage of the proposed service. The significance of this proceeding can hardly be overemphasized. If rules to implement this concept are adopted, they could profoundly affect price competition in the motor carrier industry.

Another of the task force’s recommendations that warrants specific mention is that which would establish limits on the ability of existing carriers to protest applications for new authority. The rules proposed in this proceeding, Ex Parte No. 55 (Sub-No. 26), Motor Carrier Application Proceedings—Protest Standards, would, if adopted, limit protests to those filed by carriers who had actually hauled the traffic at issue or had actively solicited it.

E. NEW INITIATIVES IN MOTOR CARRIER RATE REGULATION: EX PARTE NO. MC-98 AND OTHER PROCEEDINGS

Numerous and complex disputes between carriers and shippers come before the Commission on a routine daily basis. Rather than resolve recurring disputes on a case by case basis the Commission, when appropriate, utilizes its broad rulemaking powers in an attempt to resolve the national transportation problems which underlie many of these disputes. A recent example is Ex Parte No. MC-98, New Procedures in Motor Carrier Restructuring Proceedings.\(^{36}\) That proceeding concentrated on problems related to small shipments but also examined rate issues common to the motor carrier industry in general. The transportation of small shipments by motor common carriers is a multifaceted problem. On the one hand, shippers maintain that the rates are too high, in some cases even serving as an embargo; on the other, carriers complain that the rates are too low and even noncompensatory. Some shippers contend that small shipments subsidize larger less-than-truckload (LTL) and truckload (TL) traffic while carriers assert that the larger LTL and TL traffic subsidizes small shipments, and that such overpricing of the larger, more desirable LTL and TL traffic subjects this traffic to diversion to private and contract carriage. Shippers maintain that small shipments are "captive" traffic for the motor carrier industry, subject to the whims of an inefficient but very expensive source of transportation. They complain of poor service generally while carriers assert that they are already losing money on this traffic and that providing better service would only result in further losses.

The notice of proposed rulemaking in MC-98 elicited over 60 pleadings representing approximately 70 parties. This provides an indication of the importance of the issues raised and the interest in them.

Many parties expressed dissatisfaction with the present classification system. As we stated in our Notice of Proposed Rulemaking:\(^{37}\)

The present motor carrier LTL rate structure is essentially a copy of the classification-based system developed, and still used, by rail carriers. When regulation was expanded to include motor carriers, it became necessary for the motor carrier industry to publish a rate system of its own. That was done by adopting the rail classification and superimposing the principles underlying that system upon the motor carrier industry. The various individual rate bureaus developed a number of systems for differentiating between the relative transportability of different commodities.\(^{38}\) At the time, this worked to the advantage of the motor carriers because value of service factors, inherently part of the classification of high value goods, allowed them to attract the most prof-


\(^{38}\) The National Motor Freight Classification generally applies nationally for motor carriers except for within New England. The Coordinated Classification is the motor classification utilized within New England.
itable portion of the LTL traffic from the rails by a skillful matching of rates and service.

A freight classification is a division of groups of the commodities transported by common carriers according to their transportation characteristics in order to assure that all bear a fair share of the transportation burden. Thus, the primary purpose of a freight classification is to assign each article, or a group of articles, to a class according to well-known classification principles which recognize distinctions between the articles from a transportation standpoint, along fairly broad lines.

Characteristics of the commodities which are considered in fixing classification ratings are: shipping weight per cubic foot, liability to damage other commodities with which it is transported, perishability, liability to spontaneous combustion or explosion, susceptibility to theft, value per pound in comparison with other articles, ease or difficulty in loading or unloading, stowability, excessive weight, excessive length, care or attention necessary in loading and transporting, trade conditions, value of service, and competition with other commodities transported. The importance of each of these classification elements varies with each commodity or group of commodities with similar transportation characteristics. The classification of property into groups designed to spread the burden of transportation fairly has never been successfully reduced to formula.39

The pleadings revealed a widespread dissatisfaction with the present classification system. Although the rate bureaus defended the system, many shippers and individual carriers strongly criticized it.

A nationwide uniform system of classification of articles transported by rail became effective in 1952 pursuant to Docket No. 28300, Class Rate Investigation, 1939.40 In that proceeding we prescribed a scale of class 100 rates upon which rates for all other classes would be based. A similar system was subsequently adopted by motor carriers. Those articles the transportation of which cost more or less than the cost attributed to class 100 articles were given a separate classification representing a percentage of the class 100 rate. Thus, a shipment of a commodity classified at 35 was transported at 35 percent of the class 100 rate, while a shipment classified at 125 was transported at 125 percent of the class 100 rate. In recent years, the motor carrier industry has departed from that system primarily as a result of general increases and the periodic imposition of weight brackets. Classification, as it was originally conceived, has become distorted, resulting in the anomaly of having a multiplicity of classes for any particular commodity. Articles taking the same class truckload regularly take widely

varying classes less-than-truckload with no apparent justification for such differences.

There was not enough evidence in the record in MC-98 for us to determine fully how the present system can be best improved, whether a modification of a density based system modeled after the Coordinated Classification should be adopted nationally, or whether the entire system should be abandoned and a totally new system designed. We therefore found that an investigation into the classification system is warranted, and it will soon be initiated.

In MC-98 numerous shippers expressed dissatisfaction with the quality and quantity of the small shipments service provided by motor common carriers.

In 1967 an Ad Hoc Committee of the Interstate Commerce Commission conducted a study of the small shipments problem.\footnote{Report of the Ad Hoc Committee of the I.C.C. Composed of Commissioners Murphy, Wolrath and Brown, Small Shipments Problem (Nov. 30, 1967).} The study was conducted primarily by making a number of investigations of a selected number of service failures. In this respect the shippers involved attended meetings with one or more members of the Committee and fully explained the problems which they faced. Thereafter the carriers named by the shippers were contacted and again either individually or in groups explained the circumstances which surrounded specific service failures.

Another phase of the investigation involved conferences with a number of shipper groups and various organizations of carriers. At these meetings rather than discussing specific occurrences, each group discussed the situation in general, presenting their needs, problems, and opinions of possible solutions to service failures. Other information gathering was accomplished through the receipt of letters from individual shippers and carriers. Data was obtained from information and reports received from both the headquarters and field staffs of the Commission.

Presentations before the Committee indicated that shippers find three major faults with the services of motor common carriers on small shipments: (1) carriers selected the commodity they desire to transport because of its physical characteristics, (2) carriers select shipments on the basis of the volume tendered, and (3) carriers are unable or unwilling to interline in certain circumstances, thereby preventing the through movement of a shipment. Another common complaint is the inability to obtain service from or to small cities or areas not generating large amounts of backhaul traffic.

The practice of selecting and choosing traffic is, of course, a direct violation of a carrier’s obligation to transport, without discrimination, all traffic covered by its certificates and tariffs. The justification usually given by a
carrier for its refusal to accept less desirable traffic is that its facilities are overloaded and that the article tendered for transportation might be damaged if held over until a slack period is reached. Carriers ascribe this refusal to accept what they consider to be the less desirable traffic as being simply a matter of good business judgment.

Although it would seem that a carrier could be easily and quickly enjoined from violating the terms of its tariffs, the situation is not susceptible to a simple remedy because of the reluctance of shippers to take direct enforcement action. The position of shippers is understandable, particularly in the case of joint-line traffic where the institution of an enforcement action may result in action by the involved carriers to cancel the joint arrangement. In some instances a complete loss of through service may result.

It is settled that a carrier may not limit services offered in its tariff to something less than that which it is certified to handle.\(^4^2\) A carrier failing to comply with its published tariff authority and refusing to render service is subject to serious sanctions by the Commission. Accordingly, carriers have been ordered to delete from their tariffs provisions restricting service to less than a carrier’s full operating authority.\(^4^3\)

A carrier or any party acquiring the operating rights of another carrier, whether by consolidation, merger, or sale, also acquires all the rights and all the obligations of the second carrier. Failure to provide the full certified service subjects the acquiring carrier to sanctions. Thus, a carrier not complying with its service obligation may have its certificate suspended or revoked, may be subjected to an order to cease and desist, may have an injunction imposed against it, or may be criminally prosecuted. Failure to meet service obligations is grounds for refusal of an application for a new grant of authority, for acquisition of existing authority via sale, merger, or consolidation, and in denying rate increases.

In spite of general complaints there is some evidence that service levels, on the whole, are adequate. For example, the “hot-line” instituted by the National Small Shipments Traffic Conference was abandoned for lack of genuine service complaints. Also a Department of Transportation study dated December 1975, “Industrial Shipper Survey (Plant Level),” indicated that overall quality of service on small shipments transported by motor carriers is adequate or more than adequate on 98 percent of the

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42. Ex Parte No. MC-77, Restrictions on Service by Motor Common Carrier, 111 M.C.C. 151 (1970). As a result of that proceeding we amended 49 C.F.R. by adding thereto § 1307.27 (k) (i) which reads in part as follows: "No provision may be published in tariffs, supplements, or service to less than the carrier's full operating authority or which exceed such authority. Tariff publications containing such provisions are subject to rejection or suspension for investigation."

shipments. In our report, we stressed that the individual carrier which is
guilty of abusing its certificate is liable to prosecution, to being refused per-
mission to sell, consolidate or merge, or being denied a rate increase.
However, the shipping public was encouraged to come forward with spe-
cific complaints and participate in formal proceedings where evidence of a
carrier's failure to meet its obligations will have an impact.

Many parties to the proceeding in MC-98 criticized motor carrier oper-
ations as inefficient. We noted that studies to increase productivity are be-
ing conducted and that innovative programs are continually being instituted
in an attempt to further improve motor carrier service, and we encouraged
carriers and shippers to continue to investigate means of expediting the
handling of freight and decreasing the costs of providing service.

We intend to study the matter further and consider whether additional
proceedings are necessary.

The efficiency of carrier operations is of major concern to us because
the Commission, in prescribing just and reasonable rates, is required by
section 216(i) of the Act to give due consideration to among other factors:
the need, in the public interest, of adequate and efficient transportation
service by such carriers at the lowest cost consistent with the furnishing of
such service; and to the need of revenues sufficient to enable such carriers,
under honest, economical, and efficient management, to provide such serv-

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ice. Carriers have an obligation to reduce expenses by the exercise of better
management.46

Thus, we believe that carriers have an obligation to present evidence
showing what efforts are being made to offset increased costs by greater
efficiency, and we also believe that this area needs to be emphasized in
rate proceedings involving small shipments. Accordingly, as a result of MC-
98 we now specifically require carriers to submit a brief summary of what
steps have been taken, within the year preceding the time of filing for a rate
increase to reduce their costs on small shipments to the extent such costs
can be reduced.

The information submitted will be considered in determining the merits
of a general increase proposal. If it becomes apparent that insufficient
steps are being taken to deal with this problem, then further action on our
part may become necessary.

44. OFFICE OF TRANSPORTATION PLANNING ANALYSIS, INDUSTRIAL SHIPPER SURVEY (PLANT LEVEL)
(September 1975).
46. Increased LTL, AQ, and TL Rates, To, From, and Between New Eng. Terr., 329 I.C.C. 244, 521 (1966);
Freight Forwarder General Increase, Transcontinental Terr., 326 I.C.C. 216 (1966); Increased Rates Within Southwest, and Between Colo. and Wyo. and Southwest, 326 I.C.C. 216 (1966); LTC Class Rates and Minimum Charges Between Midwest and Central Terr.,
One of the major innovations in MC-98 is our advocacy of a small shipments tariff.

We believe the establishment of a small shipments tariff to apply to shipments under 500 pounds will encourage rate bureaus and carriers to file such tariffs as well as assist in their drafting. The creation of a small shipments tariff is essential to improving the competitive position of motor common carriers. The publication of these tariffs should bring rates more in line with the cost of service and insert a flexibility into the system designed to cater to the needs of the shipping public.

To assist the carriers in drafting such tariffs we set forth a number of features which we believe should be contained in any small shipments tariff. First, small shipments tariffs must provide separate rates for pickup, and line-haul service.

Pickup and delivery service consists of calling for and collecting freight and receipting therefor from a dock, platform, doorway, or other facility directly accessible to highway vehicles. In the case of LTL shipments this service generally is performed in connection with transportation from or to the premises of the motor carrier’s terminal. A motor carrier may perform its own pickup and delivery service, and loading and unloading service, or it may arrange to have it performed by another.

Pickup and delivery constitute a substantial portion of the carrier’s expense.

Some shippers of small shipments contended that both shipper and carrier costs can be reduced if shippers and consignees have the option of declining pickup and delivery services, and are willing and able to do their own pickup and delivery. However, the evidence also indicated that many of these shippers and receivers do not presently perform these functions simply because the economic incentive to do so is inadequate.

The Commission wishes to encourage tariffs which provide shippers with an adequate economic incentive to perform these services themselves, if they are so equipped. Such incentives, to be just and reasonable, must be cost based.

In an attempt to accommodate shippers and receivers willing and able to pickup and/or deliver to or from terminals, without penalizing shippers and receivers unable to perform the service themselves, we took two steps in MC-98. First, where allowances are published based on carrier cost we required them to increase whenever there is a rate increase, inasmuch as the cost of pickup and delivery also increases. It is unjust and unreasonable not to give the shippers an allowance which is a true reflection of costs.

The law is well settled that shippers which deliver their own goods to a carrier’s loading station or terminal, in lieu of using the available pickup service of the carrier, are entitled to compensation reasonably commensu-
rate with the facilities furnished and the services performed.\textsuperscript{47} The owners of
the property are rendering a service in connection with the transportation
for which they are entitled to a just and reasonable allowance under section
225. An allowance in excess of or far below the shipper’s cost would be
unjust and unreasonable.\textsuperscript{48}

Second, in instances where allowances are not published we will re-
quire tariffs setting forth special rates for small shipments to establish two
sets of rates: one for pickup and one for line-haul and delivery. Pickup is to
be performed at the option of the shipper, the carriers are not relieved from
their duty to provide this service. Such a breakout in charges will allow the
carrier to tie the charge more closely to the cost of service. For example,
the rate for pickup will reflect whether the service is to be performed in a
high cost or low cost area. Although many consignees would like the op-
tion to perform their own delivery, it is not practical at this time as it may
overtax the carriers’ terminal facilities which are not designed as ware-
houses and may subject articles which are stored for consignees to greater
risk of loss or damage.

An aggregate or multiple tender rate is an incentive rate given to the
shipper upon tendering several shipments to the carrier at one time. These
rates are intended to encourage fewer pickup trips thereby decreasing car-
rier expenses. MC-98 encourages carriers to publish and shippers to use
these rates, and the small shipments tariff endorsed contains provisions for
aggregate tender rates.

As stated earlier pickup and delivery costs are a substantial portion of
a carrier’s expense, especially with regard to small shipments. A primary
element of this cost is the expense of time required for the vehicle to go
from the terminal to the shipper’s dock and back again. Travel time is the
same, regardless of the number of shipments tendered or their size. Cost
differentials do not appear until the carrier actually handles the shipments
and the cost is proportionately greater for smaller shipments. It is only logi-
cal that if a carrier can pick up two or more small shipments at one time
rather than making a trip for each, its expenses will be reduced.

The Commission and the courts have held that reduced rates based on
the ability of a shipper to tender large or aggregate shipments are not dis-

\textsuperscript{47} See United States v. Baltimore & O.R. Co., 231 U.S. 274 (1913); Pickup and Delivery
Allowance at St. Louis and Kansas City, 64 M.C.C. 163, 165 (1955).

\textsuperscript{48} New York Central R.R. v. United States, 199 F. Supp. 955 (S.D.N.Y. 1961); Automobile
Parts and Other Articles Within Central Terr., 316 I.C.C. 143, 145 (1962).

1967), dismissed as moot, 345 F. Supp. 1389 (D. Del. 1972); Aggregate Class Rates, between
Points in the South, Midwest and East, 332 I.C.C. 524 (1968); Aggregate Rates, Rochester, N.Y.,
to Eastern, Central, and Southern States, 325 I.C.C. 474 (1965); Iron Ore from Cleveland, Ohio, to
Ohio and Pennsylvania, 323 I.C.C. 746 (1965); Multiple Shipments from California to Oregon and
ences in the cost of handling single versus aggregated shipments, and that these differences justify differences in rates.

The pleadings restated that shippers often require a carrier to pickup or deliver small shipments daily. Some small shippers do not have large warehousing facilities, and because there is no incentive to withhold today’s shipment until tomorrow, they require the carriers to make two trips instead of one. We believe that if shippers are given adequate incentive, they will aggregate their shipments.

In addition to provisions for separate pickup charges and aggregate tender rates, MC-98 provides that small shipments tariffs may, at the option of the carrier, contain provisions relating to discounts for prepayment and prepaid shipments. We believe such tariff offerings will improve the carriers’ competitive position on this traffic and we hope carriers will take advantage of this opportunity.

The Commission believes the publication of small shipments tariffs by interested carriers will improve competition among them. However, there are other ways competition and lower rates may be achieved. One of the methods we are studying is released rates. Under released rates a carrier is subject to limited liability. In exchange for a lower rate, shippers “release” the carrier from liability in excess of a certain amount per pound. This system is reputed to benefit the shipper of less valuable commodities. Shippers of commodities of greater value have three choices: (1) they may not release and pay the normal (and higher) rate for the carrier’s common law absolute liability; (2) they may release, pay a lower rate and purchase insurance independently; or (3) they may release, pay a lower rate and take the risk and absorb any losses, i.e., self-insure. As a practical matter, the last two options are available only to larger shippers. Small shippers may have difficulty in contracting for this type of insurance or in absorbing the losses, and accordingly may be forced to pay the higher rate.

The value of a commodity transported is an element in ratemaking aside from the risk of loss or damage, because it serves to measure the value of service rendered the shipper. But where rates based on declared or agreed value have been authorized by us, the statute accords shippers the right to understake the value for the purpose of securing a lower rate, and it is clear that if the excess of the unreleased over the released rates is more than the cost of insurance, shippers will ordinarily release the carrier and obtain transit insurance elsewhere. But frequently transit insurance can not be obtained. When it is not available, those shippers who are financially able to do so will assume the risk of loss themselves. The small shipper is less apt to be able to do so and will be compelled to resort to the higher, full

value rate for adequate protection. The alternative rates which would result from the carriers' proposals will thus not work with equal justice to all.

Section 20(11) of the Act\textsuperscript{50} restates the common law rules that a common carrier is ordinarily an insurer against loss, damage, or injury to property committed to it for transportation, and declares any limitation of liability or recovery to be unlawful and void. However, this section gives the Commission authority to grant partial exemption from full liability in cases where rates depending upon, and varying with, declared or agreed value would, in our judgment, be just and reasonable under the circumstances.

The purpose of maintaining released-value rates is to accord a shipper the choice of two different rates. Under the higher rate unlimited carrier liability attaches and under the lower the shipper, in consideration for the reduced rate, declares or agrees that in the event of loss or damage the value of the shipment is a sum certain. When such an agreement is made at the time of shipment, the shipper is bound by his declaration and is estopped from claiming or recovering more than the value stated in case of loss or damage.

In the past, before authorizing partial exemption from full liability, we have required a showing that traffic is highly susceptible to loss or damage, and that the commodities involved have a wide range of values making the amount of any claim that may arise difficult to estimate.\textsuperscript{51}

The criteria for gaining released rates are: (1) a wide range in value of the commodity making the amount of any claim that may arise difficult to estimate; (2) comparatively high susceptibility of the traffic to loss or damage; (3) a high ratio of claims to freight charges; and (4) a great number and frequency of claims for loss and damage. Other factors have been (5) difficulty of a carrier in obtaining adequate insurance coverage; (6) unreasonably high cost of insurance; and (7) competitive necessity.

The parties have indicated that the major problem with small shipments service is that rates are too high. Many parties have stated that if rates were lower they would find general commodities carriers' service more attractive than available alternatives. One way in which lower rates may be offered is to limit carrier liability. The Commission indicated it lacked sufficient data to authorize blanket released rates for all shipments under 500 pounds based upon the record in Ex Parte No. MC-98. The Commission indicated it was taking two steps to obtain the necessary information. First, we are taking a survey of shippers. The survey is designed to determine shipper attitudes toward released rates and to gauge shippers' present use of released rates, use of transportation alternatives for small


\textsuperscript{51} Released Ratings on Rates on Engines, 47 M.C.C. 767 (1948); Wearing Apparel, Accessories, Piece Goods—Shulman, Inc., 321 I.C.C. 1 (1963).
shipments, and ease or difficulty with settling claims problems. Second, we are instituting a rulemaking on released rates. The purpose of the rulemaking is to determine the desirability of released rates for shipments weighing 500 pounds and under in connection with a small shipments tariff, and if desirable, what form they should take.

In Ex Parte No. MC-98 we received a great number of comments from shippers which find it difficult to schedule pickup and deliveries. This results in unnecessary congestion part of the day and empty docks the rest of the day. Our analysis of this matter led us to conclude that both shippers and carriers could benefit from scheduling and that carrier failure to attempt to accommodate shippers in this regard may indicate lack of competition in any proceeding where competition is in issue, such as rate disputes, operating authority applications, or sales and mergers of existing trucking operations.

Problems associated with rates on small shipments can also be reduced, we determined, by channelling this traffic to trucking operations geared to it. Whether this is done by carriers that specialize in small shipments, or by carriers that dedicate a division to this traffic is immaterial. What is needed, it was concluded, is expertise, as well as specialized facilities to make the handling of this traffic more cost effective. Thus, in MC-98 we encouraged carriers to specialize in small shipments and we stated that as a matter of policy we will issue certificates of public convenience and necessity to those who seek to specialize in small shipment traffic.

Recent years have witnessed efforts by motor common carriers to select the traffic they handle through self-imposed service limitations in their tariffs as well as other means. Following is a brief discussion of a number of proceedings, recent or current, where the Commission has acted to provide that the service held out to the shipping public by the regulated carriers conforms in letter and spirit of what is intended by the Interstate Commerce Act.

Over the years the Commission's Bureau of Traffic, Section of Rates and Informal Cases, received hundreds of complaints against carriers, particularly motor common carriers of property, regarding their practice of handling overcharge claims. In many instances the carriers did not timely acknowledge such claims, and in some instances never acknowledged them. The Commission has instituted Ex Parte No. 342, Procedures Governing the Processing, Investigation and Disposition of Overcharge, Duplicate Payment, or Overcollection Claims, to establish rules for the timely handling and processing of these claims. The proceeding is pending, and it is anticipated that it will be decided next month.

52. 359 I.C.C. 211 (1978).
Duplicate payments have been the subject of recent vigorous enforcement action by the Commission's Bureau of Investigations and Enforcement. Last November the ICC brought a court action against 23 Midwest truckers for withholding more than $4.5 million in duplicate payment from shippers.\footnote{53} And this is just the beginning; we have reason to believe that this practice is widespread, and we intend to see that it is stopped. I am happy to report to you that our court actions are proceeding well. To date, the Commission has secured court orders against 14 of the 23 defendant companies wherein the trucking companies have been ordered to make refunds of duplicate payments made to them and hereafter to implement plans to identify and refund duplicate payments. The Commission estimates that the successful conclusion of these 14 court actions should lead to refunds of up to two million dollars to shippers and consumers. Indeed, by these actions the Commission seeks to protect shippers who have lost their capital and consumers who ultimately share in the double payments through higher prices for merchandise.

In the early 1960's motor common carriers began publishing tariff provisions which provided for the application of additional charges on shipments picked up at or delivered to private residences, schools, churches and similar type locations. From that time on, the practice spread nationwide and virtually all carriers published these charges. As a result the Commission's Bureau of Traffic, Section of Rates and Informal Cases, received numerous complaints alleging that the charges were unjust and unreasonable. In response, the Commission, on its own motion, instituted Ex Parte No. MC-97,\textit{ Investigation into the Practices of Motor Common Carriers of Property on Residential and Redelivered Shipments},\footnote{54} which resulted in residential delivery charges being prohibited and an order requiring carriers and their tariff publishing agents to cancel any such provisions outstanding. The rationale of the Commission decision is that all classes of shippers and receivers should be treated equally. The Commission's decision was ultimately upheld by the U.S. Court of Appeals. As a result of our action, small consumer's transportation costs were reduced by substantial amounts.

Practices of the household goods moving industry have presented a particular challenge. Post-World War II American society became highly mobile. These trends have created a great demand for household goods moving service and a concomitant concern as to its quality.

The unique, personal nature of household goods moving service has been recognized by the Commission. Shippers of household goods expect

\footnote{53. Court action was brought against each individual trucker. The figure of $4.5 million was arrived at by adding amounts from individual actions. \textit{See ICC News, Release 235-77, November 3, 1977. It describes how the ICC went into federal court against 12 companies for illegally retaining 2.3 million dollars.}}

\footnote{54. 353 I.C.C. 689 (1977).}
good service when moving their personal possessions to a new home and
the motor carrier industry has, as it should, encouraged the public to enter-
tain this confidence.\textsuperscript{55} The fact that the industry has not always justified
that confidence has resulted in a very active role by the Commission with
regard to household goods carriers.

The Commission undertook corrective actions in a series of proceed-
ings under Ex Parte No. MC-19,\textsuperscript{56} from the early 1960's to the present. In
these proceedings the Commission has adopted new and amended rules to
govern the practices of household goods carriers intended to assist the
shipping public in obtaining more efficient and expeditious movement of his
or her possessions. Because the user of household goods services is often
an infrequent shipper, new rules were adopted to enable the individual con-
sumer to select rationally from among the various carriers and to know what
he or she has a right to expect from the carrier in terms of performance.
Performance reports are now required of carriers by the Commission and
the carrier must give the prospective customer a copy of its report along
with a pamphlet, published by the Commission, setting out the obligations
of the carrier and giving general guidance on what the shipper should do to
insure a successful move. Further, the Commission, through its field of-
fices, offers its assistance to the shipper in securing remedial action by the
carrier should the move go awry.

The household goods moving industry is a prime example of an area
where increased and continual regulatory activity is especially required.
New problems are always arising and old problems often take new forms. I
believe the Commission has exercised the sort of vigilance required by the
unique nature of the household goods moving service for the public through
its oversight of the industry's practices and contribution to improved con-
sumer awareness of what the act requires of the carriers.

The Commission has recognized that some carriers may attempt from
time to time to restrict the availability of their services. Efforts to restrict
services are accomplished by tariff publications and are designed to elimi-
nate less profitable traffic or avoid doing business with particular clients and
connecting carriers. These service restrictions to say the least are generally
contrary to the common carrier obligation to serve the public.

Motor carrier tariffs\textsuperscript{57} define what services a carrier holds itself out to
the public to perform and the rates at which these services are available.
The foundation of these tariffs is the carrier's certificate of public conven-
ience and necessity. Carriers enjoy a degree of freedom to adjust their tar-

\textsuperscript{55} 96 M.C.C. 196 (1964).
\textsuperscript{56} Ex Parte No. MC-19 (Sub-No. 33), Practices of Motor Common Carriers of Household
\textsuperscript{57} The term "tariffs" is synonymous with the term "schedules," as used in the Interstate
Commerce Act.
iff at their own discretion, subject to the statutory requirements that changes be effected on at least 30-days' notice and subject to possible investigation and suspension by the Commission. Tariffs and tariff modifications must be filed with the Commission and in the manner prescribed in the Commission's regulations. These regulations are part of the Code of Federal Regulations. Tariff publications forwarded to the Commission for filing but not conforming with the regulations may be rejected.

In its efforts to preclude unwarranted service restrictions, the Commission has by rulemaking established a regulation requiring a carrier's tariffs to embrace the full scope of its operating authority. The rulemaking proceeding was docketed as Ex Parte No. MC-77, Restrictions on Service by Motor Common Carriers, and was concluded in 1970. The regulation makes clear that publications attempting to limit or withhold service will be subject to rejection or suspension. In a subsequent rulemaking proceeding, Ex Parte No. MC-77 (Sub-No. 1), the Commission identified and analyzed the lawfulness of specific, recurrent restrictions. The interpretations set forth in this subsequent proceeding are the guidelines for reviewing tariff publications and rejecting those which create unwarranted restrictions. The guidelines reach both direct and indirect restrictions. An indirect restriction would be a tariff provision which removes the applicability of single-factor through rates for the unfavored traffic, leaving a higher combination of local rates. Although service would be available under the restrictions, the rate levels are so high as to constitute an effective barrier to the movement of the traffic.

Examples of prohibited restrictions are provisions which embargo or which preclude the applicability of single-factor through rates on:

- shipments not delivered by the publishing carrier
- shipments of a particular named commodity
- less-than-truckload shipments
- shipments not meeting unrealistic minimum weight requirements
- shipments not meeting unrealistic packaging requirements

Additionally, the Commission has directed carriers to eliminate tariff provisions which prevent the applicability of class-rates on through movements involving three or fewer carriers.60

58. 49 C.F.R. § 1307. 27(k) (1977).
59. This proceeding was entitled Restrictions on Service by Motor Carriers (Compliance Reports and Interpretations), 119 M.C.C. 691 (1974), 126 M.C.C. 303 (1977), aff'd, Eastern Central Motor Carriers Ass'n, Inc. v. Interstate Commerce Commission, 571 F.2d 784 (4th Cir. 1978).
60. The Commission does not have the power to force motor carriers of property to enter into through routes and joint rates although it has sought legislation authorizing it to do so. The Commission believes that joint rates and through routes are desirable because they make more service available to the shipping public at a lower rate. Thus, the Commission discourages carrier actions that adversely affect through routes and joint rates, as is exemplified in this aspect of the decision in Ex Parte No. MC-77 (Sub-No. 1).
These guidelines and prohibitions are intended to assure the availability of a nationwide system of motor common carriers at reasonable rate levels. In Fiscal Year 1977 the Commission’s Bureau of Traffic rejected 83 publications as contrary to the Commission’s MC-77 regulations. An additional 22 publications were suspended and placed under investigation.

Loss and damage claims are a national transportation problem. The Commission is convinced that a critical part of solving this problem is the creation of an expeditious method of adjudicating these claims. Loss and damage claims are often ignored or unfairly declined, and, for the small shipper especially, the cost of litigation often surpasses the amount of the claims. However, the Commission’s successive requests for legislation granting it jurisdiction to adjudicate these claims have not been acted on.

Nonetheless, within the limits of its current Congressional mandate, the Commission is doing what it can to improve loss and damage claims settlement. For example, in Petition to Institute Proceeding to Amend CFR 1051.1(b), 61 we found it necessary and therefore now require "either the address where remittance must be made or the address of the principal place of business of the issuer of the freight to expense bill, or both, at the issuers option," on the freight or expense bill. Prior to institution of this rule shippers often had difficulty in placing loss and damage claims with the carrier responsible for handling the claim within the statutory period of limitations because of the difficulty in ascertaining the proper address. We believe this rule will somewhat facilitate settlement of claims.

IV. COST FINDING AND EVALUATION OF REVENUE NEED APPLICATION IN GENERAL INCREASES AND SPECIFIC RATE ADJUSTMENTS

A. COST FINDING: AN OVERVIEW

In 1935, when motor carriers engaged in interstate and foreign commerce were brought under the jurisdiction of the Interstate Commerce Commission, the carriers were, for the most part, small and unfamiliar with the intricacies of ratemaking. They displayed little interest in or knowledge of cost finding. Instead, they found it easier to ascertain the established rate of the railroads and adjust them to fit their circumstances. If traffic could more readily be handled by the motor carriers, it was possible to maintain rates at the rail level or slightly higher than the rail rate. If it was found necessary to reduce the rates in order to attract the traffic, that was done. As competition grew in the motor carrier field and the nationwide depression intensified, the rate structure become depressed. Consequently, it became apparent that the method of ratemaking then followed was no longer

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adequate. Of necessity, greater emphasis had to be placed on the cost of performing the service.

In response to a clear need to find a firm starting point for judging the reasonableness of rates, the Commission formally organized the Section of Cost Finding in 1939. The principal function of the Section at that time was to develop cost finding procedures for determining the cost of transporting freight by various modes of transportation. The development of costs was not instantaneous, for transportation industries offer a multitude of services and the task of costing each one is a complex undertaking.

Under regulations, a uniform system of accounting and reporting to the Commission was first required for the motor carriers.\textsuperscript{62} This provided data for use in determining the carriers' over all financial stability and revenue need, but it did not provide the necessary information for determining the cost for particular segments or specific movements of traffic. Before data could be developed to satisfy this more specific need, principles had to be developed to allow the segregation and treatment of variable costs, joint costs, and constant costs, and also to weigh the economic significance attached to each. Indeed, there is no easy way of costing individual shipments of different weights and sizes moving over a wide range of distances, and which are transported by vehicles and men involved in performing special services for many commodities at the same time. If you see a truck traveling down the road, it may be loaded with 100 different shipments of different weights. To determine why one of those shipments may cost more per hundred pounds than another when they are all handled in one operation as indicated by the movement of the vehicle, is no easy task. Yet, clearly, no one would dispute that different costs apply to different weight and size shipments, moving different distances.

While the problem of determining costs for ratemaking purposes was difficult, it was not unsurmountable. The first study of note which set forth cost finding methods and principles was published in 1943.\textsuperscript{63} This study presented information on rail freight service costs in the various rate territories of the United States. By 1948, procedures for determining costs were well established by the Commission's section of cost finding. Several cost formulas had been developed, and unit costs for both rail and motor were being published each year. Costs developed from these formulas were and still are widely used by the Commission and the industry in determining the reasonableness of rates.

The term "study" appears frequently throughout this testimony. As we use it, "study" may be broad or narrow in its connotation depending on the


project to which it applies. Thus, a traffic study is essentially the collection and enumeration of a quantity of data sufficient to portray the characteristics of a particular block or segment of traffic handled by a carrier or group of carriers. A cost study may be the production of regional unit costs through the application of Highway Form A to the expenses and statistics of a regional group of carriers. A cost study may also be the application of unit costs to traffic study data and matching the results with the associated revenues by traffic segment.

Highway Form A and Highway Form B are two of the cost finding formulas developed by the Commission's Cost Finding Section.\(^{64}\) Highway Form A, *Formula for Determination of Costs of Motor Carrier of Property*, is an 87-page document that separates motor carrier operating expenses, rents, and taxes, excluding income taxes, among four basic functions: line-haul, pickup and delivery, terminal platform, and billing and collecting.\(^{65}\) It also provides for the determination and distribution of the "cost of capital." After assignment to functions, the expenses are related to service units and unit costs developed. Service units used in these calculations include vehicle-miles, hundredweights involved in pickup and delivery service, hundredweights handled over the platform, and shipments billed.

The expenses and certain statistics used in the formula are obtained from annual reports filed by the Commission by Class I and Class II motor common carriers of general freight. The formula is designed to accommodate the expenses and statistics of carriers which derive an average of 75 percent or more of their revenues from the intercity transportation of general commodities and which have averaged annual gross revenues of $500,000 or more.\(^{66}\) Carriers whose operations meet these criteria are required to separate certain of their major accounts between line-haul and pickup and delivery work and to report certain supplemental statistics.

In applying Highway Form A, annual report data is supplemented by special study information furnished by the carriers as follows:

1. Form 2, traffic analysis, provides percentages for distributing annual shipments and pounds to types of movement and to weight brackets in Highway Form A.
2. Form 4, pickup and delivery study time, provides time and motion factors for distributing pickup and delivery costs to various weight shipments receiving pickup and delivery service.
3. Form 7, line-haul trip report study, provides data for computing the round-trip load factor (average load) by length of haul separately for four major weight groups and for all weight groups combined.

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\(^{65}\) Id.

\(^{66}\) Id.
(4) Form 10, platform study, determines the extent to which shipments for various weights are handled over the carriers' terminal platforms.

(5) Form 11, analysis of peddle-trip operations, provide annual information for use in separating peddle operations between the pickup and delivery portion and the line-haul portion of the trips.

(6) Field reports provide additional accounting information to supplement the accounting and statistical data shown in the carriers' annual reports to the Commission.

As in any system of measurement, the accuracy of the results of our cost studies depends on the integrity of the data fed into them. In this regard, our field audit program plays a twofold role. First, the regular carrier audit insures that the carriers' books of account and other records are correct, uniform and maintained in accordance with Commission-prescribed requirements. In addition, for carriers participating in a regional study, the auditors review their compliance with the special study requirements and assist in resolving any problems which may arise. Headquarters staff thoroughly screen annual, quarterly and special study reports filed with the Commission. Wherever possible, data cells are reviewed and matched against other comparable data for reasonableness and accuracy. As necessary, carriers are requested to verify and/or correct data cells which look questionable. Our data capture system uses internal checks to insure the accuracy of the transfer of data from hard copy reports to the computer. As a result, we have the utmost confidence in the costs published in our regional studies and the results of properly applied Highway Form B's.

Highway Form A is a complex formula and it soon became evident that few, if any, motor carriers could apply the formula, which requires many special and costly studies that must be processed through numerous schedules, forms, and summaries. The problem, therefore, was how to develop specific costs for an individual motor carrier or group of motor carriers involved in supporting rates on traffic movements which do not fit into the general rate structure. Stated differently, traffic hauls which only involve a particular carrier or a small group of carriers may accrue costs that differ from regional average costs. The Commission requires that costs for determining reasonable rates should, to the greatest extent possible, reflect the cost of the carrier or carriers participating in the traffic.\textsuperscript{67} This means that individual carrier costs should be developed to estimate the costs applicable to the given traffic.

The Commission's Section of Cost and Valuation developed a cost formula, Highway Form B. Simplified Procedure for Determining Cost of Handling Freight by Motor Carriers,\textsuperscript{68} whereby a carrier or group of carriers

\textsuperscript{67} Id. at 305.
\textsuperscript{68} Id. at 338, 424.
could develop specific costs applicable to their own operations, as opposed to those average costs developed on a regional or territorial basis.

Highway Form B provides a simplified or shortened procedure so that carriers can readily develop unit costs by services and therefore the costs for specific hauls, without the necessity of making the extensive "special studies" which are required as a part of the more refined Highway Form A used to develop regional or territorial costs. In lieu of these "special studies," the allocation of costs among various sizes of shipments in Highway Form B is achieved by applying cost relationships, developed through the application of Highway Form A, to the average cost for all shipments. Highway Form B procedures provide the means for developing terminal costs at origin, destination and interchange points; adjustment for partial pickup and delivery service at origin and destination; computation of pickup and delivery costs applicable to either a cargo or equipment interchange; adjustment of system average load for length of haul; and adjustment to terminal and linehaul cost to give effect to the density (pounds per cubic foot) of the commodity.

When used properly, Highway Form B can be a useful tool for management because it provides carriers with support for rate proposals, for controlling costs, and for setting future budget estimates. Highway Form B is also used by shippers, competing carriers and other interested parties in protesting rate proposals.

B. COST LEVELS

Whether it be Highway Form A or Highway Form B, the products of these formulas are "service unit costs" which, in essence, have been divided between those which are long run variable and those which are constant. The long run variable costs are computed at "90 percent variable," i.e., 90 percent of the carriers' operating expenses and cost of capital (debt and equity) are considered as being directly variable with output—with the remaining 10 percent being, relatively speaking, constant.69

Standing alone, however, these service unit costs have no effect, and it is only when they are "applied" to assumed or known transportation movements, of different characteristics, that they have meaning and use. The so-called application of these service unit costs, including the various adjustments that may be possible, to "cost out" any given traffic can provide costs at various levels.

Generally speaking, there are three levels of motor carrier costs which, under various circumstances, are helpful in analyzing and testing the compensatory character of a rate. All three provide the complete cost picture, and all three are necessary on occasion to explain motor carrier rates. (1)

69. Id.
The first and lowest cost level consists of those one-way variable expenses which are separable from the joint expenses incurred in the round-trip movement of the equipment. (2) The second level of cost includes the (variable) expenses applicable to the operation as a whole. It embraces those joint expenses such as the round-trip movement of the equipment, which, while of a joint character for an individual segment of the motor carriers' operations, are viewed as a whole. (3) The third level of cost consists of the so-called fully allocated costs which are made up of the (variable) costs plus an apportionment of the constant expenses.

C. **Regional Average Costs**

To fill the need for regional and territorial motor carrier costs the Commission's Section of Cost and Valuation has published a series of studies which provide territorial unit costs, cost scales, and performance factors based on data of motor common carriers of general commodities operating principally within 13 specified regions or territories.\(^{70}\)

These studies represent territorial average costs, *i.e.*, they are based on a large group of carriers treated as if they were one large carrier, and are derived from Highway Form A. We attempt to make cost studies for about 1/3 of these regions each year, completing the cycle every three years. In the interim period, these regional studies are updated to a current level, and unit costs and operating factors for all regions are published in one statement each year. This provides comparable cost data for all regions regardless of the year in which the base cost study was conducted. These statements provide a complete explanation of how the costs can be used to develop costs for specific movements of traffic based upon how a given traffic is handled. The studies also provide the Commission with information on motor carrier costs for use in its various regulatory functions and makes available to the public cost information useful to carriers, shippers, traffic organizations, rate bureaus, educators, and others.

Granting that regional cost studies are not the answer to all ratemaking situations, these studies are of great value in measuring the general level of costs in rate proceedings covering large segments of traffic. They are also invaluable in ascertaining the compensatory nature of the rates on shipments that receive average transportation services. However, because they represent the average cost for all shipments falling within various weight brackets, they do not necessarily reflect the cost of specific traffic weighing other than the average or the cost of receiving special services other than the average service accorded all shipments within the weight bracket.

\(^{70}\) The ICC Bureau of Accounts prepares these regional studies on a cyclical basis every three years. An example is ICC Bureau of Accounts, Statement ZC 16-73, Cost of Transporting Freight by Class I and II Motor Carriers of General Commodities (April 1978).
For this reason when costs are desired for a specific shipment with known transportation characteristics which are different from the average, the unit costs developed through Highway Form A are adjusted based on the services actually accorded specific shipments.\textsuperscript{71} For example, adjustments can be made for:

(1) Actual platform handling experience. The costs developed in Highway Form A reflect the average platform handling experience for various size shipments. However, in actual practice, some shipments may receive a platform handling at origin, destination or interchange point and some may not. When actual platform experience is known, costs are adjusted accordingly.

(2) Partial pickup and delivery. Methods are provided for adjusting pickup and delivery running and stop costs, and for determining trailer drop and pickup costs.

(3) Density of the commodity transported. Adjustments to pickup and delivery and platform costs are provided to adjust costs reflecting average density of all traffic known to traffic density.

(4) Actual miles of haul. Line-haul costs should be based on the actual miles traveled in transporting the traffic which can be determined by special study of a representative number of trips. In those instances where a study is not made, the miles may be based on the short-line miles from the Household Goods Carriers' Bureau Agent Mileage Guide, increased 6 percent for circuity.

(5) Round trip load factor. This is an adjustment to the line-haul cost to reflect the actual round trip load of a specific shipment.

(6) Line-haul density. As in (5), round trip load factors and the resulting line-haul costs are adjusted to reflect density and not weight alone.

(7) Different line-haul running speeds. The line-haul cost per vehicle-mile in Highway Form A reflects the average line-haul running speed for the carriers included in the study. Under certain circumstances the overall cost per vehicle-mile may be adjusted to reflect changes in cost due to speed.

Some point out that ratemaking costs based on the territorial average by weight bracket and distance block fail to recognize carriers whose costs are higher or lower than the average. However, judging rates in terms of average costs tends to hold down the rates and revenues of the high cost carrier, thus providing an incentive for a more economical operation. It also enhances the possibilities of profit for the low cost carrier, rewarding it—some would say unduly—for its efficiencies.

It should not be concluded that average costs preclude the use of individual carrier costs in rate cases. Individual costs are, in fact, preferred.\textsuperscript{72} For instance, in adjustments in which several carriers participate, costs developed on an average basis are entitled to weight in the absence of more specific data, in passing on the compensatory character of rates. System average costs of a large group of carriers, reflecting costs of movement of a variety of commodities over a wide area with diverse operating conditions,

\textsuperscript{71} See 1970 Rules, supra note 64.
\textsuperscript{72} Id. at 304-05.
cannot be as decisive in determining reasonableness of particular rates on a specific commodity, especially where the proponent has been moving the traffic at rates the same as those proposed for several years under operating conditions similar to those attending to anticipated movement.

If the proponent is primarily a hauler or less-than-truckload traffic, its system average operating expenses do not provide an adequate standard for measuring compensativeness of proposed truckload rates. From the above, it can be seen that the Commission is well aware of the limitation on the use of average costs.

Observers of the Commission’s use of the average costs sometimes mistake the role of costs in the Commission’s decisions. Rates are not made by combining various ingredients measured according to established formulas. Ratemaking always has been and no doubt always will be a process depending importantly upon the exercise of judgment. The Commission has always tried to remain flexible in its treatment of costs in the belief that only in this way can it arrive at sound and logical conclusions consistent with the National Transportation Policy. On this basis rates have been approved in a number of proceedings which would not have been compensatory under normal costing methods. Yet, costs remain a most important factor. The position taken in the so-called Doyle Report73 coincides with that of the Commission. Thus, as stated in the report:

Throughout the course of our examination of transportation policy it has been repeatedly impressed upon us that, while cost is not the sole factor in pricing, it is the only measurable one. Sound cost analysis is an essential pricing tool . . . .

D. One-Way Costing

Another controversial area of costing is what is called one-way versus two-way costing or back-haul rates.

For the motor carrier industry to be sound and financially stable, overall rate levels must provide the carriers with adequate revenues to enable them to continue furnishing service. This principle is set forth in section 216(i) of the Act.74 One application of this principle is that variable costs are found generally indicative of the minimum level of expenses which must be recovered by a carrier in providing particular services. In computing variable costs, the Commission in the past often required the calculation to be on a roundtrip basis.

However, in Carbon Black from the Southwest to Ind.,75 Ohio & Mo.,

75. 325 I.C.C. 138 (1965).
the Commission authorized use of one-way costing. In that proceeding the motor carriers showed that they had lost a substantial volume of carbon blacks traffic over a 2-year period as the result of a reduced rail rate and that a "heavy and chronic imbalance of traffic" existed in the going direction of the proposed rate. In the light of that evidence the Commission approved a proposed rate which exceeded variable costs computed on a one-way basis.

There is another situation where the Commission has allowed incremental costing of back-haul traffic. This is where the traffic would not move but for the reduced rates or where the traffic would otherwise move in private carriage.\textsuperscript{76}

\textit{Carbon Blacks, Aluminum Extrusions}, and similar cases subsequent to them, therefore, recognize that transportation conditions may justify one-way costing. We believe that these cases reflect sound policy and will consider whether the use of one-way costing should be expanded.

\textbf{E. General Rate Increases}

As discussed in a previous section of this testimony, the post-World War II period has been marked by increasing carrier utilization of general rate increase proposals. As stated there, a request for a general increase is based on systemwide revenue needs instead of those concerning only particular movements, commodities, or segments of traffic. Unlike ordinary rate proposals, a general increase is normally sought as a percentage increase applicable to all or nearly all rates maintained within a ratemaking territory. Recognizing the need for such measures, the Commission has endeavored to ensure that the proceedings are determined in the fairest way possible to both carriers and shippers, balancing the carriers' need to charge rates sufficient to meet their revenue needs and to enable them to fulfill their service mission and the public's entitlement to adequate and efficient service at the lowest cost consistent with the furnishing of such service. Over the past thirty odd years, the Commission, through its decisions in general rate increase proceedings and its overall efforts to develop valid criteria to apply to such proposals, has steadily improved the quality of its considerations in general rate increase proposals.

For a period of time during and following World War II, the Commission relied primarily on the evidence of the operating ratio of carriers in general rate increase proceedings. The term "operating ratio" refers to the ratio of the carrier's operating costs to its total operating revenues. The theory behind the reliance on operations revenues is that because trucking requires low fixed investment, the primary risks of business is involved in operating outlays. An operating ratio of 93 percent was thought appropriate to insure

\textsuperscript{76} Aluminum Extrusions from Miami to Chicago, 325 I.C.C. 188 (1965).
the viability of carriers. However, in the early 1960's, emphasis began to shift away from the operating ratio as a viable criterion of revenue need. In passing upon the merits of the operating ratio standard in General Increases—Eastern Central Territory, the Commission stated:

Although an operating ratio of 93 percent has been found reasonable in the past, we do not regard such an operating ratio as an immutable standard. In view of the numerous changes which have taken place in the motor carrier industry, we believe this matter should be thoroughly explored in the light of a more complete record developed either in a further hearing in the instant proceeding or in some similar proceeding. At the same time, we believe that the parties, in cooperation with the Commission, should produce all the information required to show the precise effect of transactions between carriers and their subsidiaries or affiliates on carrier operating ratios.

Passing again on the merits of the operating ratio a year later in General Increases—Middle Atlantic and New England Territories, the Commission found that: "The mere showing of present operating ratios of above 93 percent without a showing of the factors that make up such a ratio is not sufficient for our purposes."

The Commission’s consideration of general rate increase proposals became more refined. As the Commission moved away from reliance on the operating ratios of the carriers, it started to require various other financial data from the carriers. Cases in 1962 and 1963 stressed the need for more precision in showing the effect of transactions between carriers and affiliates or subsidiaries and more detailed evidence of expense items of representative carriers.

In 1964 an order was issued intended to insure the submission of adequate information in future general rate cases. The order required carriers to provide supporting data for individual representative carriers in the form of various financial ratios relating to overall carrier operations and the specific territories and traffic affected by the rate proposal.

General rate increases came to a virtual standstill for the period immediately following the 1964 order. By early 1967 the motor carriers had been denied seven straight applications over a two-year period primarily on the basis of the lack of representativeness of the sample carriers. As a

77. 316 I.C.C. 467, 481 (1962).
79. Id.; General Increases—Eastern Central Territory, 316 I.C.C. 467 (1962).
80. Prior to the rules adopted in Ex Parte No. MC-82, New Procedures in Motor Carrier Revenue Proceedings, 339 I.C.C. 324 (1971), evidentiary guidelines governing general increase proposals were issued on an ad hoc basis. These determinations are the so-called "big orders." An example of a "big order" is found in Increased Rates and Changes From, To and Between Middle West Territory, 335 I.C.C. 142, at 151-54 (1969).
81. LTL Class Rates and Minimum Charges Between Midwest and Central Territories, 325 I.C.C. 106, 111 (1965); General Increases Between East and Territories West, 329 I.C.C. 626, 640 (1965); Increased Rates Within Southwest and Between Colo. and Wyo. and Southwest, 326
result of *Ringsby Truck Lines, Inc. v. United States*, the Commission undertook to delineate more specifically the evidentiary requirements for general rate increases. This effort was manifested in the so-called Big Order of April 27, 1967. The requirements of the order related to determination of a traffic study, a cost study, affiliate data, and evidence of required operating ratio and desired profit level.

On April 3, 1968, the Commission ordered the motor carriers to produce evidence of:

[The sum of money, in addition to operating expenses, needed to attract debt and equity capital which they require to insure financial stability and the capacity to render service. This evidence should include, without limiting the evidence that may be presented, particularized reference to the respondents' reasonable interest, dividend, and surplus requirements and experienced, projected, and needed rate of return on depreciated investment in transportation.]

This order was reaffirmed by the Commission in its decision of June 5, 1969, on *Increased Rates and Charges, From, To, and Between Midwest Territory*, which stated in part: "The single most important gauge of a motor carrier's ability to attract equity capital is its return of value over and above the values the investors have committed to the enterprise. Two significant measures are the rate of return on stockholders' investment and the rate of return on assets."  

The experience of carriers and the Commission under these orders was mixed. The experience, however, highlighted the need for an even more definitive approach to determining the evidentiary criteria for general rate increase cases.

The culmination of this experience was the institution on August 1, 1969, of Ex Parte No. MC-82, *Proposed New Procedures in Motor Carrier Revenue Proceedings*. This proceeding, a major formal rulemaking, gathered substantial input from a wide spectrum of shipper and carrier interests and resulted in the fullest consideration of the subject of general increase cases, carriers' revenue need requirements, and the data necessary to permit rendering of the fairest possible decision.

The proceeding led to the adoption of special rules which apply to the

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83. See note 80 supra.
84. Increased Rates and Charges, From, To, and Between Midwest Territory, 335 I.C.C. 142, 152, app. A (1969).
85. Id. at 148.
more significant motor carrier general increases on freight rates and charges. The rules themselves are often referred to as "the MC-82 rules" in reference to the proceeding\(^{87}\) in which they were adopted.

Our rules governing general increases of motor common carriers of property\(^{88}\) apply only on the major increases. One of the threshold criteria, for example, is that the increase involved generate more than 1 million dollars in additional revenues. The rules also embrace major restructurings.\(^{89}\)

The MC-82 rules have been revised twice in the light of suggestions for their improvement by shippers and carriers as well as our own experience with them.\(^{90}\) Significant further revision is now in process.\(^{91}\)

The rules are essentially procedural, specifying when, what, and with whom the carriers (or the bureaus acting on their behalf) must file. The carriers are free to supplement the mandatory data with any other data they believe is relevant. The rules ensure that the Commission has before it the minimum data which experience has shown is needed to evaluate whether the proposed increases or restructuring are in fact justified. They ensure that interested shippers and the public-at-large or governmental agencies and bodies wishing to participate\(^{92}\) also have this data with enough time to oppose the tariff proposal. The rules achieve these objectives in part by requiring that the increase tariff and the entire justification relied on be filed with the Commission and served on interested parties at least 45 days prior to the effective date of the proposed tariff.\(^{93}\)

The data we require includes (1) a traffic study, (2) a cost study, (3) revenue need information and (4) affiliate data.\(^{94}\)


\(^{88}\) Somewhat analogous rules were adopted last year to govern industry-wide increases in bus fares and are codified at 49 C.F.R. § 1104(b) (1977). The Commission is currently exploring the feasibility of adopting comparable rules to govern general increases of other specialized carriers, such as those transporting household goods.

\(^{89}\) Restructurings are widespread rate changes but, unlike general increases, many are downward so that the net increase in revenues may be minor. Typically, they involve increasing rates and charges on smaller LTL shipments (e.g., under 500 pounds) and decreasing rates and charges on larger shipments. The Commission's concern about the impact of these restructurings have on the so-called "small shipments" problem led to the institution of Ex Parte No. MC-98, New Procedures in Motor Carrier Restructuring Proceedings, 41 Fed. Reg. 41 Fed. Reg. 1923 (1976).


\(^{91}\) 357 I.C.C. 498 (interim report decided June 9, 1978).

\(^{92}\) Protests and briefs to proposed general increases in rates and in fares have been filed by federal (the Departments of Justice, Transportation, Agriculture, Defense, as well as the Council on Wage and Price Stabilization), state, and local governmental bodies.

\(^{93}\) Because a general increase tariff and its justification are often complex, the 30-day statutory lead time is inadequate.

\(^{94}\) 49 C.F.R. § 1104.2-1104.5 (1977).
1. The Traffic Study

The traffic study is based on the industry's continuous traffic study (CTS)\(^{95}\) and must be conducted in accordance with specific guidelines to ensure that its conclusions are representative.

The rules specify the study carriers\(^{96}\) and require that the study be for the most current 12-month calendar year for which the carrier system operating data is available. They require that the study include a probability sampling of the actual traffic handled during identical time periods for each study carrier.

2. The Cost Study

Additionally, the MC-82 rules require a detailed costing of the sampled traffic. The carriers are required to develop service unit costs for each individual study carrier, adjust them by size of shipment and length of haul, and then apply these unit costs to the traffic service units developed from the traffic study. Operating ratios are then derived for the issue traffic by individual weight brackets.

The basic cost analysis performed by our cost analysts, under the MC-82 rules, is confined to the evidence of record. Further, when necessary, underlying workpapers may be requested to support allocation factors or other data which is not clear on the record. Under MC-82 the burden of proof rests with the carriers to support the reasonableness of their proposed rate adjustments. In addition, each case is treated on its particular merits because from case to case, rate relief is sought by the various carriers for different reasons and under varying economic circumstances. Common to most general increase and restructuring proceedings filed under the provisions of Ex Parte MC-82 are various items pertaining to traffic study, frame carriers used, cost study, updating, through versus carried method of costing, density adjustment, and cost revenue comparisons by weight bracket.

More specifically, the items identified above are examined in the following manner:

(1). Justification statements submitted in accordance with Ex Parte No. 

\(^{95}\) The CTS is based on a statistical sampling plan prepared by an expert in the field. 49 C.F.R. § 1104.9 (1977) (one of the MC-82 rules) ensures that shippers as well as the Commission have ready access to all underlying data used in the preparation of the materials used by the carriers as their justification, and thus enables the shippers and the Commission to examine the sampling procedures for the traffic study in the event there is reason to question the traffic sampled.

\(^{96}\) The study carriers are those carriers participating in the traffic requirement for allocation expenses between line-haul and pickup and delivery services [i.e., those specified in 49 C.F.R. § 1207 (1977) instruction 27] which participate in one of the motor carrier industry's Continuous Traffic Studies (CTS), and which derive $1 million or more in annual operating revenues from this issue traffic or 1 percent or more of the total annual operating revenues of all carriers from the issue traffic.
MC-82 procedures contain financial data, as well as cost data. The pro forma portion of the financial data is based on updated costs developed through the cost study. Consequently, the validity of the methodology employed in developing this cost study must be initially verified to determine the adequacy of this data for cost and financial analysis purposes. If the cost study is found to be deficient, this data is restated, if possible, to correct these deficiencies. When restatement of this data cannot be ascertained, the analysis, which is developed for the Commission, indicates that the justification statement submitted in support of the particular rate proposal is unacceptable for determining the reasonableness of that proposal.

(2). All cost data in the justification statement is also examined for compliance with the requirements established in Ex Parte No. MC-82. Specifically, the traffic study is reviewed to determine if the procedures utilized by respondent carriers in developing this study conform to the prescribed regulations. As a practical matter, the general design of the traffic study has not changed materially since the inception of Ex Parte No. MC-82.

Similarly, the cost study is scrutinized with regard to the method employed in developing costs for the base study year, the present pro forma year, and the restated pro forma year. Particularly, the assignment factors and expense allocations used in the cost study are analyzed with respect to their reliability. In addition, the procedures used in updating labor and non-labor expenses to both the present pro forma level and the restated pro forma level are examined for their accuracy and theoretical validity.

The specific unit costs of each carrier are applied to the traffic characteristics of that same carrier, i.e., the "each-to-each" costing methodology prescribed in this proceeding. These data are then accumulated using all carriers employed in the cost study. This includes both the more efficient and the less efficient carriers. Thus, this use of all carrier data provides the average transportation costs for the traffic at issue and keys rate levels, insofar as costs are considered, to the average carriers.

(3). The method administered in rerating base year revenues to both the current level and the proposed level is reviewed with regard to its reasonableness and accuracy. Ex Parte No. MC-82 requires that estimates of current revenues should reflect all rates and charges in effect no later than 45 days prior to the date of the tariff filing and that the proposed level should reflect conditions prevailing on the effective date of the rate proposal.

(4). In those instances where respondent carriers submit data on both a "carried" and a "through" basis, the evidence is examined to determine its credibility, accuracy, and compliance with the prescribed procedures. The "through" basis evidence is further analyzed to substantiate the lack of any significant sampling bias. Absent adequate evidence demonstrating that the use of the "through" basis does not result in a substantial sampling
bias, all conclusions based on cost analysis relating to the reasonableness of the rate proposal are predicated solely on "carried" basis data. (5). Finally, the cost-to-revenue comparison, developed on the basis of the cost study for the individual weight brackets affected by the rate proposal, are thoroughly scrutinized to determine if there is any cost justification for the proposed rate adjustments. Where provable carrier expense increases exceed proposed revenue increases, the rate proposal is considered to be totally cost justified. On the other hand, if the increases in revenues equal or exceed increases in expenses, prior to consideration of the proposed increase, the rate proposal has not been shown to be cost justified. Of course, in between these two extremes are the rate proposals that are only partially cost justified. In these cases, only a certain percentage of the proposed revenue increase is necessary to cover provable expense increases. When this occurs, the exact percentage of the proposed revenue increase that is cost justified is calculated.

Basically, these cost-to-revenue comparisons are the crux of the cost analysis conclusions. More importantly, however, cost analysis provides one element of input to be considered in rendering a decision.

In addition to analyzing the justification statement initially filed by respondent carriers, protests and replies are also analyzed.

Concomitantly with the "cost analysis" of data in MC-82 type proceedings, the "carriers' revenue need" is also carefully examined and evaluated. "Carrier revenue need" is defined as the revenue generation required to cover operating expenses and provide fair and reasonable returns to the carriers' capital suppliers. To provide safe and reliable service to the shipper, carriers must maintain adequate truck fleets and terminals. Maintenance of adequate plant requires capital which in turn requires adequate income levels to repay borrowing and pay dividends. Revenue and profit levels are revenue need questions which the Commission addresses in each and every general increase case.

If the carriers' data justification is not assailed by any protestant to the tariff in issue, the Commission and Staff, including the Section of Cost and Valuation and the Section of Financial Analysis, closely review the mandatory evidentiary materials. If the supporting data appears weak or marginal, an investigation into the lawfulness of the tariff will be ordered. The effective date may also be suspended for seven months while the investigation is undertaken.

If an investigation is initiated, it will culminate with a Commission decision granting, denying, or approving the increase in part, as the evidence may warrant. In deciding the lawfulness of any particular general increase, the Commission balances the economic and public policy considerations involved, including the need, in the public interest, of adequate and efficient transportation service by motor carriers at the lowest cost consistent with
furnishing of such service and the need of the carriers for revenues sufficient to enable them under honest, economical, and efficient management to provide such service.\textsuperscript{97}

The above outline of the MC-82 procedures and our analysis thereunder is only an outline. The procedures themselves are complex and involve some highly technical issues. The complexity of the problems involved in getting probative traffic, cost, and revenue data is reflected to some extent in the size and complexity of our three MC-82 reports to date as well as the large amount of data included in filings by the carriers under the procedures. While we believe that the procedures essentially achieve their objective of providing necessary data to assess the carriers revenue need proposals, we also recognize that further refinement is foreseeable. The MC-82 rulemaking itself is open-ended to facilitate revisions to the rules. Major revisions, in fact, are currently being considered, as has been noted by our report in Ex Parte No. MC-98.

Rate increases not falling within the specific parameters of the MC-82 rules, of course, remain subject to various statutory and Commission procedural requirements designed to ensure that the public is not likely to overlook important tariff changes. These procedural safeguards include the Commission's strict rules governing tariff publication, ensuring that rate changes are clearly identified, requirements which, when coupled with the 30-day statutory lead time accorded by section 217(c) of the Act,\textsuperscript{98} ensure that the public has sufficient notice of the proposed tariff and adequate time to file a protest to objectionable changes. These provisions also ensure that the Commission through its Suspension and Fourth Section Board has sufficient lead time to act on the protest. If the circumstances should warrant, section 216(g) of the Act\textsuperscript{99} gives the Commission authority to suspend the tariff for seven months while investigating the lawfulness of the proposed rate changes. If found unlawful, the Commission will order the objectionable provision canceled.

F. PROBLEM AREAS

In the past, the Commission's Section of Cost and Valuation has concentrated its efforts in costing to motor carriers of general commodities. However, specified carrier groups, such as household goods carriers, have come to the forefront due to the traffic volume and magnitude of their rate increase requests, and their impact on the nation's economy. As an indication of their impact, in 1976, specialized carriers generated 40 percent of the revenues of all motor carriers having annual operating revenues of

$500,000 or more.  

1. Specialized Carriers

The Commission has found during the course of considering rate increase requests of some of the specialized carrier groups, that the cost evidence has been inadequate. This lack of adequate cost evidence has brought about a need for additional MC-82-type proceedings for these carriers. Such proceedings foster the development of minimal data requirements which (1) impose a scheme of fact presentation on the parties which is both logical and understandable; (2) allows interested parties to study the financial position of the carriers; and (3) allows the Commission to assess and evaluate the revenue needs of the carriers.

The Commission’s Section of Cost and Valuation is currently investigating the possibility of a rulemaking proceeding for household goods carriers. Future plans include the development of MC-82-type procedures for both the bulk motor carriers and possibly heavy haulers.

2. Need for New Cost Formulas

The Section of Cost and Valuation has determined that a need exists for special cost allocation formulas for various types of specialized carriers. This need stems from the fact that the operating and accounting characteristics of these particular carriers differ from the operating and accounting characteristics of general commodity carriers, i.e., Highway Forms A or B are not suited to the development of costs for these carriers. Accordingly, the Commission’s Section of Cost and Valuation is currently researching reported data, studying the systems of accounts and anticipates meeting informally with certain specialized motor carrier groups to discuss operating characteristics and available industry data. A major problem which must be resolved stems from the fact that many specialized carriers rely on owner-operators to perform the transportation service. In the past, it has been virtually impossible for the carrier to collect and submit reliable cost data for representative owner-operator movements.

3. Field Studies

A natural out-growth of formula development and the subsequent cost computations is the need for special field studies to enhance and refine cost estimates.

V. RATE BUREAU MONITORING

Carrier management initially decides what level of rates it will seek to establish. These rates are published by the carrier and filed with the Commission. Copies of those rates are available for public inspection at each carrier’s office and at the Commission. The public availability of these rates tends to assure that shippers, towns, ports and individuals are being charged the right amount and neither receive any special preference nor are the subject of any unjust discrimination.

An individual carrier may publish and file with the Commission its rates in its own tariffs, or have its rates published by an “agency” for its own account or jointly with all carriers willing to establish the same charges.

Agency tariffs are published under the auspices of a rate bureau. Rate bureaus are carrier-owned organizations, formed by agreement between and among regulated common carriers, for the purpose of joint or collective ratemaking activities. Those agreements set forth the procedures for the joint consideration, initiation, and/or establishment of rates, fares, classifications, and certain other related matters applicable to the transportation of property and passengers in interstate or foreign commerce. Section 5a of the Interstate Commerce Act\(^\text{101}\) authorizes motor common carriers to apply to the Commission for approval of those agreements, and approval relieves the member carriers from the operations of the antitrust laws.

To warrant Commission approval and hence exemption from the operations of the antitrust laws, a rate bureau agreement must guarantee that members have the full, free, and unrestrained right to take independent action either before or after any determination arrived at through the collective action procedures of the agreement.

Over the years, other conditions have been prescribed, including the following:

1. All eligible carriers must have a right to become a party to an approved agreement upon the same terms as present members.
2. No member carrier may be expelled except for nonpayment of dues, and provisions must be made for reinstatement.
3. The terms of an agreement must be definite and certain, with the procedures for collective action clear and orderly. No open-ended provisions can gain approval.
4. Ultimate responsibility and power with respect to the determination and establishment of rates must be with the carrier managements, and not with the bureau.
5. Carriers must be free to publish their own individual tariffs.
6. There must be adequate carrier representation on committees and reasonable quorums for meetings.
7. Dues assessment must be correlated to the size of the carrier member.

In addition to the enumerated conditions, a rate bureau agreement to be approved by the Commission must provide that any interested person (member carrier, shipper, bureau, etc.) may initiate a rate proposal before the bureau. All collective proposals for new or changed rates and related matters must be docketed and adequate notice given, usually by publication in a transportation journal of national distribution or by docket bulletin of the bureau. Opportunity must be given for any interested person to express his views for or against a proposal either orally or by written representation.

The Commission requires that procedures used during the processing of proposed rate changes must be carefully detailed in the agreement, and that adequate public notice be given at each stage of the collective process and at the time of final disposition. The same strict notice requirements apply for independent action proposals. These safeguards, which are necessary to protect the public interest, are included in all approved agreements.

My prior testimony before this subcommittee last October concerned price competition and the role of rate bureaus in the motor carrier industry. There was much discussion of the Commission's recent rate bureau investigation in Ex Parte No. 297 and the continuing exercise of the Commission responsibilities in the area. Recent Commission actions affecting motor carrier collective ratemaking activities give added emphasis to the significance of the Commission's oversight function.

On July 7, 1977, the Commission, in response to a petition filed by the Department of Justice, instituted Ex Parte No. 297 (Sub-No. 2), *Notification of Rate Proposals Following Prior Independent Action*¹₀² to determine whether to adopt a rule proposed by the Department of Justice. The Department of Justice had alleged that rate bureaus were concealing and modifying independent action rates without the consent or knowledge of the carriers which had established the rates through independent action. The rule proposed by the Department of Justice would require rate bureaus to notify affected member carriers of proposed changes and cancellations of independent action rates and would prohibit rate bureaus from changing such rates for the account of any carrier without first obtaining the carrier's written consent.

In response to the proposed rule, the Commission received comment from 48 shippers and carriers as well as from the Department of Justice. Public comment on the proposal revealed that modifications, and cancellations of motor carrier independent action rates without notice to the carriers which had established those rates, can and do occur. Changes of this nature are caused by the inadequacy of notice to carriers, docketing practices of rate bureaus, and carrier inattentiveness. These practices infringe upon

the right of independent action. Comment also revealed that notice to shippers and interested parties of proposals to change motor carrier and rail independent action rates are inadequate, and that motor carriers, shippers and others interested are often accorded insufficient time to reply to these proposals. These practices violate the right to notice and the right to be heard in the rate bureau setting.

With these problems in mind, the Commission adopted a rule\(^{103}\) that will do three things: (1) require that motor carriers, shippers and other interested parties be accorded notice of proposals to change or cancel rates established by independent action, (2) require that the parties be allowed a minimum of fourteen days to reply in person or in writing to proposals to change or cancel independent action rates, and (3) require that motor carrier rate bureaus obtain the written consent of carriers before changing or cancelling independent action rates in which they are participating. In addition, the rule defines key terms such as "independent action," "adequate notice," "rate bureau," and "rate."

The rule will also make an exception. It will release rate bureaus from complying with the notice and consent requirements of the rule when proposing changes in independent action rates pursuant to a general rate increase or rate restructuring. The exception is made because general rate increases and rate restructurings do not affect the efficacy of the right of independent action. Nor do they deprive carriers, shippers and other interested parties of their right to notice, because changes of this nature are widely publicized well before the fact.

The rule is scheduled to take effect ninety days after publication in the Federal Register. The evidence of record and Commission knowledge of rate bureau operations indicates that rate bureaus will be able to comply with the rule if given sufficient time to prepare to do so. Thus, the rule will address genuine problems in current rate bureau practices detrimental to carriers, shippers and consumers without unduly hampering rate bureau operations.

Last October, I indicated that the Commission had developed some experience in applying the provisions of section 208 of the 4-R Act\(^{104}\) to rail rate bureaus, and would consider whether those provisions should be applied to motor carrier rate bureaus. On December 30, 1977, the Commission instituted a rulemaking proceeding on its own motion in Ex Parte No. 207 (Sub-No. 3), \textit{Modified Terms and Conditions for Approval of Collective Ratemaking Agreements Under Section 5a of the Interstate Commerce Act}, to determine whether the prohibitions on collective ratemaking contained in section 5b of the Act should be adopted as additional terms.

and conditions on the approval or continued approval of collective ratemaking agreements subject to section 5a of the Act. Section 5a of the Act governs collective ratemaking among freight forwarders, water carriers and motor carriers.

The provisions in section 5b of the Act to be studied prohibit participation in agreements with respect to, or any voting on, single-line rates, or on joint-line rates unless the participating or voting carrier can practicably participate in the interline movement. Section 5b also prohibits any agreements which provide for joint action to protest or seek suspension of any rate filed by any carrier, whether it belongs to the rate bureau or not.

These prohibitions allow for two exceptions: voting on general rate increases or decreases, and on broad tariff changes. The Commission will study whether these exceptions should be adopted, as well as whether parallel behavior should be prima facie evidence of a violation of section 5a.

More than 100 persons have notified the Commission of their intent to participate in this proceeding and a procedural schedule for comments has been established.

In addition to these rulemaking proceedings the Commission issued an order on December 30, 1977, in Ex Parte No. 297 (Sub-No. 4), Reopening of Section 5a Application Proceedings to Take Additional Evidence, requiring that carrier members of all currently approved collective ratemaking agreements under section 5a of the Act submit additional evidence to demonstrate that those agreements should continue to have Commission approval. The reopening order also applies to all applications pending Commission approval (excluding rail agreements now subject to section 5b of the Act).

The Commission instituted this proceeding to re-examine all agreements presently approved under section 5a to determine whether these agreements still satisfy the standard of review set forth in paragraph (2). Pursuant to paragraph (7) of section 5a, the Commission is taking additional evidence to determine whether previously approved agreements (excluding agreements now subject to section 5b of the Act) still satisfy the requirements of the Act. The Commission will incorporate this evidence with revisions preferred under Ex Parte No. 297, as well as any other revision the parties in each proceeding wish to submit, to determine whether such agreement should continue to have the approval of the Commission. Approval of agreements found not to conform to section 5a will be discontinued as will approval of agreements for which no evidence is filed.

Parties to collective ratemaking agreements are required to submit evidence consistent with their burden of proof. Other interested parties, such as shippers, ultimate consumers and public interest groups, the Federal Trade Commission and the Department of Justice were invited to participate in the proceedings. The latter two government agencies were particu-
larly invited to comment on the anti-competitive effects of the agreements under consideration. Evidence submitted by all parties in any proceeding must be relevant to one of these three issues:

1. Whether the agreement enhances one or more national transportation policy goals,

2. Whether the agreement will harm interests intended to be protected by the antitrust laws, and,

3. Whether the benefits the agreement confers on the public interest from the standpoint of the national transportation policy outweigh the harm the agreement will do to the public interest intended to be protected by the antitrust laws.

It was concluded in Ex Parte No. 297 that rate bureaus served a useful function in ratemaking. However, we are aware that most of the section 5a agreements were approved by the Commission more than 15 years ago. The substantial changes in the trucking industry during that period suggest a need to determine whether all previously approved agreements are still necessary and whether they still conform with the standard set forth in paragraph (2) of section 5a and the public interest. In this regard, the Commission has established a staggered procedural schedule for the filing of additional evidence by the rate bureaus which will bring all currently approved and pending section 5a agreements before the Commission within one year from the date of service of the order in this proceeding, January 6, 1978.

As noted in my prior testimony, the motor carrier rate bureau regulations issued by the Commission in Ex Parte No. 297 were challenged by three different bureaus before the United States Court of Appeals for the Fourth Circuit, in Richmond, Virginia. The challenged regulations included: (1) the prohibition against rate bureau protests of independent action proposals before the Commission; (2) the prohibition against shipper-affiliated carriers serving on the bureaus’ boards of directors or rate committees without prior Commission approval; and (3) the prohibition against profit-making by rate bureaus.

On July 21, 1977, the Fourth Circuit handed down its decision. The three-judge panel’s decision sustaining the regulations in an opinion by the late Mr. Justice Clark was unanimous on two of the three issues; one judge dissented on the question of protests against independent action proposals. Petitions for rehearing were denied except with respect to the question of protests against independent action proposals. Upon further hearing on November 8, 1977, the Commission’s finding concerning that question was sustained by a majority of the Court.

Although a petition for certiorari was subsequently filed with the Supreme Court concerning the prohibition against shipper-affiliated carriers serving on the bureau’s board of directors or rate committees without prior Commission approval, no stay was entered and the Commission, by order
dated January 23, 1978, reinstated the effectiveness of this prohibition and has resumed processing shipper-affiliated carrier applications.

There is no question that a carrier which is affiliated with a shipper may become a member of an approved ratemaking organization. The concern expressed by the Commission in Ex Parte No. 297 is the role that a shipper-affiliated carrier plays. Although the Ex Parte No. 297 investigation did not reveal any pattern of undue shipper influence over affiliated carriers, the Commission was still concerned about the apparent conflict of interest and the possibility that shipper-affiliated carriers would represent the interests of their affiliated shippers and not the interests of the carrier industry when serving on rate bureau committees. The Commission was convinced that affiliation with a shipper could cause the objectivity and fairness of even the best-intentioned carrier representatives to suffer when considering rate questions in the light of their particular shipper-affiliates’ interests. Accordingly, the Commission concluded that a carrier member of a bureau, which is affiliated in any way with a shipper may not serve on a bureau’s board of directors, general rate committee, or any other committee which has the effect, either directly or indirectly, on the ratemaking function of the bureau without specific prior Commission approval.

Consistent with our oversight responsibility we are continuing our rate bureau monitoring program which is designed to ensure carrier compliance with approved ratemaking agreements and with the rules and regulations of Ex Parte No. 297. Subsequent to my testimony of last October, three rate bureau investigations have been conducted:


The reports of our investigatory teams revealed substantial compliance with the approved agreements and with Ex Parte No. 297. However, several problem areas which appear common to many motor carrier agreements were disclosed. For example, we note that, with but few exceptions, the same members and/or companies have been represented on the governing and ratemaking committees of the bureaus investigated for the past five years. The carriers usually cite economics as the prime reason for the lack of more widespread participation. Since members of rate bureau boards and committees serve without pay and are not ordinarily reimbursed by the bureau for expenses incurred in attending meetings, in many instances only the larger carriers (Class I) actively participate in the activities of various bureaus. Future investigations and Ex Parte No. 297 (Sub-No. 4)
will examine this and similar problems such as low quorum requirements, in an effort to insure that a small group of member carriers could not exercise a dominant role in rate matters.

Our investigation also revealed that some shippers were critical of one bureau’s use of so-called “canned or coded” disposition notices. These shippers stated that the reasons given for disposition were not detailed enough to allow someone totally unfamiliar with a docket to understand the reasoning behind a given disposition. In Ex Parte No. 297, the Commission expressed its concern regarding the lack of information as to the justification for the disposition of ratemaking proposals, and required that public notice of recommended final disposition by rate bureaus contain the reasons for the action taken. The involved bureau will be required to amend its present practice concerning disposition notice to reflect the Commission’s directive.

In addition to these formal investigations, personnel from the Bureau of Operations and attorneys of the 5a/5b Unit attended General Rate Committee meetings of the Steel Carriers’ Tariff Association, Inc. at Pittsburgh, Pa., and the Central States Motor Freight Bureau at Chicago, Illinois, on January 4, 1978, and January 10, 1978, respectively.
Collective Ratemaking: A Case Analysis of the Eastern Central Region and an Hypothesis for Analysing Competitive Structure*

ANDREW F. POPPER**

I. POLICY GUIDELINES FOR EX PARTE 297
II. BASIC LEGAL STANDARDS FOR REVIEW
III. GENERAL COMPETITIVE PROBLEMS RELATING TO ALL BUREAUS
IV. ACADEMIC ANALYSIS AND FURTHER STANDARDS
   A. MARKET STRUCTURE AND THEORY
   B. DIRECT APPLICATION OF THEORY
V. FINAL THOUGHTS ON MARKET PRESSURES AND CONCLUSION

I. POLICY GUIDELINES FOR USE IN EX PARTE 297

On December 30, 1977, the Interstate Commerce Commission issued an order in Ex Parte No. 297 (Sub. No. 4)¹ in which the Commission stated that it desired to review certain findings made earlier relating to the status of various rate bureaus throughout the United States. Essentially, the Commission re-opened all applications which had been issued under section 5a

* This article was submitted to the United States Interstate Commerce Commission in Ex Parte No. 297 (Sub-No. 4) (August 9, 1978) as expert testimony.

365
of the Interstate Commerce Act. The Commission indicated concern that there may be certain deficiencies in the various agreements which had been approved in the past and that the purpose of this particular proceeding was to discover those collective ratemaking agreements in which deficiencies existed and to remedy them. The order seeks to bring all collective ratemaking agreements before the Commission for review.

This article discusses the various aspects of collective ratemaking related to the approved agreement held by the Eastern Central Motor Carriers Association. This agreement was approved by the Commission in 1955. The Commission is seeking to ascertain whether the geographic marketplace in the Eastern Central Region is a healthy marketplace, taking special notice of the market effect of collective ratemaking as it interfaces with existing open market pressures. The material which follows centers on the question of whether the marketplace is indeed viable. The apparent task of the Interstate Commerce Commission is to insure that its approval of an agreement for collective ratemaking does not adversely affect the various competitive regulatory pressures which Congress intended to exist with the pure regulatory pressures which regulation over rates and entry naturally provides. Thus, an approved collective ratemaking agreement acknowledges the coordinated existence of certain open market competitive pressures as well as straightforward regulatory pressures. These two forces are to work in tandem to insure that the public interest is served by workable regulatory competition which should result in a reasonable rate of return on investment as well as a just and reasonable rate structure.

The end results of an effective regulatory system and of an effective open market system are identical. There are four market objectives: fair rates or pricing that is consistent with cost plus a reasonable rate of return, efficiency, innovation, and logical control over market participants or entry. Whether a system is regulatory or open market, or a mixture of both, these objectives remain constant. In the motor carrier industry, the Commission must perform a rather delicate task. It must insure the existence of certain open market pressures and insure the maintenance of certain service obligations by regulatory pressures while at the same time achieving the four goals stated above. By applying both regulatory and open market pressures in tandem, the Interstate Commerce Commission carries forward a long tradition of regulatory agencies which seek to balance regulatory obli-

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3. 2971.C.C. 563 (1955). As of this writing the Commission has not yet decided whether it will reapprove the agreement.

4. These include open market pressures from independent action and contract and private carriage pressure exerted by the potential of any shipper choosing to opt for transportation services other than that which is provided by motor freight common carriage.
gations with open market obligations. The balance is difficult since an overly zealous application of open market pressure is destructive to a highly regulated entity. On the other hand, an excessive regulatory pressure will result in a situation where open market pressures cannot be brought to bear. This too is unhealthy.

In balancing these two market forces, Congress has provided certain policy determinations on which the Commission can operate. One of those decisions is that the conduct involved in collective ratemaking, to the extent that such ratemaking is carried out pursuant to an agreement which has been approved by the Interstate Commerce Commission, shall be exempt from the application of the antitrust laws. In conjunction with this exception, the courts and Congress have jealously guarded the right of carriers to participate in their own independent action proceedings. If there is effective collective ratemaking pursuant to an approved agreement and if there is a requisite degree of independent action and if the resultant marketplace is healthy, then the objectives of Congress have been carried out and the objectives of the competitive policies underlying the antitrust laws have been met. The Commission's obligation is no greater than to see that the activity undertaken pursuant to a collective ratemaking agreement is consistent with the approved agreements and to also determine, from time to time, whether the resulting market structure allows for growth and meets the general market obligations regarding cost, entry, efficiency, and innovation.

It is not the Commission's responsibility to enter into an analysis of whether the antitrust laws are "more important" than the other considerations found in the national transportation policy. Most certainly, it is not the Commission's function to determine if the service obligations are more or less significant than competitive obligations by redrafting the national transportation policy in an ex parte proceeding. Competitive considerations are but one factor to be analyzed in determining whether the public interest has been satisfied pursuant to our stated national transportation policy. It is not the Commission's task in this proceeding to enter into that public interest balancing anew. That is a matter for Congress.

In reviewing the order of December 30, 1977, one might be led to believe that such a balancing between the national transportation policy and antitrust considerations is the task of the Commission. It is not. Competition is a part of the goals of the regulatory process. Indeed, a regulated marketplace is not by definition a noncompetitive marketplace. The marketplace which is involved in this proceeding is a regulated marketplace

6. Id.
7. Id. § 10101.
which has various component parts of competition in the open market context as well as in the regulatory context. If it appears that the marketplace is organizationally diverse, and it appears that it is an innovative and efficient marketplace where consumer prices are reflective of cost plus reasonable rate of return, and it appears that the controls over entry do provide reasonable stimulation, then the marketplace is healthy. If, however, it would appear that the motor carrier industry in any geographic market is non-organizationally diverse, dominated by a small number of carriers or oligopolistic, if it is not innovative, if there are negative service and efficiency ratings and if there is not logical open market or regulatory control over entry, then the marketplace is not healthy. These criteria are painfully simple.

In one major predefined geographic market, the Eastern Central Region, there are 1078 carriers now participating in Eastern Central tariffs, 855 of which submitted revenue questionnaires. The 855 carriers who have incomes from several thousand dollars to over a hundred million dollars are a direct indication of diverse organizational structure. Secondly, the high frequency of independent actions indicate that that particular open market force (independent action) is working well. The percentage of independent action filings appears to be approximately 41% of all filings. As to price, cost, and efficiency, the statement of the shippers and carriers who exist within the defined marketplace indicate little complaint in that area. By maintaining collective ratemaking, a regulatory control over the price structure has been imposed which has prevented major carriers from undercutting and eliminating smaller carriers. Quite simply, that kind of negative competitive pressure has been healthy in the marketplace and has allowed it to flourish.

II. Basic Legal Standards for Review

This proceeding raises a threshold question of legal standards. To as-

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9. These statements are on file at the Commissioner's offices in Washington, D.C. See note infra.
11. See note 9 supra.
12. There are two important supporting documents on which many of these conclusions are premised. The first is a comprehensive listing of carriers and revenue generated over a set period of time. This is provided to display the structure of the marketplace in terms of the market participants. This document reveals that there are indeed a large number of extremely diverse carriers. The second document is a graph summary of independent action proceedings undertaken in the year 1977. The table suggests a percentage of independent action for the L.T.L. shipments of around 25%. This is a very significant statistic in that it indicates that carriers feel quite able and willing to participate in independent action when the collective ratemaking process does not satisfy their own individualized interest. Success ratios for these proceedings vary from 80% to 90%. See G. DAVIS & C. SHERWOOD, supra note 10, at 75.
assess a collective ratemaking agreement, must the ICC relive the debates which surrounded the Reed-Bulwinkle Act 13 thirty years ago? Clearly, the answer is no. Contrary to the Commission's own order initiating this proceeding, 14 the task at hand is not to balance the national transportation policy and the antitrust laws. Rather, the task is to assess whether the competitive obligations which are to be satisfied by both open market and regulated market devices are in fact being met, based on the existing market structure.

The national transportation policy 15 requires an assessment of competition in the regulatory process. It is painfully naive to think that competition does not exist in a regulated marketplace—it simply takes forms different from the basic price competition format, usually seen as efficiency and service competition at the 'conduct' 16 level of assessment and as organizational diversity at the 'structure' level. The task of the Commission is to determine if the existing agreements which have been approved by the Commission over the last thirty years have allowed for the development or maintenance of a healthy marketplace or whether the regulatory pressures and open market forces have not produced or maintained a healthy market. The focus must be centered on structure, since the primary conduct, collective ratemaking, is exempt. As to structural analysis, many of the federal government guidelines can be used, 17 as well as the work of structural economic theorists discussed in part IV of this article.

One can look to the overall policies of the Interstate Commerce Act, and especially the national transportation policy statement, 18 to determine the prevailing policies of the Reed-Bulwinkle Act 19 Such a technical assessment is quite necessary to appreciate the success of the collective ratemaking-independent action potential competition mix in the various designated markets. The market studied for this article is that of the Eastern Central Region, serviced by the Eastern Central Motor Carriers Associa-

16. Naturally, one would include in this definition basic coordination as a competitive structure.
17. See, e.g., [1974 - 1] TRADE REG. REP. (CCH) ¶ 4510 regarding market structure analysis which states in part:
   (a) General enforcement policy . . . Market structure is the focus of the Department's merger policy chiefly because the conduct of the individual firms in a market tends to be controlled by the structure of that market . . . [N]ot only does emphasis on market structure generally produce economic predictions that are fully adequate for the purposes of . . . [§ 7, but it] also facilitates both enforcement decision-making and business planning.
19. Id. § 10706.
Cases have interpreted the overall policy of the Interstate Commerce Act:

The Act is affecting throughout its provisions . . . of securing the general public interest in adequate, nondiscriminatory transportation at reasonable rates.\(^{21}\)

The Transportation Act was designed to protect the public against action which might endanger its interests.\(^{22}\)

The principal objects of the Interstate Commerce Act were to secure just and reasonable charges for transportation; to prohibit unjust discriminations in the rendition of like services under similar circumstances and conditions; to prevent undue or unreasonable preferences . . . to inhibit greater compensation for a shorter than for a longer distance over the same line and to abolish combinations for the pooling of freights.\(^{23}\)

While these references are devoid of the necessity for maintaining a competitive marketplace, that has been a general obligation of all regulatory bodies since 1890. In *New York Securities Co. v. United States*,\(^{24}\) an argument was made that the criterion of "public interest" was uncertain. The Court said that:

It is a mistaken assumption that this is a mere general reference to public welfare without any standard to guide determinations . . . . Going forward from a policy mainly directed to the prevention of abuses, particularly those arising from excessive or discriminatory rates, the Transportation Act of 1920 was designed better to assure adequacy in Transportation service.\(^{25}\)

[Public interest . . . is not a concept without ascertainable criteria, but has direct relation to adequacy of transportation service, to its essential conditions of economy, efficiency, and to appropriate provisions and best use of transportation facilities.\(^{26}\)]

As to the question of congressional authority:

The Congress which had power to impose prohibitions in the regulation of interstate commerce, had equal power to foster that commerce by removing prohibitions and by permitting acquisitions of control where that was found to be an aid in the accomplishment of the purposes in view in the enactment of the Transportation Act, 1920.\(^{27}\)

Thus the Interstate Commerce Act requires more than just a view toward public welfare. The Act *mandates* a test of public interest which includes periodic assessments of market structure and *mandates* consideration and promotion of public interest and welfare in the transporta-

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25. *Id.* at 24.
26. *Id.* at 25.
27. *Id.* at 25-26.
tion area.\textsuperscript{28}

Although the Act gives parties to the agreements approved under 5a relief from operation of the antitrust laws, the exemption is confined to the conduct of collective ratemaking. Several recent U.S. Supreme Court cases indicate that qualified immunity or exemption from any antitrust mandate cannot be lightly construed. Indeed an exemption must be both specific and born of apparent and legislatively recognized public need. Immunity will no longer be implied unless there are very unique circumstances involving an exhaustive regulations inquiry where the regulatory body is making a competitive assessment, such as certain federal licensing programs.\textsuperscript{29} However, because of the specificity of 5a there is no need to evaluate factors of implied immunity. Likewise, decisions like United States v. Otter Tail Power Co.,\textsuperscript{30} Detroit Edison v. Cantor-Seldin,\textsuperscript{31} and Parker v. Brown,\textsuperscript{32} do not directly apply to Reed-Bulwinkle\textsuperscript{33} matters since these cases center on conduct by regulated parties which is outside of the different exemptions at bar. That fact notwithstanding, the case law on antitrust immunity is worth summarizing. Basically, if a governmental process actively provides regulatory input, if periodic assessments of competitive impact are made, and if Congress has directed immunity for specified conduct in a given area, then the private or public entities subjected to this process shall not be subjected to antitrust enforcement for non-predatory conduct.

It is as clear that the antitrust laws apply to predatory conduct of motor common carriers\textsuperscript{34} as it is that they do not apply to conduct enumerated in specified agreements submitted to the Interstate Commerce Commission and approved by that body. This approval is made after assessing the National Transportation Policy,\textsuperscript{35} part of which requires an assessment of anti-competitive considerations.\textsuperscript{36} If there is apparent discord between the antitrust laws and the specified immunity, the Act merely grants a competent administrative agency the authority to resolve the conflict. This is a fundamental premise of primary jurisdiction. A recent decision has restated this


\textsuperscript{29} 42 U.S.C. § 2135 (1976) is a good example of this phenomenon. It requires pre-licensing antitrust review of applications for licenses to construct or operate a utilization or production facility of nuclear power.


\textsuperscript{31} 428 U.S. 579 (1976).

\textsuperscript{32} 317 U.S. 341 (1943).


\textsuperscript{34} McLean Trucking Co. v. United States, 321 U.S. 67 (1944).


\textsuperscript{36} H.R. REP. No. 1100, 80th Cong., 2d Sess. 1855 (1948).
proposition of exposing regulated carriers to competitive obligations while carefully circumscribing that exposure:

This Act left the Antitrust laws to apply with full force and effect to carriers . . . except as to such joint agreements or arrangements between them as may have been submitted to the ICC and approved by that body upon a finding that by reason of furtherance of National Transportation policy as declared in the Interstate Commerce Act, relief from Antitrust laws should be granted.\textsuperscript{37}

Naturally, courts have made it clear that the immunity does not extend to activity outside of approved agreement functions. For example, in \textit{Baltimore and Ohio Railroad v. New York, New Haven and Hartford Railway},\textsuperscript{38} the Esch Car Service Act, when it directed the railroads to get together to establish reasonable rules and regulations for the interchange of freight cars, simply authorized the railroads to establish joint rates. It may have immunized them from a charge of entering into price-fixing agreements illegal per se, but it did not protect other activities proscribed by the Antitrust laws.\textsuperscript{39}

The Interstate Commerce Commission is directed to approve only those agreements that come within the criteria set out in the Act, though when it does so, that immunity is complete, if mandated by legislation. In \textit{Riss & Co. v. Association of American Railroads},\textsuperscript{40} the Court confined the parameters of approved agreement: "We do not think the Act or any agreement which has been approved under it can be construed as authorizing the use of . . . practices that eliminate competition."\textsuperscript{41} The Court finishes the qualification with this language:

A joint act, if combined with the unlawful intent of eliminating a competitor would fall outside of the immunity granted by 49 U.S.C. 5b(9) . . . Antitrust immunity . . . designed to protect ordinary ratemaking in the course of regular business so as to adjust to changing costs and to meet the challenges of outside competition. The protection of 5b(9) could not extend to the use of the power to set rates in concert as part of a plan or conspiracy to eliminate competition.\textsuperscript{43}

Independent action can also be seen as part of the legal basic standard for competitive assessment. The Reed-Bulwinkle Act\textsuperscript{44} preserves the potential of competition in guaranteeing the right of individual action. "The right of independent action is paramount to maintaining the integrity of the

\textsuperscript{37} Motor Carrier Traffic Ass'n. v. United States, 559 F.2d 1251, 1253 (4th Cir. 1977).
\textsuperscript{39} Id. at 740.
\textsuperscript{41} Id. at 361.
\textsuperscript{43} Riss & Co. v. Association of Am. R.R., 170 F. Supp. 354, 366 (D.D.C. 1959) (emphasis added). These are still uniform standards. However, since there are no "practices that eliminate competition" or "plans or conspiracy" alleged, the standards raise no problem in this case.
\textsuperscript{44} 49 U.S.C.A. § 10706 (West Supp. 1979).
grant of antitrust immunity.\textsuperscript{45} The question of how independent action becomes a part of the regulatory competition is slightly more complex than would first appear. If the regulatory structure provides a competitive format for yardstick competition and efficiency competition, as well as direct contact and private carrier competition, is independent action theoretically unnecessary or merely a sop to antitrust-conscious legislators? The answer to this question is that every regulated industry, even those which are 'completely regulated', e.g., nuclear power generation, contain a mix of regulation as a substitute for competition as well as limited pockets of open-market competition. In the electric utility industry, wholesale-for-resale bulk power exchange pricing is open, providing some competitive pressure, or a pocket of competition. In motor carrier ratemaking, the preservation of independent action provides a similar pocket of competition, though it in no way supplants the regulatory process which is designed to produce the effects of competition while at the same time existing in a regulatory setting.

In 1972, there were 32,922 motor carrier bureau regular and emergency proposals.\textsuperscript{46} The 1973 Annual Report to the ICC stated that the percentage of independent action filings was in the neighborhood of 28%, indicating heavy open market competitive pressure.\textsuperscript{47}

This is particularly significant in light of Motor Carrier Traffic Association v. U.S.\textsuperscript{48} which should stimulate even greater numbers.\textsuperscript{49}

One can conclude that since independent action does present a viable alternative to collective ratemaking, the Commission has actually developed a very sophisticated and effective marketplace which combines open market and regulated activity, in a naturally occurring balance. This is one of the important reasons why the industry enjoys significant organizational diversity. In the Eastern Central Bureau, there are 855 independent common carriers\textsuperscript{50} with the classical income distribution pattern indicative of an organizationally diverse market.\textsuperscript{51}

Further, the Act itself states that the Commission cannot approve an agreement unless there is accorded to each party the full and unrestrained

\textsuperscript{45} Motor Carriers Traffic Ass'n. v. United States, 559 F.2d 1251, 1255 (4th Cir. 1977).
\textsuperscript{46} G. Davis & C. Sherwood, supra note 10, at 73.
\textsuperscript{47} Id., citing RATE BUREAUS AND ORGANIZATIONS ANNUAL REPORT TO THE ICC (1973).
\textsuperscript{48} Motor Carriers Traffic Ass'n. v. United States, 559 F.2d 1251 (4th Cir. 1977).
\textsuperscript{49} Statistics for the Eastern Central region are on par with the industry, independent action amounting to thirty-five to forty-five percent of filings. These statistics are on file at the Commissioner's offices in Washington, D.C. See note 12.
\textsuperscript{50} These statistics are on file at the Commissioner's offices in Washington, D.C. See note 12 supra.
\textsuperscript{51} Central to this article is the concept that if the participants in a given marketplace are organizationally diverse, i.e., of varying sizes, revenue patterns, and ownership forms (publicly held, privately held, family-owned, etc.), an assumption can be made that the marketplace is competitive.
right to take independent action either before or after any determination.\textsuperscript{52}

Furthermore, this right of independent action preserves competition to an extent in that just having the potential for independent action exerts considerable competitive influence.\textsuperscript{53} Looking to the Eastern Central Region, the question of preserving the right of independent action has been closed since the \textit{Motor Carrier Traffic Association}\textsuperscript{54} case.

Therefore, when one views the specific exemption granted by Reed-Bulwinkle,\textsuperscript{55} combined with the standards used by the Interstate Commerce Commission in approving agreements and the preservation of the right of independent action, it seems natural to conclude that the granted exemption has allowed for the creation and maintenance of a competitively healthy marketplace.

On a different point relating to legal standards, the Commission's order speaks specifically of a national transportation policy-antitrust balancing:

[T]he question as to whether or not an agreement is to be approved involves the accommodation and comparative evaluation by the Commission of two policies, the one, the national transportation policy, the other, the antitrust laws.

Under the standard in [section 5a] Congress entrusts to the Commission the task of applying to particular cases the general formula which Congress finds is determinative of the public interest and directs the Commission to determine whether the advantages to the public interest, through furtherance of the national transportation policy, are such as to outweigh the disadvantages to the public interest intended to be guarded against by the antitrust laws.\textsuperscript{56}

As noted earlier, such a policy balance is a matter resolved by Congress and not appropriately before the Commission at this time. However, one must distinguish between the \textit{balancing} required to be employed by the ICC in approving or disapproving agreements, and the initial \textit{balancing} that took place in Congress in granting the immunity in the first place.

In \textit{Georgia v. Pennsylvania Railway},\textsuperscript{57} the Court struck down as illegal collective ratemaking. Congress later formulated the Reed-Bulwinkle Act.\textsuperscript{58} This indicated a recognition that carriers cannot respond to all the duties mandated by the Interstate Commerce Act if they are forced to act in an open market setting. It also indicated that Congress recognized the destructive nature of price competition in this particular industry. Thus, it was


\textsuperscript{54} Motor Carrier Traffic Ass'n v. United States, 559 F.2d 1251 (4th Cir. 1977).


\textsuperscript{57} 324 U.S. 439 (1945).

\textsuperscript{58} Ch. 491, 62 Stat. 472 (1948) (current version at 49 U.S.C.A. § 10706 (West Supp. 1979)).
in the interest of the national transportation policy that an exemption from the antitrust laws be granted.

Frankly, the balancing should not be phrased in terms of open market or antitrust policy versus national transportation policy. Rather, the Commission should recognize the balancing accomplished by Congress in enacting the Reed-Bulwinkle Act,59 which juxtaposed a semi-free market setting against a controlled or regulated marketplace where price competition was no longer a factor and where a competent agency reviews the initial agreements, considering national transportation policy and the competitive policies thereunder. If in a given marketplace, open market forces would produce a desirable result, the ICC ought not approve the agreement either initially or in subsequent review; if a regulatory formulation that excludes price competition appears superior, then the agreement should be approved, at which time the exemption would go into effect.

In Florida East Coast Railway v. United States,60 the court was faced with a "head-on collision" between the antitrust laws and the Interstate Commerce Act. The case involved a merger of the Atlantic Coastline Railway Company and the Seaboard Airline Railway Company. The court stated that "all too much time had been consumed in showing a violation of the antitrust laws and too little time devoted to assessing the 'public interest' expressed in the Interstate Commerce Act."61 In other words, the court was concerned that basic balancing had already been done by Congress, as is the case with section 5a. The Florida court goes on to say:

ICC review involves the review of intricate, expert plenary judgment in a highly specialized area of our economy that has long been subject to direct, precise regulations... for purposes of national transportation policy. Congress has told us that not all restraints and monopolies which violate antitrust laws are bad... The ICC in its wisdom... is to determine which are to be allowed and which are considered bad.62

Further, in Motor Carriers Traffic Association, Inc. v. United States,63 the court said: "Congress directed that the Commission should weigh the conflicting demands of the antitrust laws and the surface transportation system, resolving the same by the application of the standard involving national transportation policy."64

This phraseology is another way of addressing the same question. The Commission is charged to "weigh the conflicting demands..."65

59. Id.
60. 259 F.Supp. 993 (M.D. Fla. 1966).
61. Id. at 997.
62. Id. at 1002.
64. Id. at 1255.
65. Id.
but not the broad policy decisions in initial approval of the agreements, nor indeed, at any point thereafter. This never meant, however, that the Commission should establish a scale and balance the national transportation policy and the antitrust laws in a broad scale review. That was a task done by Congress in the debate surrounding Reed-Bulwinkle, and need not be undertaken in this forum.

III. General Competitive Problems Relating to All Bureaus

Within the last five years, courts and administrative agencies in this country have sought to combine functional powers to assure that the ends of the competitive system are met by means which do not necessarily include price competition. As stated in part II, our economy can only function when the ends of reasonable cost, regulation over entry by market forces or by assessments of public convenience and necessity, maximum efficiency, and innovation are met. In the nonregulated sector of the economy, these goals are attained by periodic private-party or governmental application of the antitrust laws coupled with other "normal" competitive pressures such as potential competition. In the regulated sector of the economy, these goals are met by induced competitive pressures as well as the application of regulatory principles regarding rates and entry to the various regulated industries.

The motor carrier industry is not the first industry which has required the application of both a comprehensive regulatory system and antitrust pressures outside of the regulatory system. In the nuclear power field, Congress declared that the agency which regulates nuclear energy production, today the Nuclear Regulatory Commission, may not grant or issue a permit or license to operate if that granting or issuance would "create a situation inconsistent with the antitrust laws." The NRC recently held that the existence of a regulatory structure does not preclude direct application of antitrust principles to areas not specifically exempted. While this decision may be creating waves in the traditional electric utility world, its import should be no shock to the motor carrier world including the rate bureau structure. Competitive consequences in the motor carrier world have been recognized almost since the beginning of motor carrier transit, and well

68. The next section of this article draws from testimony prepared for a hearing before the Antitrust and Monopoly Subcommittee of the Senate Judiciary Committee. The testimony was not, however, orally presented to the Subcommittee at the scheduled hearing held March 24, 1978.

The Ex Parte No. 297 proceeding does not question the applicability of the antitrust laws to the regulatory system. Instead it seeks to answer some of the questions which the Reed-Bulwinkle Act\footnote{49 U.S.C.A. § 10706 (West Supp. 1979).} left open. These questions are not easily answered, particularly if one simply makes glib reference to boilerplate antitrust considerations. It is clear that outside of the Reed-Bulwinkle Act,\footnote{Id.} collective ratemaking between horizontally-aligned competitors is simply inconsistent with the antitrust laws.\footnote{E.g., United States v. Socony-Vacuum Oil Co., 310 U.S. 150 (1940).} Thus the rate bureaus exist only by virtue of legislative exemption, within a carefully drawn line of immunity which resulted after substantial congressional inquiry.

Many of the fundamental concerns which have been evidenced by the Commission’s order focus on the existence of rate bureaus as well as the right of independent action. Such inquiry seems out of focus based on prior congressional action. Likewise, they appear to focus on the effectiveness of rate bureaus’ capacity to establish reasonable and just rates, in conformity with the mandates of the Interstate Commerce Act.\footnote{49 U.S.C.A. §§ 10101-11916 (West Supp. 1979).} Since this responsibility is historically shared by both the bureaus and the Commission, it too seems unjustified. Nonetheless, as to the legitimacy of the collective ratemaking process and the sustained existence of the rate bureaus, my position is easily clarified.

In the last two years, I have become convinced that the abolition of the rate bureau system would create a grossly anti-competitive situation in the motor carrier industry. The "parade of horribles" that would result is well known in the antitrust field. Major motor common carriers, having the capacity to operate for brief periods of time at a cost formula which does not reflect a reasonable rate of return would soon eliminate marginal competitors in a horizontally organizationally diverse marketplace. These eliminations would then be followed by rapid incremental increases in price. A leveling-off would occur in which we would find massive integration at both the horizontal and vertical levels in the motor carrier marketplace. The resultant effect would be a pure oligopoly market setting with little opportunity for systemic or functional coordination or competition and maximum opportunity for over-pricing, inefficiency, and the like. The chaotic conditions that gave birth to the Motor Carrier Act of 1935\footnote{Ch. 498, 49 Stat. 543 (originally codified at 49 U.S.C. §§ 301-327 (1976); now codified in scattered sections of 49 U.S.C.A. (West Supp. 1979)).} would not be duplicated, but
instead would be substituted with the onerous price consequences of unjustified market power. Maintenance of the rate bureau system insures that market dominance and the power to exclude competitors by reducing prices in the margin will not be a factor in the diminution of organizational diversity. This is one of the fundamental reasons for regulation and it has not ceased to exist in the motor carrier world.

The second fundamental question, assuming the rate bureaus continue to exist, is whether those bureaus have the technical capacity to produce efficient rates which are in fact related to the variable cost factors that the law requires. Again, after two years of observation of the motor carrier industry. I have come to the conclusion that the rate bureaus are efficient professional organizations which have the capacity to produce rates which are related to cost plus a reasonable profit. Perhaps indicative of the success ratio, in terms of the antitrust laws, are the 1976 statistics from the Interstate Commerce Commission’s annual report relating to concentration in the motor carrier industry. This report concludes that the industry is non-concentrated and enjoys significant intramodal competition as well as intermodal competition. That would not exist if motor freight common carriers utilizing collective ratemaking had been working under a system of cost-excessive tariffs.

The process of ratemaking is an extremely complex process. The function of the rate bureaus in establishing the basic data which becomes the predicate for the approved tariff is vital to the regulated structure. Further, it would be untrue to state that the Interstate Commerce Commission has the technological hardware or legislative mandate to undertake the ratemaking process. The bureaus are ideally constituted to perform this function, and do so adequately.

A final concern of matters common to all bureaus impacting tangentially on this proceeding involves bureau protest of independent action. In light of the correct reading of the independent action portion of section 5a found in the Motor Carrier Traffic Association case, it seems clear that bureaus may not protest independent action filings. To do so directly would violate the Fourth Circuit order and to do so indirectly would tempt the application of the sham exception to the Noerr-Pennington doctrine.

IV. ACADEMIC ANALYSIS AND FURTHER STANDARDS

Perhaps the most well-known 'legal economist' in the antitrust area today is Richard A. Posner. In a law review article published in the University of Chicago Law Review in 1971, Posner articulated certain market characteristics which he believed were indicative of an unhealthy market setting. It should be noted that the article was written for the purpose of giving the United States Department of Justice, Antitrust Division; some guidelines for prosecution. These characteristics are not necessarily unique to the nonregulated marketplace. However, like the characteristics enumerated in the introduction of this article, they do form a useful guideline for the Commission's assessment of market ''healthiness.''' As you will recall, I stated that if a marketplace was organizationally diverse, if there was cost related to specific output plus reasonable rate of return, logical control over entry, and an innovative and efficient market setting, then the marketplace was healthy regardless of the balance between regulatory pressure and open market pressures.

In his article, Posner sets out negative market characteristics that are indicative of market collusion in an unhealthy context. The characteristics are: few firms accounting for most sales, inelastic demand at the competitive price, slow entry, standard product, many customers, ''the members of the cartel sell at the same level in the chain of distribution,'' price competition appears more important than other forms of competition, there is a high ratio of fixed to variable costs, demand is static or declining over time, and finally, sealed bidding. Posner suggests that when the market structure reflects these phenomena, the marketplace is in difficult straits. Taking these factors as applicable to regulated markets a brief look at the Eastern Central marketplace indicates that most of these characteristics do not exist. Indeed, by virtue of the maintenance of collective ratemaking, the marketplace is extremely healthy in terms of the number of firms, the elasticity of demand, entry, the absence of price competition, and finally, by virtue of the collective ratemaking process working in conjunction

81. The following material draws from certain theorists who have expressed opinions on the type of economic regulation discussed in this article.
83. Essentially, since the Commission's task is confined to assessment of market structure and not the specific conduct of collective ratemaking, that being exempt, theorists have been selected who have worked in the structural analysis arena. I in no way suggest that any of these theorists necessarily agree with the original Reed-Bulwinkle balancing which allowed for the collective ratemaking immunity. They are simply chosen because they have provided the public with their own independent notions of market viability, and as to those notions, the Eastern Central market appears almost model in most respects.
84. Posner, supra note 82, at 516-19.
85. Id. at 529.
with the independent action process, there is no problem that would parallel the "sealed bidding" problem which Posner discusses.

Another treatise in the area is the Economic Regulation of Business by Thomas Morgan.86 In the chapter on government regulation and competition, Morgan mentions the Reed-Bulwinkle Act specifically. The mention is brief: "The Reed-Bulwinkle Act, passed in 1948, changed the law in this area to expressly permit "rate bureaus" to discuss and propose rates. Such agreements and discussions leading up to them are immunized from antitrust liability."87

Morgan goes on to ask whether such agreements are desirable and what constructive contribution can be made by allowing for such collective ratemaking. Again, since the resulting market is healthy, I submit that Morgan’s concern is without market justification. While Morgan does not answer these questions, these are the questions asked by the Commission in Question 3 of its main interrogatories in the December 30th Order.88 However, in terms of a straight legal analysis, Morgan leaves little question as to the issue of immunity and the viability of the Reed-Bulwinkle Act.

Another theorist, Charles F. Phillips, Jr., also addresses the question of the exemption to the antitrust laws provided in the Reed-Bulwinkle Act directly. In his text, The Economics of Regulation89 Phillips gives the following small history:

The new law [the Reed-Bulwinkle Act] was attacked as being anti-competitive, leading to monopoly. It was defended by the railroads and some shippers as necessary to prevent ratemaking from becoming chaotic, since rate bureaus provide a forum where all interested parties can be heard before a rate is charged. Nevertheless, because the Act maintained a right of individual action and left shippers free to bring complaints directly to the Commission [footnote omitted] and because both carriers and shippers, particularly in the railroad industry, have exercised their independence and right with growing frequency, rate bureaus are less of a monopolistic devise than many originally feared.90

When one looks at Eastern Central and finds 2,920 dockets filed by the bureau and 1,194 independent actions in a set period in 1977,91 it should be clear from the numbers that the impact of independent action is significant indeed.92 This is particularly true in view of success ratios for

87. Id. (emphasis supplied).
88. 43 Fed. Reg. 1666, 1667 (1978). Question three asks "[W]hether the benefits the agreement confers on the public interest from the standpoint of the national transportation policy outweigh the harm the agreement will do to the public interest intended to be protected by the antitrust laws."
90. Id. at 469 (emphasis added).
91. These statements are on file at the Commissioner’s offices in Washington, D.C. See note 12 supra.
92. Id.
independent action filings on the order of eighty to ninety percent.93

Of the commentators that have studied the area of government regulation as it applies to the various regulated industries, David Boies and Paul R. Verkuil have recently published a text, Public Control of Business,94 which provides various economic theories and rationales for the idea of regulated collective ratemaking.

As to the specific questions raised by Ex Parte 297 and the Reed-Bulwinkle Act, Boies and Verkuil are blunt in their language. They conclude that the congressional resolution surrounding 49 U.S.C. § 11702 resolves the question of antitrust liability that was raised in the Georgia v. Pennsylvania Railroad95 decision. Reading the Georgia case literally, Boies and Verkuil find total antitrust immunity with only questions of predatory conduct and procedural omissions remaining. They state simply:

Commission approval carries with it relief from the operation of the antitrust laws with respect to conduct of the parties pursuant to the agreement . . . . Several issues remained [after the Reed-Bulwinkle Act], and remain to be worked out. For example, suppose the rate association agreement is not filed with the Commission, and an antitrust complaint arises. . . . Or suppose that the antitrust claim asserts that there is predatory purpose behind the collective ratemaking agreements approved by the Commission that exceeds the scope of § 5b(9) exemption.96

Following the theory of Boies and Verkuil, if an agreement has been approved and if the terms of the agreement are carried out in every detail, then there is no antitrust problem and proceedings such as the one presently underway for reassessment become a futile exercise. This is perhaps too extreme a position in view of the national transportation policy. However, if one reads the language in the Georgia case, the court states "Congress has not given the Commission comparable authority to remove rate fixing combinations from the prohibition contained in the antitrust laws."97 By passage of the Reed-Bulwinkle Act, Congress did give that authority to the Interstate Commerce Commission.98 It did not do so on the stated condition that the Interstate Commerce Commission periodically assess the wisdom of Congress' overall judgment by weighing out the value of regulation and antitrust immunity against the value of antitrust enforcement.99

In the interest of not misleading the reader of this article regarding the position of Boies and Verkuil, as to price regulation and collective ratemak-

93. G. Davis & C. Sherwood, supra note 10, at 75.
94. D. Boies & P. Verkuil, Public Control of Business (1977). The text is becoming the standard casebook at law schools which teach courses in the regulated industries.
96. D. Boies & P. Verkuil, supra note 93, at 826.
99. D. Boies & P. Verkuil, supra note 93, at 826.
ing outside of specific congressional exemptions such as the Reed-Bulwinkle Act, the authors come down very heavily on the side of open market forces. At one point in the text, the authors assert that the effect of collective ratemaking and price regulation which prohibits open market price competition is a negative effect, leading to excess spending, wasteful competition, unnecessary utilization of scarce social resources, possibly undue concentration, and finally, and most fervently, higher consumer costs. The economic theories which the authors use to support this position are stated throughout the text. My personal opinion of this listing is that it is a valid analytical tool.

Looking further at the balancing that must be done, preferably by Congress in matters of national importance such as collective ratemaking, one must recognize that we have competing economic strengths to reconcile. On the one hand, there is the benefit of price competition leading to maximization of resources and certain economies, while on the other hand, regulation over pricing accomplished through collective ratemaking insures a fair rate of return as well as "a reasonable" price being set for consumer purposes. The idea that "open market" competition will result in "cutthroat competition" is one which Boies and Verkuijl find particularly repugnant as too encroached in traditionalist thinking. In certain marketplaces, the authors project that collective ratemaking and price regulation, more likely than not, result in negative effects and will not stave off negative economies. The authors can be read to suggest that collective ratemaking does not assist in the maintenance of a healthy market. "Thus, an examination of other oligopolistic markets, characterized by high fixed costs and perennial excess capacity does not suggest that destructive price wars are likely." However, these conditions—oligopoly, high fixed costs, perennial excess capacity—are not conditions that exist in the trucking industry. While they may exist in the airline industry and other regulated fields, they do not exist in the motor carrier world. Making their point even more firmly, Boies and Verkuijl cite a study entitled The Economics of Competition in Transportation as authority for their proposition on the following rationale: "Steel, automobiles, rayon, copper, and other small numbers industries have no rate bureaus yet cut-throat competition does not exist." I have no complaint with this rationale. Indeed, in those marketplaces where concentration is high and there are clear signs of oligopoly the need for collective ratemaking has come to an end. However, in the motor carrier industry concentration is low, there is no oligopoly setting, the marketplace

100. Id. at 373-76.
101. Id. at 375.
103. Id. at 251.
is diverse, and the need for some control over the ascertaining of certain minimum price is high. When this is balanced with the possibility of independent action, the Boies and Verkuil analysis becomes applicable in the inverse.

In an industry where there is no evidence of oligopoly, where there are efficiency obligations which are set out in detail by several government agencies; where there is ease of entry, no high fixed cost, little perennial excess capacity, and very real public service obligations, the maintenance of a collective ratemaking system (with certain competitive controls such as independent action) guarantees the maintenance of the organizational diversity of that industry. The cessation of collective price-making capabilities will sound the beginning of the initiation of oligopoly, concentration, and the diminution of organizational diversity. In any event, it is safe to say that even those of the deregulation ilk have concluded that if Congress has gone through the balancing process and determined that the motor carrier industry would benefit from collective ratemaking when that collective ratemaking is balanced by independent action, so long as there is oversight by a competent administrative agency, Congress does not intend for that agency to redo that balancing every few years.

A. MARKET STRUCTURE AND THEORY

At this juncture a few thoughts are in order on the marketplace in question. The analysis of Boies and Verkuil regarding the viability of concentrated regulated marketplaces when collective ratemaking exists and the inverse analysis applied to organizationally diverse marketplaces become particularly valid in light of the classical product and geographic market parameters that exist in the motor carrier industry. While it is difficult to come up with a market structure analysis for rate bureaus since a rate bureau is not a competitor dealing in specific service or product that is presently under antitrust scrutiny, a general market analysis can be done simply by looking at the various participants who exist within that structure. The product that is involved in this case is actually ratemaking. The individual motor common carriers that are involved in the collective ratemaking process pursuant to a section 5a exemption are not subject to individual liability for specific collective conduct under the antitrust laws so long as that immunity is in effect. Thus, their conduct is, for all practical purposes, safe from prosecution, though subject to analysis. Naturally, if the Commission should find that any particular rate bureau agreement is no longer valid, then the possibilities of antitrust liability commence with that finding.

As to the market analysis itself, in the Eastern Central region there are, as mentioned earlier, almost twelve hundred market participants who compete at various levels. Many of the market participants are small, privately-held corporations, and a good number of the market participants are large,
publicly-held corporations. There are family corporations, independent partnerships, and almost every other form of corporate ownership imaginable operating common carriers in the region. This diversity itself leads to yardstick competition. In addition to the large numbers and varying organizational structure of the market participants, there is fluctuation in terms of yield, profit, revenue, and other easily identifiable economic indicators.104 Almost every commentator will agree that there is complete ease of entry in terms of financial acquisition, entry only being restricted by regulatory factors.

Thus the product market looks something like this: a large number of organizationally diverse independent competitors whose entry is controlled by regulation, who have price constraints established only by theories of reasonableness, and price creation methodologies that range from collective ratemaking by a sophisticated non-coercive organization to complete independent action. This marketplace is almost ideal in terms of the textbook definitions of perfect competition. There are a large number of buyers and sellers, a good spread of market knowledge, incentives for innovation and efficiency, little cut-throat pricing, but price controls which are guaranteed (by the Interstate Commerce Act) to produce “reasonable rates.”105 In this market setting, the need for preservation of the collective ratemaking mechanism with control over rate increases as a matter of regulatory obligation and control over rate decreases as a matter of carrier or shipper initiative or Commission initiative seems apparent.

In his text, Antitrust Analysis,106 Professor Areeda lists certain factors which are usually stated as a traditional rationale for the preservation of a cartel. As a general notion, the cartel is supposed to prevent cut-throat competition, avoid concentration, reduce market uncertainty, finance desirable activities, protect quality from debasement, and allow for preservation of needed capacity or service (possibly the notion of public utility obligations) and for orderly contraction.107 The Areeda listing of factors which suggest the maintenance of a cartel do not necessarily suggest that cartelization, either private cartelization through international agreements or cartelization by domestic governmental regulation, will invariably produce a viable marketplace such as that which exists in the Eastern Central region.108 However, such prognostication is unnecessary when a viable

104. These conclusions are drawn from statements on file at the Commissioner’s offices in Washington, D.C. See note 12 supra.
107. Id. at 269-75.
108. Indeed, it should be noted in discussing the listing given by Professor Areeda that his textual material questions the typical economic rationalization for the maintenance of a cartel. Most of the factors cited by Areeda can be interpreted in a number of different ways. In his textbook at pages 269-275, Areeda suggests that these traditional economic reasons frequently do not result
competitive marketplace exists and has as one of its essential components collective ratemaking.

Since it is clear that Congress has intended that the specific act of collective ratemaking be immunized from antitrust scrutiny after the approval of an agreement by the Interstate Commerce Commission,\(^{109}\) then subsequent review of the marketplace, or of market participants, must be directed away from the phenomenon of collaboration in a negative context and directed to the structure of the industry itself. Naturally, this is done with the caveat that if the activity becomes predatory, liability might attach. That caution aside, structural analysis of the marketplace is the function of the Interstate Commerce Commission and is the only proper purpose of Ex Parte 297.

**B. DIRECT APPLICATION OF THEORY**

Antitrust analysis under the Sherman Act,\(^{110}\) as well as analysis under the Clayton Act\(^ {111}\) and the other antitrust laws, always included the following components: first, an assessment of the parties who are or might be subject to the antitrust laws; second, an analysis of the conduct or activity that is involved; third, if there is no conduct or activity, an assessment of the structure of the marketplace; fourth, an assessment of the specific parameters of the geographical market; fifth, if structure is involved, as opposed to conduct, an assessment of that structure in terms of past, present, and future market effect.

For the participants of the collective ratemaking process, the analysis is not complex. The participants in the marketplace are the motor freight common carriers. The conduct that is involved is collective ratemaking. That conduct is immune from antitrust scrutiny as a matter of law. Since this conduct is immune, the structure of the marketplace itself can be analyzed. The marketplace is the market of public transportation services provided by the motor freight common carriers, and the geographic market is the Eastern Central Region. The market impact or market effect of the particular process which is involved can be analyzed by viewing the existing structure of the marketplace, as has been done in this article. The market reveals organizational diversity, yardstick competition, competitive coordination, service efficiency, and reasonable rates as mandated by law—in other words, the earmarks of a viable marketplace.

It is always dangerous to put the cart before the horse and argue that

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in optimal market conditions. However, in the motor carrier world, and particularly in the Eastern Central region, the result of the collective action has been positive and substantiates some of the traditional economic learning regarding the creation of cartels.


since the marketplace appears to be healthy, therefore the conduct which is taking place is healthy as well. However that is exactly the kind of reasoning that must be undertaken in this proceeding. If alternative competitive methodologies are going to be imposed on the motor carrier industry, particularly in the area of ratemaking, then Congress must once again decide the question of the meaning of section 5a of the Interstate Commerce Act. Until such time as Congress chooses to do that, the Commission is left with analyzing the effect of carrying out Congress’ plan regarding collective ratemaking.

V. Final Thoughts on Market Pressure and Conclusion

Viewing the specific regulations which apply to collective ratemaking and the immunity that applies to that process, one must keep in mind the obligations of any carrier who joins a particular tariff agreement. The public service burden which is placed on a common carrier is part of the market analysis that must be used in assessing the overall viability of the marketplace.\footnote{112} The regulated common carrier who is a participant in the rate bureau is subjected to these regulatory pressures, as well as being subjected to other competitive forces.

In terms of independent action as a competitive force, it should be stressed that the success of independent action filings is considerable (approximately ninety percent).\footnote{113} The shipping public, in the year 1972, incurred over a hundred million dollars in expenses for transportation services pursuant to independent action filings. This is more than ten percent of the total expenses incurred under all tariffs.\footnote{114}

Beyond independent action as a competitive force, it would be error not to take into account other natural competitive forces which have a conclusive impact on the relevant market participants. As was suggested earlier, the number of private carriers and contract carriers is constantly growing. Likewise, shippers who have not elected to use private carriage maintain the capacity to utilize private carriage should the rates created by the collective ratemaking process become excessive. On the same plane, common carriers who do not belong to tariff bureaus exert a competitive force that has rarely been dealt with in the literature in this field. Further, shipper involvement in the ratemaking process, whether by direct participation in a bureau or by shipper-created information which is fed into the technological systems of the bureaus, form a balance in the collective decisionmaking process itself.

\footnote{112} See, e.g., Ex Parte No. MC-77 (Sub-No.2), Restrictions on Service by Motor Common Carriers, 126 M.C.C. 303 (1977), and 129 M.C.C. 71 (1978).
\footnote{113} G. Davis & C. Sherwood, supra note 10, at 75.
\footnote{114} Id. at 77.
The competitive forces just enumerated form those pockets of competition mentioned earlier which, along with the regulatory competitive pressure, have created a viable marketplace. While it is clear that having a competitive and healthy marketplace is part of the national transportation policy, that "does not mean that all possible methods of competing in the economic process must be tolerated nor that all private economic regulations should be prohibited."115

The majority of economic theorists discussed above take the position that price-fixing and collective ratemaking are basically anticompetitive methodologies which do not result in satisfaction of public interest obligations. Recognizing that the theorists, among them Areeda, Boies and Verkuil, and Posner, have this economic-political philosophy regarding price-fixing, and recognizing further that most of their theory is formulated for non-regulated markets, it is necessary to justify why my conclusions are as they are. I have concluded that the marketplace which exists in the Eastern Central region is a viable and healthy marketplace. My conclusion is based on the fact that the market as it presently exists, outside of any theoretical permutations regarding economic structure, has a sufficient number of organizationally diverse carriers and good mix in ownership patterns. The cost-to-consumer, efficiency, and innovation assessments are all positive.

Could it be that the theory projected by the principal legal and economic experts in the trade regulation field is improper? I would contend that while the theory projected by Professor Areeda and others in the field is valid and accurate, it simply cannot be imposed on a regulated but organizationally diverse marketplace comprised of numerous participants. That is to say, theories of cartelization and price-fixing apply almost solely to those marketplaces confronted with oligopoly or situations where a single entity has achieved dominance or monopoly. In those markets where there is a large number of market participants, these theories are not uniformly applicable. A recent study by Glaskowsky, O'Neil and Hudson on motor carrier regulations has concluded that, "Views regarding effective marketplace competition are wholly pragmatic. Workable economic theories of motor carrier transport competition are tested and proved in the marketplace, and nowhere else."116 The Glaskowsky study goes on to note:

There is no question that there exists a fundamental policy conflict between the original antitrust policies concerning collective ratemaking actions and the transportation needs of the economy. The record is clear that resolution of this conflict in favor of partial carrier relief from the antitrust laws was reached after

115. FORTMAN, THEORY OF COMPETITION POLICY 246 (1966).
extremely thoughtful and thorough consideration of the issue. The record shows that no alternative exists which would adequately satisfy the market information needs of the shipping public. The potential for abuse of the immunity privilege is obvious, however, so it's necessary that collective activities be closely monitored to insure strict compliance with high standards of concern for the public interest.117

This close monitoring to which Glaskowsky refers is what I have called a periodic assessment of market structure, but not of immunized conduct.

The legal requirements which follow from section 5, part a(9)118 regarding antitrust immunity, are clear. The law simply provides that if an approved agreement is enforced, then antitrust immunity shall attach to the process of collective ratemaking. That immunity does not prevent periodic administrative review of the market structure which has resulted. Such review is taking place in Ex Parte No. 297. Should the Commission find, based on competent economic data, that the marketplace has become dominated by a single or small group of carriers or that the marketplace is reflective of anticompetitive patterns that redound to the consumer's dramatic disadvantage, then the Interstate Commerce Commission would be justified in taking close examination of the particular agreement that is involved. In the market studied, no such structure appears. It is my hope that the Commission will study each of the various markets in the manner suggested.

117. Id. at 60.
Motor Carrier Regulatory Reform and its Impact on Private Carriers*

WILLIAM H. BORGHESANI**

With your indulgence, I would like to review the important topic of motor carrier regulatory reform and its impact on private carriers. This, of course, is a timely subject, first, because many companies are now making a decision to enter private carriage and, second, because regulatory reform issues are being intensively debated in Washington at this time. There are interrelationships and I hope to detail some of them for you so that you will have a clear view of the setting of this "great debate," if you will, now going on in Washington.

With the main exception of private carriers, interstate for-hire trucking has been regulated by the Interstate Commerce Commission since 1935. Forty-three years have passed and we now have a piercing review of the impact of that regulation on the economy, on regulated carriers, and on shippers. Into the lists have come two contending viewpoints. One is the status quo viewpoint: make no regulatory change. The Motor Carrier Act under which the ICC regulates common and contract carriage has served us well. This status quo viewpoint, entailing as it does massive resistance to any regulatory reform, is embodied principally among the common carriers—particularly the larger regular route general commodity carriers.

At a polar opposite, and representative of the other extreme, are those

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* Based on remarks prepared for presentation at the Annual Meeting of the Private Carrier Division, Texas Motor Transportation Association, Dallas, Texas, November 3, 1978.
who want to eliminate totally all trucking regulation. Sometimes these people are referred to as "deregulators": they believe in wide open competition and in the free play of market forces. This is the "think tank" perspective, espoused by such groups as the American Enterprise Institute for Public Policy Research. Sources high in the Carter administration identify with this view as do certain sources in the Congress; and so also do the Antitrust Division of the Department of Justice and the Council on Wage and Price Stability.

A more moderate stance is being taken by the Interstate Commerce Commission which, paradoxically for a regulatory agency, is in the process of implementing some thirty-nine Task Force recommendations to reform, both from a procedural and a substantive standpoint, motor carrier regulation. This effort to reform is probably the supreme irony of all because rarely have I experienced in Washington a regulatory agency reforming itself by diminishing the total amount of regulation which it imposes over industries under its jurisdiction!

In terms of the claim of total disaster if we have sweeping regulatory reform versus the claim of supreme public good if we do, I am reminded of a story of the young English lieutenant, a recent graduate of the English West Point, Sandhurst. Unfortunately, this gentleman was at the bottom of his class. Shortly after graduation, he was drilling his troops near the cliffs of Dover. He gave the order, "Forward march." The troops marched toward the precipice. Looking deeply troubled, and as the troops approached the brink, a wise old sergeant-major turned to the young lieutenant and said: "Sir, if you don't know how to say 'halt,' at least say 'goodbye'!" And so it is in Washington these days. Some think we are saying goodbye to the regulated trucking industry as we have known it for the past forty-three years. Some think the status quo should be maintained. Others think there is a middle course to regulatory reform. The questions are beginning to be answered now and will be answered in the next few years with responses that will determine the future of the regulated trucking industry. These responses will have and, indeed, are already having a very considerable impact on private carriage.

PRIVATE CARRIAGE AN EMBARRASSMENT

Those who want sweeping regulatory reform and those who want to maintain the status quo as far as regulation is concerned both find the existence and evident phenomenal growth in recent years of private carriage an embarrassment. There is a considerable paradox in this. Those who want to retain the status quo, namely, the larger common carriers, find the existence and growth of private carriage embarrassing, notwithstanding that they could point to it with some advantage in their battle to avoid sweeping
regulatory reform, to wit, "deregulation." Private carriage could be identified as an open market competitor to regulated trucking, which indeed it is. Its growth, in accordance with figures I will cite for you shortly, suggests that it is a very effective response or alternative to deficient common carrier service and high rates. Nevertheless, the regulated carriers are afraid to point to private carriage or its growth because to do so suggests that there may be something wrong in certain quarters with the current regulatory scheme. While the existence and growth of private carriage would be plausile aids to the arguments against sweeping regulatory reform, they also (and here's where the irony lies) constitute to some extent a criticism of the regulatory scheme as it now exists. Thus, according to the status quo lines of reasoning, to point to the growth of private carriage would also be giving aid and comfort to those who want sweeping regulatory reform.

On the other hand, the "deregulators," those who want sweeping regulatory reform, ignore, perhaps deliberately, the dimension of private carriage in the trucking marketplace of the United States. It is no help to them to point out that shippers have a choice. If regulated carriage does not suffice for any reason, free entry into private carriage, without any operating authority or permission of the ICC, is available. Indeed, private carriage is a surrogate regulator so that, arguably, where the ICC fails in its regulation of the common carriers, private carriage succeeds through the normal interplay of market forces.

Further compounding the paradox is the fact that private carriers have to a large extent (and I admit there are exceptions) opted out of this national debate over regulatory reform. One does not see many private carriers lining up on one side or another of the major regulatory reform issues. Most private carriers appear to have chosen not to worry too much about the outcome of the great debate because they are hauling their own traffic. I realize this is an oversimplification, but there is a great deal of truth in it. Indeed, private carriers themselves, by their very judgments to go into and expand private carriage, represent a special free market manifestation of regulatory reform. Ironically, however, these very private carriers all too commonly seem not to appreciate fully the implied criticism of motor carrier regulation that their involvement in private carriage represents.

Private carriers are moving away from common carriage with an ever-quckening pace. No "by-your-leave" is needed from the Congress, the Carter administration, or the Interstate Commerce Commission to do this. Managerial decisions do it. Thus, I submit to you that if we look deeply enough, we'll find that private carriers themselves exemplify a profound manifestation of regulatory reform in terms of increasing dissatisfaction with the way common carrier service is offered and regulated in the United States today. But the kind of regulatory reform private carriers are interested in lies wholly within their own control. This is why we see little, if any,
identification of private carriers with the formal regulatory reform issues as they are being debated today within the Carter administration, the Congress, and, significantly, within the Interstate Commerce Commission itself.

GROWTH OF PRIVATE CARRIAGE

I think some figures are in order which will underscore the dimension of private carriage in the United States today. I certainly don’t want to overwhelm you with statistics, but I do want to leave you with the impression that, as far as the trucking industry is concerned, private carriage dominates. Regulated carriage does not. These figures bear very heavily on the regulatory debate but are not acknowledged by the principal debaters. For example, in American Trucking Trends, 1976 Statistical Supplement,¹ we note that in 1975, the latest statistical year, there were twenty-four and a half million trucks on the road in the United States of all sizes.² But twenty-three and a half million of these vehicles were used by private carriers.³ Interpreting, over ninety-five percent of all trucks on the road that year were utilized by private carriers! Five or less percent were utilized by regulated carriers, common and contract, local and long-distance. When we look at the largest vehicles of five or more axles, called “eighteen wheelers” in the trade, we see that there are just about as many of these trucks used by private carriers as are used by for-hire carriers. It is a one-for-one ratio! If you want to test this, spend a few hours driving on an interstate highway and note the ratio of private trucks to regulated trucks.

In a June 20, 1978, report on issues in regulating interstate motor carriers, the General Accounting Office pointed out that in 1977 there were about 16,600 trucking firms under ICC regulation.⁴ These are common and contract carriers. The same GAO report indicated that there are an estimated 113,000 to 150,000 interstate private carriers,⁵ the private carriers thus outnumbering regulated carriers by more than nine to one. Actually, no one knows the number of interstate private carriers because they are not required to register as such with any regulatory body, but road checks and private surveys confirm the above-100,000 figure for interstate private carriers.

A recently concluded survey, done at decade intervals by the Private Carrier Conference of the American Trucking Associations, showed dra-

² Id. at 20.
³ Id.
⁵ Id.
matic growth in private carriage. Ten years ago 72.6% of private carrier fleets were twenty units and under. Currently, 73.5% are twenty units and over. Fleet size is up 130% in eleven years. Private fleets were found to be covering wider service areas. The number of fleets covering twenty or more states doubled in the decade from 19% to 38.2%. All fleets involved leasing of some type, and the biggest gain was in driver leasing by private carriers. According to the Private Carrier Conference, some 20.7% of all private carrier fleets utilized leased drivers. As the Conference survey pointed out, U.S. private carriage fleets have been a little-known factor in the huge trucking industry.

A 1972 Census of Transportation reflected its estimate that on a total intercity ton mile basis (that is, one ton moved one mile by a truck) including all freight commodities, both private and exempt motor carriers accounted for some 57.9% of the total intercity ton miles moved by truck. The Interstate Commerce Commission, for one, has acknowledged that the bulk of the intercity motor traffic is, therefore, not regulated and has stressed that the enormous extent of unregulated motor carriers represents a continuing competitive challenge to common carriers.

In a very interesting presentation, W.K. Smith stated his belief that there has been a decline in the position of common carrier trucking relative to private and exempt truck carriage. Significantly, he added that the use of private and other forms of nonregulated truck transportation now constitutes the largest share, revenue basis, of intercity freight. Quoting from the Summary of National Transportation Statistics released by the Department of Transportation in its Annual Report in June 1976, he stated that some 26.1 billion dollars were expended for unregulated intercity trucking while some 22.7 billion dollars were expended for regulated intercity trucking.

Are the common carriers concerned? They appear to be. In a 1980 projection survey conducted by the ATA, it was concluded that there is unmistakable evidence that the regular route carriers face their most signifi-

7. Id.
8. Id.
9. Id.
10. Id.
11. Id.
12. Id.
13. Id.
15. Address by W. K. Smith, Vice President of Transportation, General Mills.
16. Id.
17. Ex Parte No. MC-98, New Procedures in Motor Carrier Restructuring Proceedings (Interstate Commerce Comm'n, April 20, 1976), Initial Statement of Regular Common Carrier Confer-
cant and fastest-growing competition in the form of private trucking.\textsuperscript{18} This study showed that shipments under 500 pounds are not significant to private carriers with only 3\% of this traffic moving in private carriage and with no increase projected by 1980.\textsuperscript{19} However, the Common Carrier Conference anticipated that there will be increasing diversion of traffic to private carriage in other weight categories. For example, in the 500 to 5,000 pound category, 8\% moved in private carriage in 1976. This is scheduled to increase to 10\% in 1980, a 25\% increase.\textsuperscript{20} In the 5,000 to 10,000 pound category, the common carriers believe that 13\% of the shipments moved in private carriage in 1976 and that this would grow to 20\% by 1980. This is a 54\% increase.\textsuperscript{21} Shipments weighing over 10,000 pounds moved approximately 24\% in private carriage in 1976. This number would grow to approximately 39\% by 1980. This is a 62\% increase.\textsuperscript{22}

Overall, the common carriers believe that approximately 40\% of available tonnage in 1976 moved in private carriage and that this is slated to go to 52\% in 1980, an increase of 30\%.\textsuperscript{23}

\textbf{ACCOUNTING FOR THE SHIFT}

Why the shift to private carriage? The universal answer is dollars—dollars in terms of direct reductions in costs compared to common carrier rates or dollars in terms of service which may be described as “keeping the customer.” Service and economics vie as the only reasons for this growing movement toward private carriage and away from regulated carriage. Most observers conclude that this shift is symptomatic, that there is something wrong with the way the regulated carriers conduct their business and with the way they are regulated by state and federal agencies.

Most companies do not want to go into private carriage. They are in it because they have to be. They would prefer to rely, to the extent reasonably possible, on regulated carriers to handle their traffic. Transportation is an alien business to them, one they must learn in terms of diversification.

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\item[\textsuperscript{18}]\textit{Id.} at 4.
\item[\textsuperscript{19}]\textit{Id.}
\item[\textsuperscript{20}]\textit{Id.} at 5.
\item[\textsuperscript{21}]\textit{Id.}
\item[\textsuperscript{22}]\textit{Id.}
\item[\textsuperscript{23}]\textit{Id.}
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from the normal primary businesses with which they are familiar. Notwithstanding, even if we had the best regulated trucking system in the world, there still would be a considerable amount of private carriage. No one expects otherwise, but I submit to you that the very dimension of private carriage, its growth trend, exemplifying as it does a shift away from regulated carriage, suggests that those who advocate a serious, nonpartisan examination of the regulatory structure may have sound reasons for endorsing such an examination. Unfortunately, however, all too often the debate becomes clouded with too much propaganda.

Alfred F. Dougherty, Jr., Director of the Bureau of Competition of the Federal Trade Commission, stated, in criticizing the current rate bureau system for fixing common carrier rates, that such a system tends to raise the prices charged through the tariffs on the regulated truckers. He stated that unregulated truck rates in Canada, for example, are about seven percent lower than corresponding rates in the United States. Even regulated carriers that do not belong to rate bureaus have testified that their rates are at least five percent lower than the rates of bureau members. Additionally, case studies examining reasons for shifts by shippers from common to private carriage have often found that the shippers have concluded they can maintain the same service at a lower cost. Dougherty’s views are reflective of one of the principal areas of regulatory reform debate today, namely, the way rate bureaus are administered. At present they are immune from the impact of antitrust laws by virtue of exemptions granted by Congress and sustained by the Interstate Commerce Commission. But the rate bureaus are under deep challenge at the ICC by the Antitrust Division of the Department of Justice; we may see some change here.

Those who argue that the rate bureau concept is an abuse stress that it creates inflated regulated truck rates and this, in turn, creates an economic climate where shippers find it increasingly attractive to switch to private carriage. They argue that if there is no change in the rate bureau concept, shippers having freedom of choice will increasingly move to private carriage, thereby effecting their own version of regulatory reform no matter what the Interstate Commerce Commission does or doesn’t do.

In a practical vein, Joe Sims, a former Deputy Assistant Attorney General, Antitrust Division, Department of Justice, has assailed the rate bureaus. In his view, the regulated trucking industry is a legal cartel. He charged that as a cartel the regulated trucking industry is doing a better job than many “honest-to-gosh cartels” in the most important function of a car-

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...making monopoly profits. He alleged that trucking companies make more money than they would in a competitive market. He cites as support for his view ICC statistics on earnings of Class I motor carriers. In the calendar year ending December 31, 1977, according to the ICC, the return on equity of these carriers averaged 19.66%—up almost 3% from the previous year. It would have been much higher except for the Western District, where carriers only managed, according to Mr. Sims, a 15.95% return on equity. In both the Eastern and Southern Districts, he pointed out that the average return on equity exceeded 20%! In drawing comparisons, he pointed out that domestic trunk airlines have in recent years only been earning about 7%, although they have been doing much better recently. The median for all U.S. industries is generally thought to be somewhere around 14%.27

Moreover, he charged that this 20% rate of return does not include the 13% per year appreciation in the value of certificates—"those four billion dollar guardrails that keep out the rabble and insure high profits for those already in," according to Mr. Sims.28 Whether or not he is correct, I do not know; but I do know that the whole concept of rate bureaus is in for a profound reexamination. Whether their current use will be reaffirmed, modified, or discontinued remains to be seen. But what does not remain to be seen is the reaction of private carriers who are increasing the size of their fleets. Here we see the paradox of the marketplace reforming itself irrespective of what the Department of Justice, the Interstate Commerce Commission, and the regulated trucking industry do.

As I see it, what I have said so far and the figures I have quoted to you underscore the soundness of the decision of many companies to commence in a very substantial way proprietary fleet operations. As a result of a recent survey, a typical large company has concluded that about forty million dollars was spent on regulated truck transportation. But with the establishment of a transportation division, private carriage would offer this company a 15% reduction from the prevailing common carrier rates. This discount is acknowledged to be approximately equal to the sum of the common carriers' marginal profit, administrative, and sales expenses. By providing service equivalent to or better than that offered by commercial carriers, private carriage would supplant 20% of the company's estimated commercial truck traffic during the first year of operations and, selectively, increase penetration in future years to a rate of 30 to 40%. Relating this 30 to 40% figure to the 1976 survey figure of forty million dollars, and this no

26. Id.
27. Id.
28. Id.
doubt will increase, you see exemplified in one company the very shift of traffic for economic and service reasons that I have been talking about.

**Driver Unions Oppose Reform**

It may be difficult to accept that there are bureaucrats in Washington who actually want to reduce the amount of regulation which they impose on American industry. But this is true today. Here we have another irony. Those in industry who benefit from regulation because of its limitation on competition resist a reduction in the quantity of regulatory burdens because to the extent these burdens are reduced, competition is increased. This resistance to reform is not only true among the trucking companies themselves, but it is also true of the driver unions, principally the Teamster union. To this degree, labor and management in the regulated trucking industry see eye to eye and both are on the defensive about any significant measure of regulatory reform which would have the impact of increasing competition and reducing union driver membership.

Recently, Frank Fitzsimmons, the President of the International Brotherhood of the Teamsters, publicly berated the ICC by saying: "Can you imagine, these bureaucrats in Washington are actually trying to reduce regulation in the trucking industry!" As some people see it, Frank Fitzsimmons is being forced to bargain with the Blackbeard of regulatory reform while the regulated trucking industry is walking the "deregulatory" planks.

Regardless of whether this is true or not, we must acknowledge that the Teamsters are a potent force in the regulated trucking industry and that their bargaining prowess has an impact on private carriage. As you know, private carriers as such are not a party to the National Master Freight Agreement and will not be sitting around the bargaining table in the next few months in an attempt to negotiate another three year Master Freight Agreement. To this extent private carriers have more freedom and a little immunity from the economic impact of such bargaining. Moreover, even where private carriers use Teamster drivers, they negotiate independently White Paper contracts that are tailored to their own needs and which differ in many respects in terms of economics and working rules from the National Master Freight Agreement.

There is, however, an overriding irony because, to the extent that the Teamsters are successful every three years in forcing up the wage and fringe benefit levels (and I might add paragnostically that Mr. Fitzsimmons is looking for a forty percent increase this time around) Teamsters "improve," if I can use that word, the economic climate for private carriage. Private carriers have a better control over their costs and when the tariff rates begin to reflect the increases bargained with the regulated trucking industry by the

IBT, it becomes all the more economically attractive for shippers to accelerate the shift toward private carriage and away from regulated carriage. So to this extent, the very near-term success of the Teamsters in raising wage and fringe benefits also may be adjudged in a parallel sense a long-term failure! This is privately admitted by certain Teamster officials who, although they express concern about the growth of private carriage, are candid enough to admit that they are a principal contributor to this very growth.

Recent reports indicate that the number of truck drivers in the 2.4 million-member Teamsters union has fallen to about 300,000 at present, down perhaps 25% from a decade ago.\(^\text{30}\) The union’s top negotiators clearly see this trend. Some of this decline in Teamster driver membership may be attributed to the fact that the percentage of the nation’s freight hauled by predominantly nonunion irregular route carriers rose from 24.5% in 1965 to 28% in 1976. During the same period, the share of freight hauled by highly-unionized, regular route carriers fell from 34 to 26.5%. But also figuring into this equation is the growth of private carriage with nonunion or non-Teamsters’ union drivers being utilized. The IBT’s top negotiators clearly see this trend.\(^\text{31}\)

In 1976, the Teamsters won wage and benefit increases totalling 35% in the Master Freight Agreement that expired last March 31, and the drivers now earn an average of $25,000 to $30,000 a year. “They are making a lot of money, and they know it,” says Roy L. Williams, Chairman of the union’s central conference and a key national negotiator. Instead of money, he says, “This year the emphasis is going to be on getting more free time.”\(^\text{32}\) This will be in the form of longer vacations and fewer hours at the wheel for over-the-road drivers. Rest assured that if this is the goal, it will be more time off for the same amount of money with ever-increasing costs to all kinds of carriers. So money it is and more of it!

**Driver Leasing Accelerating Growth of Private Carriage**

Enhancing still further the increasingly attractive economic environment, driver leasing is accelerating the growth of private carriage. This service industry has been growing very rapidly. It is rare today for a company that decides to go into private carriage not also to give serious consideration to the concept of leasing drivers who would remain for payroll and labor relations purposes as employees of a driver leasing company, but be utilized in a day-to-day sense by a private carrier as would directly-employed drivers. Many driver leasing companies can offer very expert labor relations counseling and are potent negotiators when it comes to dealing

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\(^{30}\) _Business Week_, Aug. 21, 1978, at 86.

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with any driver union. This translates into an economic advantage. By using such driver leasing companies, many private carriers have found that they achieve an effective labor relations advantage while at the same time having the benefit of private carriage. In a unionized driver situation, leasing tends to make for labor relations harmony and this, in turn, has both tangible (or measurable) and intangible economic advantages. Sometimes drivers can be leased more cheaply than they can be directly employed, even when the wage scales are identical, because of negotiated work rules and savings in overhead or administrative expense. There are fewer labor disruptions and, frequently, there is less driver turnover. Moreover, many private carriers are leasing non-union or non-Teamsters' union drivers. This also translates into dollars, efficiency, and smooth operations and constitutes a parallel inducement to private carriage expansion.

Just what will happen with respect to the upcoming National Master Freight Agreement negotiations is anybody's guess at this time. The Carter administration is really up against it with regard to inflationary factors. The Teamsters' negotiation is regarded as the key union wage pact for 1979 as far as inflationary implications are concerned. In this, too, there is a paradox because Frank Fitzsimmons is certainly a persona non grata at the White House. This is particularly nettlesome to a man of such power. Mutual acceptance is the usual badge of honor in Washington among the peerage of the powerful. As a result of the government's pension investigations, particularly as regards the central states trust fund, the Teamsters have had little to do with Labor Secretary Ray Marshall, and the White House has publicly shunned Teamster President Frank Fitzsimmons. The consequence has been an almost total absence of any coherent labor relations policy toward the upcoming trucking negotiations. As one administration official is reported to have said, "How the hell are you going to get a settlement with the Teamsters when Fitz wants an invitation to the White House and Marshall wants to send him to jail?" 33

CONCLUDING OBSERVATIONS

May I offer you a few concluding observations. Whether they will be proven true in the future remains for the future to tell us.

First, private carriage is here to stay. If, for whatever reason, a company enters private carriage, it will probably stay in it. This will be true no matter what degree of regulatory reform we get, if any, which might erode the economic basis for going into private carriage in the first place. Once companies make the commitment to private carriage and structure their operations around it, there is scant likelihood that they will ever phase it out notwithstanding any change in the economic climate.

Second, private carriage will continue to grow disproportionately to the growth of the gross national product if some changes are not made in the regulatory scene. Moreover, in the broadest sense, no matter what happens, private carriage will also be a substitute regulator or aid to direct regulation of the trucking industry by the Interstate Commerce Commission. This, however, is no reason to be complacent and, although private carriers in a special sense may be opting out of the regulatory reform debate, they still will be impacted by the consequences of this debate.

Third, the proprietary fleet will be recognized as a national resource. I have already given you the figures and dimension of this private fleet. The idea that the common carrier system is the backbone of the national transportation system must be concluded to be a myth. Indeed, a substantial argument can be made that unregulated motor carriage, principally private carriage, constitutes the backbone of the national transportation system. This in turn suggests that national policies should take this into account. I think they will.

Fourth, there are growing pressures to increase competition via regulatory reform. One source of these pressures is the Carter administration. If the Teamsters try to get too much, President Carter will probably accelerate the regulatory reform pace by introducing more competition in the trucking industry. This, in turn, would give the Teamsters pause because when this happens, Teamster driver membership will decline still further. Another source of this pressure to increase competition is inflation itself. There is a strong move within the federal government to increase competition generally in all industries to shake out the alleged "regulatory fat." This process is thought to be anti-inflationary and should not be discounted as a potent factor heating up the regulatory reform debate.

Fifth, another factor, quite apart from the others, is the growing resentment against the layering of regulation on American industry and the costs which are involved in meeting these regulatory requirements. This, of course, is broader than trucking regulation, but trucking regulation is caught up in this grassroots movement. It is influencing the people in Washington very heavily to minimize or do away with, wherever possible, the ever-growing heap of regulations imposed on business. This is a potent force which in my opinion will continue to grow in dimension and will have telling effects.

Sixth, still another factor is Senator Kennedy. As Chairman of the Senate Subcommittee on Antitrust and as the future Chairman of the Senate Judiciary Committee, he is an enormously powerful factor. He has been holding hearings which have been highly critical of the regulated trucking industry. Alone or in combination with the other factors, Senator Kennedy cannot be dismissed and must be recognized as having an increasingly potent impact in the regulatory reform debate.
Seventh, we of course have the Antitrust Division of the Department of Justice. I have previously spoken about its activities. Such activities are increasing and the Division is participating in ICC proceedings when regulatory reform issues are being considered. The Antitrust Division is very pro-competition and wants to reduce the amount of regulation or otherwise increase the alternatives to the use of regulated industry service. This has already been achieved in the telephone industry.

Eighth, we have the growing impact of airline deregulation. We all know the growth in the airline passenger traffic occasioned by the so-called "discount" fares. There is increasing movement at the CAB to deregulate the airline industry still further. This, in turn, is generating more momentum and intensifying the trucking industry regulatory reform debate. I am not making a value judgment on the comparison. I am simply suggesting that it is a contributing factor which proponents of regulatory reform cite as at least partial proof of the effects of competition in lowering rates.

Last, but not least, is the activity of the Interstate Commerce Commission itself. As I said earlier in my remarks, the ICC is doing what regulatory bodies rarely do by trying to reduce the amount of regulation on the industry it regulates. This has been done under the recent chairmanship of A. Daniel O'Neal. At present the ICC is down to six commissioners, and the chances are that the Commission make-up will increasingly reflect the regulatory reform views of Chairman O'Neal. He has already taken many steps suggested by the ICC Task Force on regulatory reform and no doubt will be taking more in the future. To a great degree, the Carter administration and the Congress are looking to Chairman O'Neal to continue to initiate regulatory reform measures.

Noting that one should be wary of analogies, I still cannot help thinking of the telephone industry. Ten years ago AT&T and the Bell System had an absolute monopoly on telephone equipment and service used by all of us in the territories they serve. An unknown man from Dallas, Tom Carter, approached the courts in Texas and the Federal Communications Commission in Washington, asking that his Carterphone be allowed to be used by people who had mobile telephones in their cars so that they could talk to their homes and offices over Bell System lines.

The reaction of the Bell System was one of massive resistance and not one of minor accommodation. By opposing big, the Bell System lost big because ten years later, Bell had lost its monopoly on telephone equipment. You are now able to buy for your home and for your office any kind of telephone equipment you choose. The opportunity to make a minor accommodation with Tom Carter would have prevented the collapse of the telephone equipment monopoly. The Bell System would still have, with the exception of a minor accommodation for the Carterphone, the ability to re-
quire that you lease Bell Telephone equipment for your home and for your office.

In a parallel vein, the Bell System made the same mistake of massive resistance to private line competition. A little entrepreneur proposed a private line microwave system between Chicago and St. Louis about ten years ago. Young Jack Goeken was rebuffed by the Bell System which said he would be skimming its cream and which resisted the licensing of such a system at the Federal Communications Commission. Here again the policy of massive resistance was a grossly defective management judgment by AT&T. It lost and has since lost all the ensuing Commission and court battles dealing with competition with new common carriers and with unregulated businesses that wanted to sell telephone equipment to users throughout the country.

Ten years later, we have the paradox of AT&T and the Bell System on the defensive before a Congress which now seeks to codify competition as a way of life within the telephone industry. The Bell System brought this on itself by a policy of massive resistance to even the slightest change. It never reached, early on, as it should have, an accommodation with change.

At its core, the problem was a failure of regulated industry leadership. Good leadership recognizes the temper of the times and accommodates change without doing fundamental violence to its own interests. We think this experience may offer some parallel insights into the current status of the regulated trucking industry today. Whether the trucking industry will, with its leadership, have the wisdom and the ability to progress with the tide of change, shape and contain it, adapt to it where necessary, and then progress to ever-increasing growth, is an unanswered question.

I suggest, however, that if the massive resistance to change of any dimension is maintained, we will see more change than we need and the regulated trucking industry, unnecessarily, will continue defaulting to private carriage.