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I. INTRODUCTION

Transportation has been subjected to profound technological changes during the last two centuries. From the steam engine in the 19th century to container transport in the post World War II era, new forms of technology have enabled the transportation industry to play a key role in society and the national economy. Railroads and steamboats extended markets beyond the local boundaries and made the division of labor possible and profitable, first on a national and finally on an international level. Urban mass transportation favored the separation of home and working place, of labor and family which, in turn, contributed to deep structural changes in modern society. The availability of bus, train, and airplane transportation is fundamentally important to the mobility of mankind.

In the legal framework of transportation, these dramatic changes are reflected by the fading away of the common law and the implementation of a voluminous body of legislative and regulatory law. Modern legislation, however, turns on old concepts such as the distinction between private and common carriers. This distinction is fundamental in the common law of
transportation and in the modern regulatory statutes.

The purpose of this article is to determine to what extent the traditional features of the law of common carriers survive in modern legislation and to what extent they have yielded to new rules specific to the various transportation modes. The first section of this analysis investigates the original common carrier concept, the policies behind it, and the reasons for its supersession by modern legislation. The second section discusses the extent to which the historical common core survives in the various statutes regulating transportation modes, in particular railroads, airplanes and ocean vessels. Finally, the third section discusses the role of the common carrier in the era of deregulation. The question posed is whether the fading away of legislative interference will strengthen the role of the common law rules and whether decontrol will result in unification or further disintegration of transportation law into branches paralleling the various modes of transportation.

II. THE COMMON CARRIER CONCEPT AT COMMON LAW

Historically, a common carrier has been defined as "... any man undertaking for hire to carry the goods of all persons indifferently," whether by land or by water. Under common law, the common carrier, unlike the private carrier is:

1. under a duty to contract with and to serve all who apply; and
2. like an insurer, he is strictly liable for all damage to or loss of goods except in exceptional cases, such as an act of God or of the public enemy. Even in such a case negligent behavior makes the carrier liable.

There are certain corollaries to these primary duties, namely that the service must be reasonably adequate and rendered upon reasonable terms, especially at a reasonable price.

The particular legal burden of common carriers contrasts with basic notions of a free enterprise economy and raises a question as to why common carriers are obliged to serve everyone indiscriminately whereas manufacturers of the vehicles they use are not. As both the concept and the

1. JEREMY, THE LAW OF CARRIERS, INNKEEPERS, WAREHOUSEMEN, AND OTHER DEPOSITORIES OF GOODS FOR HIRE 4-7 (1816); Powell, A Treatise on the Duties, Liabilities, and Rights of Inland Carriers, 25 LAW TIMES 196, 210, 211, 224 (1855).
consequential duties are deeply rooted in legal history, this discussion begins with the 19th century evolution of the status of the common carrier and his special duties.

A. *THE ORIGINS OF COMMON CALLINGS*

Common carriers have always shared their special duties with other enterprises such as innkeepers. These industries, named the common callings, can justly be regarded as an exception to the general rule of private business. This raises questions as to why they are "common," why they are bound to serve the entire public, and why they are held strictly liable?7

1. *The Middle Ages: Common Callings As Business*

The answer to the first question cannot be deduced from the definition of the common carrier, because the "undertaking for hire [to serve] all persons indifferently"8 is the very essence of every business. It distinguishes common from private carriage, the latter including all forms of non-professional transportation, like transportation of the carrier's own goods, gratuitous transportation or exceptional carriage for reward by a person who usually is not engaged in that business.9 But the definition does not explain why such a distinction is necessary or useful in transportation, and not in construction or banking.

The historical development of the legal concept of common callings was by no means fostered by an intention to confer a special status on some branches of business and not on others. The list of common callings was much longer in the Middle Ages than in the 19th century. As Adler has pointed out, in Leet Jurisdiction of Norwich during the period 1374 to 1891, there "are to be found instances of the common purchaser, common merchant, common huckster, common brewer, common fripperer, common cooiker-up, common touter. In the Year Books we have the common innkeeper, common merchant, common marshal, common schoolmaster, common tavern, common surgeon."10 Adler identifies approximately twenty other forms of common callings and concludes "the list is so long and contains such different callings that we are led to the conclusion that the term common did not serve to distinguish one employment from another and that all occupations could be common."11 Thus, the "common" exercise of a certain activity indicated that a person made it his business and did not engage in it intermittently. Drawing the distinction

9. Id.
11. Id. at 152.
between occasional and professional activities must have been of the utmost importance to medieval society. The exchange of goods and services, especially in rural areas, rarely operated on a professional basis, but was rather based on different forms of help without direct reward, such as neighborhood, social, and charitable services.\textsuperscript{12} The common callings were exceptional because they reflected a rising organization of economy with division of labor among various professions and trades.

In legal terms, the splitting of private and common activities resulted in the imposition of special duties on those who exercised the latter. According to Oliver Wendell Holmes, the common carrier's strict liability for loss of goods can be traced to the origins of the general law of bailments in the falklaws of Germany and England. These old laws gave a remedy against thieves, not to the bailor, but to the bailee who in turn had to respond for losses without any possibility of excluding liability.\textsuperscript{13} However, this ancient rule explains neither the strict liability for the damage to goods nor the duty to serve, nor does it square with the observation that the common callings were by no means confined to forms of bailment.\textsuperscript{14}

Perhaps the better view is that the special obligations of the common callings were worked out during and not before the development of assumpsit, subsequent to the introduction of the action sur le cas in 1285. When a person voluntarily dealt with another and suffered damages due to his fault, no tort arose because the injured party was looked upon as accepting and exposing himself to the risk of damage. At first, an action on the case could be entertained only if an assumpsit and a breach thereof were pleaded.\textsuperscript{15} The special duties of the common callings were based on an implied assumpsit on their part. The "holding out" to the general public was regarded as a general or universal assumpsit of both serving the public without discrimination and carrying out this service carefully.\textsuperscript{16} General assumpsit never lost its original character and still gives rise to an action in tort,\textsuperscript{17} whereas special assumpsit, which was used for private activities became the seed of modern contract theory. The evolution of the latter did not start until much later,\textsuperscript{18} when the undisputed special duties of common callings were merely referred to as "custom of the realm."
\textsuperscript{19}

\textsuperscript{12} Id. at 153.
\textsuperscript{13} Holmes, Common Carriers and the Common Law, 13 Am. L. Rev. 611 (1879).
\textsuperscript{15} Ames, The History of Assumpsit, 2 Harv. L. Rev. 3 (1888-89).
\textsuperscript{16} Holmes, supra note 13, at 615.
\textsuperscript{19} Jackson v. Rogers, 89 Eng. Rep. 968 (1684); In Pozi v. Shipton, 112 Eng. Rep. 1106,
Thus it is erroneous to assume that the legal position of common carriers resulted from conscious policy decisions by the courts, for every business originally was a common calling and derived its special duties from assumpsit.20

2. Modern Times: Common Callings As Public Employment

The concept of common callings was gradually narrowed during the 17th century until it embraced only the common carriers and innkeepers at the close of the 18th century.21 Using special contracts or, being regarded as doing so, more and more businessmen avoided the particular duties of common callings. Business became "private" in the sense that the word designated a profession with freedom to choose customers at negotiated conditions. In short, "private" business became distinguished from the public interest. At the same time, the few remaining common callings appeared in the new light of public employment, both "common" and "public" often being used synonymously.22

1110 (1838) it was decided that the custom of the realm concerning the liability of common carriers need not be mentioned in the complaint, because as a general custom and not merely a local or special one, it will be considered by the court anyway.

20. Originally, common law imposed the duty of carefully serving every customer with due care in all branches of business. Latter general business law dropped this obligation and it remained only in the law of common carriers. See Arterburn, The Origin and First Test of Public Callings, 75 U. PA. L. REV. 411, 420 (1926). The rise of monopolies and the state of social emergency following the Black Death of 1348-1349 may have helped to generate the burden. But it fits in better with medieval ideas of just reward to assume that the tightened monopolistic situations of the 14th century merely stimulated a number of legal disputes in which the preexisting special duties of the common callings were expressed. Medieval thinking conceived economic relations as a part of an eternal order inspired by God, and pricing and service were seen as moral issues rather than as methods of achieving profit maximization. Cf. 2 W. HOLDSWORTH, A HISTORY OF ENGLISH LAW 468-469 (4th ed. 1936).

21. The estrangement from business regulation can be ascribed to the change in economic and social conditions, in particular to colonialism and the industrial revolution which put a definite end to the centuries of short supply and for the first time created conditions of abundance favorable to a market economy. On the other hand, the Reformation and the centuries of religious disputes had shaken the belief in the divine designation and unchangeable order of medieval society. Where birth formerly had determined a man's place in society, now wealth began to play an important part, making profit maximizing the ladder towards higher social rungs. The way was free for the liberation of economic exchange from the chains of morality, a step accomplished by the writings of Smith and Bentham. Adler, supra note 10, at 156-158.

22. One of the earliest and clearest statements about the public interest vested in common carriers is the comparison with sheriffs by C.J. Holt in Lane v. Cotton, 88 Eng. Rep. 1458 (1701). "[W]herever any subject takes upon himself a public trust for the benefit of the rest of his fellow-subjects, he is eo ipso bound to serve the subject in all the things that are within the reach and comprehension of such an office, under pain of an action against him; . . . [I]f an innkeeper refuse to entertain a guest where his house is not full, an action will lie against him, and so against a carrier, if his horses be not loaded, and he refuse to take a packet proper to be sent by a carrier. . . . Surely then where is a public employment created by law, the obligation is the greater; as if the sheriff refuse a writ, an action will lie against him. . . ." Id. at 1464; cf. New Jersey
Neither the cases nor the contemporary writings explain why general business was free from consideration of the public interest while transportation was not.\textsuperscript{23} The space left to historical explanation has been filled by three hypotheses, one economic, one legal, and one political.

From an economic perspective, it has been argued that monopolistic tendencies in the transportation sector prevented a liberalization and maintained the public interest in this field.\textsuperscript{24} The historical correctness of this argument is questionable. There is very little evidence of a monopolistic power of the carrier in those cases which have affirmed the duty to carry.\textsuperscript{25}

Two legal reasons for the establishment of the common carrier’s special status have been advanced: (1) the evolution of contract theory, and (2) a confusion of accident and act of God in the exemptions from the carrier’s liability. As stated above, general or universal assumpsit was the legal tool used to create the carrier’s duty to serve every shipper with care.\textsuperscript{26} When assumpsit became the seed of contractual obligations, it adopted a more precise meaning and could not be maintained as the source of the common carrier’s obligations. These obligations survived as custom of the realm based upon unquestioned precedent after their historical reasons had long been forgotten.\textsuperscript{27} The second reason focuses on the exception to the

\begin{flushright}
\textit{Steam Navigation Co. v. Merchants’ Bank, 47 U.S. (6 How.) 344, 382 (1848) (‘[The common carrier] is in the exercise of a sort of public office, and has public duties to perform.’).}
\end{flushright}


\textsuperscript{24} Cf. Arterburn, supra note 20, at 427; Contra Rosenbaum, \textit{The Common Carrier Public Utility Concept}, 7 J. LAND & PUB. UTIL. ECON. 157, 165 (1931).

\textsuperscript{25} In Sandiman v. Breach, 108 Eng. Rep. 661 (1827), the plaintiff sued a stagecoach owner who had breached a contract of carriage for damages which he had suffered from hiring a post-chaise at higher expense. Traditionally, transportation monopolies were only found in rural areas. The statute of William and Mary, 1695, 526 W. & M., ch. 22, provided for 700 hackney licenses in the cities of London and Westminster. This conveys an idea of the density of urban transportation in the 1700’s. This act prohibited any one person from holding more than two licenses. Its purpose was to maintain competition, and it explicitly stated the driver’s duty to serve. Moreover, monopolies in the industry cannot explain the strict liability of carriers for loss of and damage to goods. As to the duty to serve every applicant, monopoly situations could have been countered more effectively if the enforcement of this duty had been secured by writ of mandamus, a remedy usually refused. Finally, the impact of monopoly on the carrier’s duty to serve was explicitly rejected in an early English railway case in which the defendant railway company acquired a monopoly for the carriage of coal by purchasing and shutting down a canal which ran parallel to its tracks. The plaintiff argued that even if the defendant’s charter made service voluntary, the reference in the charter to the common law liability would require carriage in the given monopoly situation. In response to this, the court said: “The argument for the plaintiff is rather one to be addressed to the legislature. The real grievance is not the mode in which the Company manages the railway, but the shutting up of the canal which the legislature has suffered to be done without adverting to its evil consequences.” Johnson v. Midland Ry., 154 Eng. Rep. 1254, 1257 (1849).

\textsuperscript{26} See supra note 16 and 17.

\textsuperscript{27} Holmes, supra note 13, at 617.
carrier’s liability. It is uncertain whether the carrier’s liability for damage extended to merely accidental destruction before 1700 or whether he was only liable for accidental loss. The cases leave some ambiguity due to the vague meaning of “act of God”, for which the carrier was not liable in either case. It was only Lord Mansfield who read the concept in a narrow sense and stated the rule with complete clarity: “The carrier is in the nature of an insurer.”28 Both of these reasons are descriptions rather than explanations of why transportation did not follow the general path of business law toward freedom of contract.

If both monopoly and legal history furnish only partial and rather fragile explanations of the common carrier’s special status, the political reasoning advanced by Oliver Wendell Holmes seems more convincing. Holmes characterized the public callings as:

part of a protective system which has passed away. An adversary might say that it was one of many signs that the law was administered in the interest of the upper classes . . . [I]t formed part of a consistent scheme for holding those who followed useful callings up to the mark.29

The English feudal society, during the 17th and 18th centuries, spent only a part of the year on the land from which it derived its income. For much of the year the nobility lived in towns supported by income from the surrounding estates. Hence, the aristocracy depended heavily upon both the availability and the safety of carriage for passengers and goods. The movement of commodities could not be entrusted to the arbitrary, profit-oriented decisions of those engaged in the industry. The liability of the carrier had to be tightened to forestall collusion with thieves.30 Although the same danger existed with respect to other bailees,31 they were less important to the nobility. The professions which survived as common callings into the 19th century can be easily linked to the infrastructure of transportation. This is obvious for common carriers of all kinds, such as ferrymen, bargemen, wharfingers, lightermen, innkeepers, as well as farriers and smiths, who were indispensable links in the preindustrial transportation chain.32

Although industrial production may have been regarded as the origin of national wealth, and large scale transportation was needed for distribution of such production, transportation could not claim the same freedom of enterprise which was conceded to general business. As Sir W. Jones stated with respect to innkeepers:

29. Holmes, supra note 13, at 629.
31. Holmes, supra note 13, at 629.
32. Beale, supra note 28, at 163.
[R]igorous as this law may seem, and hard as it actually may be in one or two particular instances, it is founded on the great principle of public utility to which all private considerations ought to yield; for travelers who must be numerous in a rich commercial country, are obliged to rely almost implicitly on the good faith of inn-holders. . . .

In a sector of the economy where both monopoly and competition coexisted, the dependency of the upper classes on public transportation is the better explanation for the particular burden which the common law imposed indiscriminately on all common carriers. In economic terms, transportation generated positive external effects of a political, social, and economic nature which extended beyond the individual transport operation and were not sufficiently rewarded by the carrier’s charges. The monopoly argument gained weight when the railroads in fact monopolized large portions of inland transport throughout the 19th century.

B. The Common Carrier Concept during the 19th Century

Before the 19th century, common carriers’ legal responsibilities were still based on status and therefore uniform. Unlike other businesses, carriers were unable to adjust the legal framework of their activities to particular conditions by means of a contract.

It is uncertain whether at the beginning of the 19th century the special duties of the common carrier extended to the transportation of passengers and their luggage. Some writers contended that a carrier who conveys passengers exclusively is not a common carrier. They relied either on cases which had refrained from treating the carrier of passengers as an insurer.


This line of thought merely reflects a balance of political power which is typical for and inherent in the tripartite carriage of goods relationship. Whereas other businessmen are only confronted with the interest of their contractor, the carrier of goods has to meet the double demands of shippers and consignees, of producers and transshippers or consumers. Their pact against the carriers became obvious when they promoted legislative regulation after the construction of the railroads. See Ulen, The Market for Regulation: The ICC from 1887 to 1920, 70 Am. Econ. Rev. 306, 307 (1980). W. JONES, CASES AND MATERIALS ON REGULATED INDUSTRIES 36 (2d ed. 1976) gives the example of the product corn which, after the Civil War, was sold at the American east coast for six or seven times the price the farmer received in the mid-west at the same time. These political pressures are sometimes attributed to the monopolistic power which the railroad companies were able to exert because of the economies of scale and their franchises. But we may safely assume that the same alliance existed before and imposed its political superiority on the lawmakers. Cf. Adler, supra note 10, at 158; M. Horwitz, The Transformation of American Law 1780-1860, 114-116 (1977) (Points out the close connection between franchise and monopoly in regard to ferries and mills at the beginning of the 19th century.).

34. Dodd, On the Contract of Coach Proprietors, 11 Legal Observer, 233, 234 (1835-36); Powell, supra note 1, at 225.

or upon the fact that a carrier of passengers, as opposed to a carrier of goods, cannot have a lien on the person of the passenger for the price of carriage. However, it was decided in Benett v. Peninsular and Oriental Steam-Boat Company, that the defendant shipowner was obliged as a common carrier of passengers to receive the plaintiff on board his ship "Montrose" and carry him to Gibraltar. American cases stressed the duty to serve more emphatically.

As for the transportation of luggage, coachmen were initially regarded as common carriers only if they had held themselves out to transport both passengers and goods and had charged a distinct price for the latter. The unwillingness to impose strict liability in all cases was probably due to the fact that a passenger could keep his luggage with him while traveling by coach. Later, railway passengers would deliver their baggage to the company and lose control of it until they reached their destination. In this situation the courts held the common carriers of passengers strictly liable for loss of and damage to luggage.

During the 19th century, the concept of a common carrier of goods was affected by major modifications which narrowed its scope and thereby encouraged economic specialization, flexibility, and free enterprise in the transport sector. The first of these changes regards the kind of goods carried. The courts began to allow the carriers to confine their common carrier status to a class of goods irrespective of whether they were able to carry other goods. To this effect, the carrier's "holding out" was given a new interpretation. It was no longer regarded as a general announcement of the carrier's profession, but acquired a meaning of a quasi-contractual offer to the general public the content of which was subject to the carrier's will.

A carrier was also permitted to specialize in certain geographical areas. Thus, in the case of Johnson v. Midland Railway Company, it was decided that:

[a] person may profess to carry a particular description of goods only, for instance cattle or dry goods, in which case he could not be compelled to carry any other kind of goods, or he may limit his obligation to carrying from one

36. Dodd, supra note 34, at 234.
38. Bennett v. Dutton, 10 N.H. 481, 486 (1839); Jencks v. Coleman, 2 Sumn. 221, 224 (Cir. R.I. 1835).
place to another, as from Manchester to London, and then he would not be bound to carry to or from the intermediate places.\textsuperscript{43}

A further development concerns forwarding agents who stepped in between shippers and carriers as transportation became more complex. Initially forwarders who merely acted as agents confining their services to the delivery of goods for carriers were not regarded as common carriers. In some American cases, forwarders were held liable as common carriers for the services which they actually performed.\textsuperscript{44} By the middle of the 19th century, forwarders performed extensive and diversified services. They undertook to arrange the whole carriage until delivery to the consignee. They assumed responsibility for handling, collection, movement, and warehousing of goods. Where the forwarder collected the freight for the carriage and conveyed the goods to a railway company which was to carry out the main part of the transportation, an English court held the forwarder liable as a common carrier for the loss of the goods which occurred during the railway carriage.\textsuperscript{45} In reaching similar results, American judges stressed the nature and extent of the forwarders' undertaking to deliver the goods at destinations that made them common carriers.\textsuperscript{46} For all the remaining activities which preceded or followed the movement of the goods without being part of it, the forwarder was not regarded as a common carrier.\textsuperscript{47} They were liable on the basis of special contracts rather than a general "holding out."\textsuperscript{48} Thus, there was no strict liability. Liability was based only on negligence.

\section*{C. The Duty To Serve During The 19th Century}

Originally, the duty to serve every applicant had been subject only to the conditions that there was room in the carrier's vehicle\textsuperscript{49} and that the

\begin{itemize}
\item \textsuperscript{43} 154 Eng. Rep. 1254, 257 (1849).
\item \textsuperscript{44} CHITTY \& TEMPLE, supra note 40, at 18; J. ANGELL, A TREATISE ON THE LAW OF CARRIERS OF GOODS AND PASSENGERS BY LAND AND BY WATER 81 (2d ed. 1851); Platt v. Hibbard, 7 Cow. 497 (Sup. Ct. N.Y. 1827); Ackley v. Kellogg, 8 Cow. 223 (Sup. Ct. N.Y. 1828).
\item \textsuperscript{45} Hellaby v. Weaver, 17 Law Times 271 (1851). Similarly, in Hyde v. Trent and Mersey Navigation, 101 Eng. Rep. 218 (1793) the defendant was held liable as a common carrier for the destruction of goods by fire which occurred after the goods had been stored in a warehouse at the place of destination. The court found that the defendant owed delivery to the consignee as he had separately billed the price for the remaining cartage by a third person from the warehouse to the consignee.
\item \textsuperscript{46} See Ahearn, Freight Forwarders and Common Carriage, 15 Fordham L. Rev. 248, 252-260 (1946).
\item \textsuperscript{47} Brown v. Denison, 2 Wend. 593 (Sup. Ct. N.Y. 1829); ANGELL, supra note 44, at 81; Thompson, The Relation of Common Carrier of Goods and Shipper and its Incidents of Liability, 38 Harv. L. Rev. 28 (1924-25).
\item \textsuperscript{48} GORTON, supra note 14, at 9.
\end{itemize}
shipper or passenger offered reasonable payment before the beginning of the voyage. During the 19th century, the exceptions became more and more numerous. Eventually the duty was confined to the carrier’s usual place of business and his ordinary business hours. He was entitled to refuse goods which were in fact or at least appeared dangerous and improperly packed. The most important limitation on the duty to carry was the exhaustion of carrying capacity. Created in the time of horsepower, coaches, and wagons with low and inelastic capacities, this exception partially lost its justification in railroad transportation because the capacity of most railroads exceeds the normal traffic demand. Nevertheless, the courts applied the old rule to the new technology. In an Illinois case, a railroad which had facilities for offering additional transportation refused to use them in a year of great harvest and limited storage room. The Supreme Court of Illinois held that neither common law nor statute "requires anything more than that the company shall furnish reasonable and ordinary facilities of transportation.

The list of exceptions to the duty to carry passengers is even longer. Carriers were held entitled to refuse drunken persons, suspected thieves and people whose behavior constituted a public annoyance, those who had previously been lawfully ejected, or who had not procured a ticket, as well as those whose purpose was not carriage, but gambling or the interference with the interests of the carrier. Finally, the carrier was not bound to transport passengers on freight trains or to places where their lives would be in danger.

While several of these exceptions merely reflect problems of social consideration arising in mass transportation as in any other mass enterprise, some of them again stress the carrier’s position as an entrepreneur in a free enterprise economy, widening his discretion as to his scope of business and as to the conditions of carriage. This is true not only for the limitation of his capacity, but also for his power to refuse transportation to the agents of his competitors or to passengers without a ticket.

51. See Lawson, 12 Cent. L.J. 110-112 (1881).
53. Parrot v. Wells Fargo (The Nitro-Glycerine Case), 82 U.S. (15 Wall.) 524, 531 (1872);
54. Union Express Co. v. Graham, 26 Ohio St. 595 (1875).
56. Jencks v. Coleman, 2 Summ. 221, 225 (Cir. R.I. 1835).
58. Indianapolis, Peru & C. Ry., v. Rinard, 46 Ind. 293 (1874).
60. Jencks v. Coleman, 2 Summ. 221 (Cir. R.I. 1835).
D. DISCRIMINATION AND REASONABLE CONDITIONS

Discriminatory treatment or unreasonable conditions imposed by a carrier exercising monopolistic power is equivalent to a refusal to serve. This explains why the requirement of "reasonable conditions" and in particular of reasonable prices was imposed on the common carrier from the beginning.63 The concept, however, remained vague and did not gain shape until the monopolistic railroad corporations tried to maximize profits by price discrimination and other selective practices.

The idea that reasonableness included equal treatment, in particular equal charges for equal cost and risk situations, was widespread. In one case, the carrier conceded an exclusive right of service to one customer, an express company, and thereby rejected all other shippers. Such an agreement was declared void because "the very definition of a common carrier excludes the idea of the right to grant monopolies or to give special and unequal preferences."64 This requirement was specifically referred to in railway charters65 or in general statutes like the 1854 English act on railway and canal traffic which prohibited the railway companies from giving "any undue or unreasonable preference or advantage to or in favor of any particular person or company. . . ."66 An example of such a proscribed preference was a railway company's refusal to accept goods delivered by A after 5 P.M. when it subsequently accepted delivery from A's competitor at a later hour.67

A counterpart of the equality principle is the assertion in early railway cases that cost differences must be reflected in rate differences.68 The English courts fought price discriminating practices operated by railway companies against forwarding agents. The cost and rate structure of the railways made it cheaper to carry one big parcel than several small ones. Forwarders made it their business to collect small parcels into bigger shipments in order to benefit from the economies of scale. The railway companies frequently attempted to charge forwarders higher rates than they charged other shippers for parcels of the same size.69 In several cases these practices were declared illegal as not reflecting differences in cost or risk.70

64. New England Express Co. v. Maine Cent. R.R., 57 Me. 188 (1869).
65. 5 & 6 Will. 4, ch. 107, sched's 167, 175 (1836).
The difficulties in applying the principle that rate differentiation had to be justified by cost or risk differences favored the railroads.\textsuperscript{71} The distinction between price differentiation and price discrimination not reflecting cost differences was unclear. The courts did not feel competent to make these distinctions which, according to Cresswell, "assume a very complicated and difficult character, and are such as we feel but little qualified to decide."\textsuperscript{72} The tendency of the court to leave the determination of the reasonableness of rates, conditions, and bylaws to the jury did not solve the problem.\textsuperscript{73}

E. THE CARRIER’S STRICT LIABILITY DURING THE 19TH CENTURY

While the common carrier of passengers was liable only for personal


Several cases show directions in which railroad companies may discriminate in response to alleged cost differences. Hamilton, Discriminative Traffic Rates, 16 AM. L. REV. 818 (1882). They were allowed to classify freights and passengers and charge different rates for different classes, if there were reasonable grounds for such discrimination in the difference of cost of service, risk of carriage, or in the accommodations furnished, but the rates had to be the same for all persons and goods of the same class. Chicago, B. & O. R.R. v. Parks, 18 Ill. 460 (1857); Hays v. Pennsylvania Co., 12 F. 309, 311 (N.D. Cir. 1882). It was held unreasonable to discriminate against small shippers in favor of larger shippers of the same class of goods solely because of the difference in quantity. Hays v. Pennsylvania Co., 12 F. 309 (1882). If the larger shipper undertook to furnish a certain amount of freight per week or month, a lower rate was permissible. Nicholson v. Great Western Ry., 141 Eng. Rep. 1012 (1860). Discrimination in favor of localities where there was competition in carriage, against others where there was no competition, was proscribed. Fares, however, could be lower than the aggregate of the way fares between intermediate points though this structure frequently was due to the existence of a competing carrier between the termini. State v. Overton, 61 Am. Dec. 671 (N.J. 1854); Ransome v. Eastern Counties Ry., 140 Eng. Rep. 179, 185 (1857). These cases show the difficulties of cost computation and the weakened control of the courts over ratemaking. The equality principle could not be imposed effectively if there were no clear answers to the basic question of how much a service cost. The vague limit of reasonableness finally superseded the equality principle when the courts allowed open price discrimination to the extent that the charges were not unreasonable per se. Garton v. Bristol & Exeter Ry., 121 Eng. Rep. 656 (1861). The Supreme Judicial Court of Massachusetts upheld a railroad rate of 50¢ per ton per mile when the same company normally charges only 20¢ per ton per mile for carrying goods of the same class on the same road. The court held that the higher price was not unreasonable per se, and that the reduction of rates below the level of reasonableness in favor of some shippers did not entitle every shipper to the same benefit. Fitchburg R. Co. v. Gage, 12 Gray 393 (Mass. 1859).

During the first decades of their existence, the railway companies could afford rate reductions because technological innovations decreased their costs. The courts took the view the former rates did not become unreasonable merely because fallen costs allowed lower rates. On this premise, the decisions cited above set the railway companies free to charge discriminating prices in the shadow of formerly higher and yet reasonable rates.
injury due to his negligence, the common carrier of goods was liable for accidental loss and damage to goods and was exempted only by an act of God or the King’s enemies, an inherent vice of the goods, fraud of the shipper, or, in the case of sea carriage, by the law of general average.

Until the middle of the 18th century, contractual modification of this harsh liability for the carriage of goods could be achieved through use of special contracts. During the latter half of the 18th century, however, the courts began to state the carrier’s liability with increasing clarity, restricting the act-of-God exception, and finally putting the carrier into the position of an insurer. From this, it followed that the carrier could charge a higher “premium” for undertaking a higher risk. From about 1750 onwards, carriers hung out signs, circulated notices among their customers, or advertised that shippers should declare the value of their goods, and that higher rates would be charged for valuables. Failure to declare the full value of goods constituted fraud barring shippers from recovering damages caused from destruction or loss of the goods during carriage. These early notices, designed to increase the carrier’s income, often worked to limit its liability.

The next step was the publication of notices which simply restricted the carrier’s liability up to a certain value, often 5£ per parcel, or only to acts of gross negligence and intent, or which excluded the carrier’s liability altogether. By 1852 English courts, in consideration of the carrier’s “liability of ruinous extent,” had ratified limitation and exemption clauses of all kinds, and their language had lost the pathos of public interest.

The carriers’ quest for freedom of contract was not confined to inland transport. Carriers by sea pushed through legislation in England to restrict specific liability risks to the value of their ships. In 1797, Parliament re-

75. PAYNE & IVAMY, CARRIAGE OF GOODS BY SEA 154 (11th ed. 1979).
76. Cf. JEREMY, supra note 1, at 36; FLETCHER, THE CARRIERS LIABILITY 179 (1932).
77. See Beale, supra note 28.
82. A contractual view of the carrier-shipper relationship was used to explain the courts’ generosity vis-a-vis a notice of exemption: “If the parties in the present case have so contracted the plaintiff must abide by the agreement, and he must be taken to have so contracted if he chooses to send his goods to be carried after notice of the conditions. The question then is whether there was a special contract.” Leeson, 171 Eng. Rep. at 442.
83. 7 Geo. II ch. 15 (1734); 26 Geo. III ch. 86 (1786); 53 Geo. III ch. 159 (1813); cf. FLETCHER, supra note 76, at 175-177.
jected a bill limiting shipowners’ liability to cases of general negligence as unnecessary because the carrier might limit his liability in all cases by special contract.\textsuperscript{84} This is in fact what the shipowners did. After 1797 a new bill of lading came into use which excepted “the act of God, of the King’s enemies, fire, and all and every other dangers and accidents of the seas, rivers, and navigation of whatever nature and kind soever, save risk of boats, as far as ships are liable thereto.”\textsuperscript{85}

In the United States, the trend toward freedom of contract met with some resistance. Although most judges acknowledged the validity of simple notices limiting the carrier’s liability,\textsuperscript{86} some would not allow the carrier to exempt himself from liability for gross negligence or fraud.\textsuperscript{87} The New York courts initially took a still stricter attitude and declared void any contractual modification of the common carrier’s liability.\textsuperscript{88} But when the United States Supreme Court indicated in dictum that carriers by giving notice could immunize themselves from liability even for gross negligence,\textsuperscript{89} the line of opposition fell everywhere.\textsuperscript{90}

This liberal trend was reversed in 1873 under the influence of the Grange movement when the Supreme Court held that a common carrier by land could not contract away his liability for negligence.\textsuperscript{91} This holding, based on the public interest in the transportation industry and the court’s concern for the unequal bargaining power of shippers and carriers was extended to carriers by water in 1889.\textsuperscript{92} Shippers were subjected to the conditions imposed by carriers, especially by the railway corporations. However, the court did recognize the validity of liability restrictions for valuables, accidental losses, risk of navigation, live animals, and goods liable to rapid decay.\textsuperscript{93}

The latter attempt of passenger carriers to reduce their liability for negligence in regard to personal injuries took a similar course. English courts restricted their inquiries to the issue of notice, and they never doubted the substantive validity of the limitation of liability.\textsuperscript{94} In the United States, there

\begin{itemize}
\item 85. FLETCHER, supra note 76, at 178 (1932).
\item 86. Cooper v. Berry, 21 Ga. 526 (1857); Patten v. Magrath, 23 S.C.L. (Dud.) 159, 163 (1838); Beckman v. Shouse, 5 Rawle 178, 189 (Pa. 1835).
\item 87. Beckman, 5 Rawle at 189; Camden & Amboy R.R. v. Baldauf, 16 Pa. 67, 76-77 (1851).
\item 92. Liverpool & Great Western Steam Co. v. Phoenix Ins. Co., 129 U.S. 397, 441 (1889).
\end{itemize}
was much confusion until 1873, when the Supreme Court upheld the mandatory character of the common law liability for negligence of passenger carriers.

Though the American courts adopted a more traditional view as compared with the permissiveness of the English courts, the courts of both countries had one thing in common. Unlike their predecessors, they regarded the carrier’s liability as an object of contractual arrangements and not as a consequence of his status. The English and American position differed as to how far these arrangements could go. When the United States Supreme Court narrowed the scope of party autonomy, it relied neither on the mandatory character of the carrier’s status nor on Lord Holt’s fear of collusion with thieves. Instead it advanced the argument of the unequal bargaining position which is at the root of present consumer protection in the law of contract. It is doubtful whether shippers were better protected under the ruling of the United States Supreme Court than they were in England. The contractual exemption from liability for accident, which the Supreme Court recognized, put the burden of proof of the carrier’s negligence upon the shipper to whom evidence usually is not easily available. Moreover, not all state courts followed the Supreme Court, and therefore uncertainty arose.

F. Conclusion: The Law of Common Carriers on the Eve of Government Regulation

What has been described in the preceding sections may be summarized as the rise and fall of judge made business regulation. We have seen that by the end of the 18th century, the needs of the nobility and later the secret alliance of producers and consumers imposed on carriers a legal duty to serve, a prohibition against discrimination, and strict liability. In other branches of business freedom of enterprise, and negligence liability prevailed.

The obligations of the common carriers, which were initially independent, influenced each other. Strict liability, initially based upon a general assumpsit to carry safely, needed a new basis when assumpsit became the cornerstone of contract law because the carrier-shipper relationship was not contractual. The carrier was under a duty to carry. This led to an in-

96. New York Central R.R. v. Lockwood, 84 U.S. (17 Wall.) 356, 380 (1873) ("The improved state of society and the better administration of the laws, had diminished the opportunities of collusion and bad faith on the part of the carrier, and rendered less imperative the application of the iron rule, that he must be responsible at all events.").
98. Id. at 142.
dependent legal development of the carrier's liability, the custom of the
realm. When the carrier's liability later approached that of an insurer, the
courts were on their way to allowing price discrimination under the concept
of different risks. Another route to the same end began with the carrier's
duty to serve which had to be supplemented by a prohibition against dis-
criminatory practices. In summary, the duty to carry has been an important
tool in shaping the particular liability and antidiscriminatory aspects of the
law of common carriers.

Although the common law imposed a heavier duty on carriers than on
other businesses, it did not provide the remedies needed by shippers and
passengers to outweigh their diminished bargaining powers.

When American legislators in the states, and later at a federal level,
were faced with the choices for government regulation of railroad rates,
they acted because of the changed reality in transportation. The problems
of rate regulation were too complex to be dealt with in an ordinary trial.
Moreover, litigation against railway companies was difficult because carriers
retained the necessary evidence while the burden of proof was upon the
shipper. The financial and legal resources of the railroads made it risky for
the plaintiff to sue if his business depended upon transportation services of
the carrier.

About 1800, the law of common carriers was still centered upon a
definition of status whereas economic development was beginning to de-
mand a flexible legal framework. In other markets, contract provided for
such a framework. In transportation, public interest seemed to exclude
party autonomy. However, gradually the courts responded to economic
pressure by allowing economic self-determination and freedom of contract
to penetrate the law of common carriers. They consented when the carriers
restricted or even excluded their liability altogether. Later carriers could
specialize in certain branches of transportation by holding themselves out
as carriers of only certain goods serving certain routes. The duty to serve
was not enforced beyond the regular scope of business they had chosen
even though their facilities might have allowed expansion. By prohibiting
certain discriminatory practices, the courts often merely showed the carriers
how to discriminate lawfully in the future. Carriers seem to have found ways
around the law of common carriers, until this body of law was nothing more
than an empty shell stranded on the beaches of legal history. Legislative
intervention was therefore much more than a remedy for technical difficul-
ties. It was the logical consequence of the common law courts' failure to
maintain and protect the public interest against the aggregate financial
power of the railroads.
III. THE LAW OF COMMON CARRIERS UNDER REGULATORY STATUTES

In the United States, the defects of the judge-made law were exposed to increasing criticism after the Civil War. The Grange movement among midwestern and eastern farmers, who complained of high and discriminatory rates favoring their competitors, resulted in pressure for legislation. Illinois took the lead in 1871 by establishing a commission to set up a schedule of mandatory maximum rates and prohibit unreasonable or discriminatory railroad rates. When the United States Supreme Court decided in 1886 that individual states lacked the power to regulate traffic originating from, or bound for, points in other states, federal action became necessary, and one year later, an act to regulate commerce (the Interstate Commerce Act, "ICA") was promulgated. The ICA was a landmark in the development of transportation law.

A. EARLY GOVERNMENT REGULATION

Transportation has always been a promising field for the public treasurers because the infrastructure of roads, canals, bridges, and ferries either necessitated public lands and rivers or the sovereign's right of eminent domain to expropriate private property.

An early and conspicuous illustration of the fiscal motive is given by an English "Act for the Licensing and Regulating [of] Hackney-Coaches and Stage-Coaches" of 1694. The House of Commons referred to the act as "being sensible of the great and necessary expense in which your Majesties are engaged, for carrying on the present war against the French king, and being desirous to supply the same. . . ." In conformity with this purpose, hackney and stage coach drivers were required to buy licenses of limited duration and to pay annual rents on them. The act also regulated service and rates in the interest of the passengers and the public. Horses had to be at least 14 hands high; coaches had to be marked with identification numbers, maximum rates were established for the first and for every subsequent hour, as well as for specific routes within London. A driver's refusal to carry was subject to penalty. Out of the 700 available hackney licenses, a person could only obtain two. Finally, a five member special commission was established to administer the licensing system, to account for the fees, to hear complaints against drivers, to fine them for unlawful

100. The legislative history of Illinois is described by W. JONES, CASES AND MATERIALS ON REGULATED INDUSTRIES 36 (2d ed. 1976).
103. 5 & 6 W. & M. ch. 22 (1694), repealed by 30 & 31 Vict. ch. 59 (1867).
behavior, and to enact further regulations in order to avoid "disturbances" and "inconveniences" in the streets.104

The Hackney statute of William and Mary also contains some very modern devices for the organizational framework of regulations. The commission united the executive, legislative, and adjudicatory functions of government in one administrative body. It decided upon individual entry into the hackney business. It included specific regulations concerning the hackney traffic as a whole, and it sat as an inferior court to hear cases against or among hackney drivers in a well-defined procedure.

However, it lacked the power to fix, change, or supervise rates and this became the primary reason for the establishment of modern regulatory commissions. The predecessors of rate control have to be sought in the advisory agencies which came into being in several American states after 1844.105 The administrative burden created by increasing railroad traffic and by rate complaints had become so heavy that the legislatures which had incorporated the railroad companies and dealt with their problems until then, delegated their tasks to the courts, selectmen, and commissions.106 Agencies which were confined to recommendations and advice directed at the legislature were the most common form. It was not until 1873 that Illinois set up the first commission with mandatory power over rates.107

Some of the advantages of legislative regulation as compared with the common law are: (1) Where the common law protected the shipper or passenger from extortion only by a vague requirement of reasonable rates, the schedules fixed by a statute or an agency clearly establish what is reasonable. (2) Where the common law remedies of damages and reimbursement of overpayments are toothless sanctions in the typical mass carriage transaction of small value, the statutory menace of fines may deter the carrier much more effectively from unlawful practices.108 (3) Rate problems are too manifold and complex to be dealt with by judges on a case by case basis. When an intervention with the market forces of supply and demand is desirable, it can be exerted more effectively by a specialized agency and ex ante investigations into the whole rate structure.

104. This statute, designed to raise revenue for the king's war, pursued a number of classical aims of economic engineering to which modern attempts at taxicab regulation adhere. See Kitch, Isaacson & Kasper, The Regulation of Taxicabs in Chicago, 14 J.L. & Econ. 285, 302-316 (1971). See also Chicago, M. & St. P. Ry. v. Minnesota, 134 U.S. 418 (1890); Smyth v. Ames, 169 U.S. 466 (1898).
105. W. JONES, supra note 100, at 31-33.
106. See Hunter, The Early Regulation of Public Service Corporations, 7 AM. ECON. REV. 571 (1917).
107. W. JONES, supra note 100, at 37.
108. For these two points, see Kitch, Isaacson & Kasper, The Regulation of Taxicabs in Chicago, 14 J.L. & Econ. 308 (1971).
B. Rail Regulation Prior to The Staggers Act

As noted above, the Interstate Commerce Act\textsuperscript{109} was principally promulgated in response to shipper complaints of high and discriminatory rates due to railroad monopoly.\textsuperscript{110} This political background is reflected both by the scope of the original act and by its concentration upon rate regulation.

1. Regulated Carriers

Originally, the ICA applied "to any common carrier . . . engaged in the transportation of passengers or property wholly by railroad, or partly by railroad and partly by water when both are used, under a common control, management or arrangement for a continuous carriage or shipment."\textsuperscript{111} The subject matter of the Act was vague as compared with the contemporaneous state of the common law. Contrary to their predecessors, especially in English courts, American judges resisted attempts to escape from the common carrier status. Supported by a number of state constitutions and statutes which declared all railroads to be common carriers,\textsuperscript{112} the courts only exempted truly private lines like industrial, mining, or lumber roads from the ICA and common carrier duties.\textsuperscript{113} Railroads were prohibited from splitting their lines into several parts in the hope of being common carriers on some and private carriers on the others.\textsuperscript{114}

Twenty years later, the Hepburn Act of 1906\textsuperscript{115} brought sleeping car and "express companies" under the control of the ICA. The United States Supreme Court interpreted this latter category as including all express firms irrespective of their corporate structure.\textsuperscript{116} The Hepburn Act widened the range of regulated activities performed by these carriers by extending the jurisdiction of the Interstate Commerce Commission ("ICC") to terminal facilities, freight depots, and all services connected with receipt, delivery, transfer, or storage of goods.\textsuperscript{117}

\textsuperscript{110} Cf. Texas & Pac. Ry. v. ICC, 162 U.S. 197, 210-211 (1896).
\textsuperscript{111} Today, in international transportation, all carriage inbound and outbound or which passes through a foreign country on its way to another place in the United States, is subject to the Act with regard to the part of the route in the United States. 49 U.S.C. § 10501(a)(2).
\textsuperscript{113} Wade v. Litcher & Moore Cypress Lumber Co., 74 F. 517 (5th Cir. 1896); Walling v. Rocklon & Rion R.R., 54 F. Supp. 342 (W.D.S.C.), 146 F.2d 111 (4th Cir.), (per curiam), affd cert. denied 324 U.S. 880 (1944).
\textsuperscript{114} Brownell v. Old Colony R.R., 41 N.E. 107 (Mass. 1895); Crescent Coal Co. v. Louisville & Nashville R.R., 135 S.W. 768 (Ky. 1911).
\textsuperscript{115} 49 U.S.C. § 10501(a)(1).
\textsuperscript{116} United States v. Adams Express Co., 229 U.S. 381 (1913).
\textsuperscript{117} 49 U.S.C. § 10102(18), (23) (Supp. IV 1980).
2. Rates

The ICA of 1887 was mainly concerned with high rates; it restated the common law and empowered the ICC to investigate into and decide on the reasonableness of rates. However, this authority was held not to include the prescription of maximum rates, a power later conferred upon the Commission by the Hepburn Act of 1906. Only four years later, the Mann-Elkins Act enabled the ICC to suspend rates filed with it, pending an inquiry, for up to seven months. This act and contemporary ICC action sought to ensure rate stability. However, the need for higher railroad revenues soon became evident as the financial situation of the railroads decayed before and during the First World War. In 1920, the ICC received the additional power to fix minimum rates to prevent rate wars and further damage to the whole industry.

This amendment changed the basic policy of railroad regulation. Established to defend shipper interests against rail monopolies, the ICC was given the responsibility of protecting both shippers and the regulated industry. Consequently, its discretion in finding the compromise between the contradictory interests was broadened. Formerly a tool of government policy, the Commission now became the policy maker under the National Transportation Policy as formulated in 1940. The purpose was:

To ensure the development, coordination, and preservation of a transportation system that meets the transportation needs of the United States, including the United States postal service and the defense, it is the policy of the United States Government to provide for the impartial regulation of the modes of transportation subject to this subtitle, and in regulating those modes—
(1) to recognize and preserve the inherent advantage of each mode of transportation;
(2) to promote safe, adequate, economical, and efficient transportation;
(3) to encourage sound economic conditions in transportation, including sound economic conditions among carriers;
(4) to encourage the establishment and maintenance of reasonable rates for transportation without unreasonable discrimination or unfair or destructive competitive practices;
(5) to cooperate with each State and the officials of each State on transportation matters;
(6) to encourage fair wages and working conditions in the transportation industry.

The system of rate regulation outlined above is still in force. The carrier must establish his rates and tariff classifications as well as rules on connected matters like packing, documents, baggage, and car service.\(^{124}\) Tariffs containing all such information have to be published, kept for public inspection, and filed with the ICC.\(^{125}\) If the rates fail to meet the standards of reasonableness, the ICC may impose maximum or minimum rates.

There are no clear standards for determining a “zone of reasonableness.” The two poles between which rate regulation oscillates are cost-of-service and value-of-service pricing.\(^{126}\) The latter is what economists call price discrimination. Rates are fixed regardless of the respective cost of carriage and merely in response to the inelasticity of demand for transportation or to what the market will bear. As long as the railroads retained a monopoly over inland transportation, this method of pricing was successfully supported by the ICC.\(^{127}\) It amounted to a subsidy or a redistribution of wealth from high-valued manufactured goods to large-volume, low-valued mining and agricultural commodities. Ratemaking became a tool for defining the balance between different industries and regions at the cost of considerable losses in terms of efficiency. When motor carriers disrupted the rail monopoly, shippers of high-valued goods shifted their cargo to trucks, and the benefits of internal subsidy could only be maintained by additional regulation of motor carriers.\(^{128}\)

3. Duty To Serve

While the original act only contained a general prohibition against discrimination, the railroad’s duty to carry was expressly codified in 1910.\(^{129}\) Also, the carrier’s right to adopt regulations establishing the conditions, methods, time and place at which he is willing to accept goods offered for carriage, has been further recognized. If these regulations are not arbitrary, unreasonable, or discriminatory, refusal of goods not tendered in conformity with them is justified.\(^{130}\)

\(^{126}\) M. Fair & J. Guandolo, Transportation Regulation 139 (8th ed. 1979).
\(^{127}\) Cottonseed, Its Products, and Related Articles, 203 I.C.C. 177, 182 (1934).
\(^{130}\) Crescent Coal Co. v. Louisville & Nat’l Ry., 135 S.W. 768 (1911); Louisville & N. R.R. v. F.W. Cook Brewing Co., 172 F. 117 (7th Cir. 1909); Platt v. Lecocq, 158 F. 723 (8th Cir. 1907).
The shortage of terminal and car facilities for special cargo induced carriers to exclude these shipments from their common carriers duties. The problem of special equipment is a question of who should bear this additional cost. The concept of the railroad's "holding out" makes the railroad responsible for these costs. Under the provisions of the ICA a rail carrier "shall furnish . . . adequate car service [including] special types of equipment." The ICC may require a railroad to incorporate its car service rules in its tariffs.

Lack of capacity due to unexpected or unusual demand is excusable only if the increase in demand was unforeseeable and cannot be matched with equipment from other sources. A railroad which could not provide enough refrigerator cars to carry a bumper crop of vegetables was held liable for breach of its duty to serve. In contrast with pre-ICA law, this decision stresses the railroads' capability and duty to adjust to shipper needs. To the same end, the ICC may directly interfere with the car service in order to overcome a traffic emergency in a section of the United States. Even without such an emergency, the ICC may, under certain conditions, require a single carrier to supply himself with the necessary equipment to furnish adequate car service.

A principal function of regulation is to ensure the availability of transportation. Regulatory action, is the most important means of achieving this aim. The common law does not provide remedies against the shutting down of unprofitable lines, nor does it provide a specific frequency of trains. The solutions to these problems must be provided by statute and regulation which indirectly define the scope of the carrier's duty to serve.

4. Carrier's Liability

The Supreme Court of the United States revitalized the rigidity of the common carrier's liability by containing attempts at contractual modification. Congress, therefore, felt little need to interfere with the courts in

132. 49 U.S.C. §§ 11121(a), 10102(2) (Supp. IV 1980); see also Midland Valley Ry. v. Excelsior Coal Co., 86 F.2d 177 (8th Cir. 1936); Famechon Co. v. Northern P. Ry., 23 F.2d 307 (8th Cir. 1927).
135. Atlantic Coast Line Ry. v. Geraty, 166 F. 10 (4th Cir. 1908).
this field in 1887, and not before 1906 was the matter subject to federal legislation by the Carmack Amendment, a part of the Hepburn Act.\textsuperscript{141} This act, like later statutes, only covered carriage of property, not the carriage of passengers which still is a subject of the common law of torts. The reasons for legislation were twofold. First, there was great disparity of judgment in liability matters among different states. Because the Supreme Court decided not to overrule the state courts,\textsuperscript{142} the unequal liability risks jeopardized uniform conditions in interstate commerce. Second, shippers found it difficult to file claims for loss or damage occurring during an interline shipment when they did not know where the critical event had occurred.\textsuperscript{143}

In response to these problems, the Carmack Amendment prohibited all contractual exemptions from liability, required the initial carrier to issue through bills of lading for interline shipments, declared the carrier liable to the shipper for damage or loss occurring on any part of the route, and allowed him to recover from a subsequent carrier, if the shipment had in fact been damaged on that carrier's line. This act not only freed the shipper of doubts as to the place of damage; it also relieved him of the burdensome litigation at a distant place by allowing him to sue the initial carrier close to his own place of business.\textsuperscript{144} In the interest of consignees, this liability was later extended to the delivering carrier.\textsuperscript{145}

Contractual modifications of the carrier's liability, though apparently excluded by the Carmack Amendment, still raised questions. In 1912, the Supreme Court decided that the statute had only codified the common law which barred carriers from immunizing themselves against negligence liability, but did not prohibit value limitations of recovery if the shipper was granted a lower rate in consideration for the liability waiver.\textsuperscript{146} The widespread practice of released rates based upon agreed cargo valuations which this opinion approved, was abolished by the Cummins Amendment of 1915\textsuperscript{147} and, with modifications, reintroduced by the second Cummins

\textsuperscript{141} Act of June 29, 1906, ch. 3591, 34 Stat. 584, 595 (current version at 49 U.S.C. §§ 11707 (1978)).
\textsuperscript{143} For a review of law prior to 1906, see Adams Export v. Croninger, 226 U.S. 491, 504 (1912); \textit{Knorst, Interstate Commerce Law and Practice} 89-90 (1953).
\textsuperscript{144} \textit{Cf.} Kulina, \textit{Liability of a Carrier for Loss and Damage to Interstate Shipments}, 17 CLEV.-MAR. L. REV. 251, 252 (1968).
\textsuperscript{146} Adams Express, 226 U.S. at 509.
Amendment one year later. The resulting law requires the carrier to pay the "actual value" of the damaged or lost goods. It also voids all exceptions or limitations of liability or recovery. There are, however, two exceptions: (1) the liability provisions are not mandatory with regard to passengers' baggage carried by common carriers and (2) the ICC may authorize or require common carriers of property to establish rates dependent upon value declared in writing where such a rate differentiation is deemed just and reasonable. The Commission developed general criteria for the appreciation of released rate applications and its action was usually upheld by the courts. Except in the movement of household goods, released rates are not commonly used.

The courts and the Commission have shown great determination to stem the carriers' efforts to isolate themselves against risk. Repeated attempts to reinterpret the statutory liability as based on negligence have been rebutted. Even in the case of damage to perishable goods, there is no presumption in favor of an inherent vice causing the damage, which would except the carrier from liability. Moreover, the recoverable amount not only includes the replacement costs of the merchandise, but also the shipper's profit derived from his bargain with the consignee. Concealed damage clauses which try to apportion damages, discovered after delivery, among the shipper, carrier and consignee were found by the ICC to violate the full recovery requirement of the ICA. Some courts have also invalidated "benefit of insurance" clauses in which carriers stipulated that they could reap the benefit of a shipper's cargo insurance. Such clauses do not impair the shipper's full recovery, but this is a result of the shipper's own expenses for insurance. Therefore, they were held to constitute an unlawful additional compensation of the carrier by the shipper. The ICC has promulgated mandatory time tables for acknowledging

149. With regard to motor carriers, see 49 C.F.R. § 1307.200, and concerning railroads, see In the Matter of Express Rates, Practices, Accounts and Revenues, 43 I.C.C. 510 (1917); Released Rates on Stone in the Southeast, 93 I.C.C. 90 (1924); and J. Guandola, TRANSPORTATION LAW 49 (3d ed. 1979).
151. Missouri Pac. R.R. v. Elmore & Stahl, 377 U.S. 134 (1964). For a critical comment, see Skulina, supra note 144, at 255, on who shared the erroneous view that the "basic theory of liability is found in negligence."
152. Polaroid Corp. v. Shuster's Express, 484 F.2d 349, 351 (1st Cir. 1973).
days), investigating (promptly), paying or declining (120 days), and reporting on (every 60 days), claims. Attempts to extend the compulsory liability insurance of motor common carriers and freight forwarders to railroads and water carriers may complete this picture in which the spirit of the common law still seems alive.

5. Other Regulations

What has been described so far is the development of ancient common law obligations. However, modern legislation has considerably enlarged the scope of regulatory power. As a consequence entry into and exit from the industry as well as single route markets are subject to elaborate rules. Licenses are based upon "public convenience and necessity." New entries must conform with "public policy." The ICC, in exercising its wide discretion, may either close transportation markets and protect established carriers or open the gates to competition. Questions affecting the carriers' financial resources and structure, like mergers, combinations, securities, accounting, valuation of property, are the object of other provisions of the ICA. Finally, the Interstate Commerce Act establishes the whole structure of the ICC as well as enforcement procedures including civil and criminal penalties. Though most of these regulations are necessary corollaries of rate regulation, they do not directly affect the carrier shipper or carrier passenger relationship and therefore may be omitted from the instant analysis.

C. Other Carriers Subject to ICC Jurisdiction

1. Pipeline Regulation

The first new mode of transportation to be included into the ICA by the Hepburn Act of 1906 was pipelines carrying oil and other commodities, except water, artificial and natural gas. Pipelines of the latter type usually

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157. Cf. Rules, Regulations, and Practices of Regulated Carriers with Respect to the Processing of Loss and Damage Claims, 340 I.C.C. 515, 570 (1972) ("The virtual inelasticity of the traditional liability of common carriers is in itself a compelling force for motivating the prompt payment of claims.").
161. See supra note 141 (current version at 49 U.S.C. § 10501(a)(1)(C) (Supp. IV 1980)).
fall under state or local public utility regulation.\textsuperscript{162} Natural gas pipelines are subject to federal regulation.\textsuperscript{163}

The extension of the ICC jurisdiction was mainly a response to monopolistic practices of the Standard Oil Company which refused the use of its own pipelines to small oil producers unless they sold their oil to Standard Oil at low prices.\textsuperscript{164} To prevent such abuses, the courts extended the concept of a "pipeline common carrier" to pipeline companies which only carry their own oil.\textsuperscript{165} Recently, pipeline regulation has been transferred from the ICC to the Department of Energy and the Federal Energy Regulatory Commission,\textsuperscript{166} and the ICC now merely retains jurisdiction over pipelines carrying commodities other than oil, such as gasoline and kerosene and perhaps coal slurry.\textsuperscript{167}

2. Motor Carrier Regulation Prior To The 1980 Motor Carrier Act

In 1935, Congress promulgated the original Motor Carrier Act\textsuperscript{168} which was designed to preserve the value-of-service rate structure of railroads which in turn protected revenues of both railroads and western farmers.\textsuperscript{169} Moreover, following a general trend of state legislation towards monopoly and protection of established carriers, Congress wanted to suppress what was thought to be excessive competition in the trucking industry itself.\textsuperscript{170}

From the beginning, however, the regulation of motor common carriers was imperfect. Carriage of agricultural commodities has always been exempt, because the farmers were not to be deprived of the low rates resulting from rail-truck competition.\textsuperscript{171} Also in the "commercial zones"

\textsuperscript{162} Beard, Regulation of Pipe Lines as Common Carriers 23 (1941).
\textsuperscript{164} Beard, supra note 162, at 10-19.
\textsuperscript{165} United States v. Ohio Oil Co., 234 U.S. 548 (1914); see also Beard, supra note 162, at 30-45.
\textsuperscript{167} According to Lorentzen, Coal Slurry Pipelines: A Railroad Perspective, 10 Transp. L.J. 153, 164 (1978), coal slurry pipelines would be essentially private carriers. But see the text accompanying supra note 165.
\textsuperscript{170} See George, Principles of Motor Carrier Regulation, 63 Am. L. Rev. 72, 76 (1929). See generally, W. Jones, supra note 100, at 499.
\textsuperscript{171} 49 U.S.C. § 10526(a)(4)-(6) (Supp. IV 1980); see also Nelson & Greiner, supra note 169, at 363.
surrounding the cities, rail and trucks do not compete, but supplement each other. Consequently, these zones have always been free from regulation.\textsuperscript{172} The principal weakness of motor common carrier regulation lies in the cost structure of the industry. Because of the low cost of entry into, and exit from trucking, high motor carrier rates prescribed by the ICC to protect the railroads\textsuperscript{173} induce shippers to buy their own trucks and change from common to private carriage.\textsuperscript{174} The result is that approximately 60\% of intercity freight is handled by unregulated trucking operations.\textsuperscript{175} The share of fully regulated transportation is further diminished by so-called contract carriers who transport for a limited number of patrons on the basis of continuing agreements.\textsuperscript{176} These carriers are not prohibited from discrimination and not bound by maximum rate standards or mandatory liability rules.\textsuperscript{177}

3. Water Carrier Regulation

In 1940, the next regulatory step was taken as the jurisdiction of the ICC was extended to interstate water carriers.\textsuperscript{178} Joint rail and water services had been under ICC control since 1887.\textsuperscript{179} Further sections of the interstate shipping industry were regulated by the Panama Canal Act of 1912, the Shipping Act of 1916 (High Seas and Great Lakes), the Denison Act of 1928 (Mississippi navigation), and the Intercoastal Shipping Act of 1933 (Panama Canal). The usefulness of these statutes was limited because they only conferred jurisdiction on the ICC or the Shipping Board in

\begin{footnotes}
\item 173. Immediately after enactment of the Motor Carrier Act, the ICC made use of its minimum rate power to level up truck rates. See Fifth Class Rates Between Boston, Mass., and Providence, R.I., 2 M.C.C. 430, 547-549 (1937); Commodity Rates of Oklahoma & Texas Transfer Co., 6 M.C.C. 259 (1938); Rates over Carpet City Trucking, 4 M.C.C. 589 (1938).
\item 174. See Wilson, \textit{Effects of Value of Service Pricing Upon Motor Common Carriers}, 63 J. Pol. Econ. 337-340 (1955). The express exemption of private carriage in 49 U.S.C. § 10524 (Supp. IV 1980) was added by Pub. L. No. 85-625 of August 12, 1958, to make clear that pseudo buy-and-sell techniques employed by carriers do not constitute private carriage. Rather, the transportation has to be incidental to a primary non-transportation business of the carrier to be exempt.
\item 177. In the terminology of the ICA, "carrier" refers to both common and contract carriers, 49 U.S.C. § 10102(2) (Supp. IV 1980), whereas the antidiscriminatory regulations of 49 U.S.C. § 10741 (Supp. IV 1980), expressly use the term "common carrier." For the freedom of maximum rates, see 49 U.S.C. § 10704(c)(1) (Supp. IV 1980). The liability provision of 49 U.S.C. § 11707 (Supp. IV 1980), expressly refers to common carriers, but contractual time limitations of less than nine months for filing claims against the carrier are prohibited for both common and contract carriers.
\item 179. Moerman, \textit{supra} note 178, at 29.
\end{footnotes}
an incoherent and fragmentary manner. Moreover, the ICC still lacked authority to regulate port-to-port rates even where water carriers and rail were competing for the same traffic.

During the 1930's, the railroads were not only faced with competition from motor carriers, but also from the Panama Canal and the construction and improvement of inland waterways. This competition drove the railroads into a deep financial crisis. In another effort to protect the railroads, the Transportation Act of 1940 transferred jurisdiction from the Shipping Board and established the ICC as the principal regulator of both inland waterway and oceangoing water transportation between points in the United States. However, the general exemption of bulk cargo for which water carriers have the inherent cost advantage professed in the National Transportation Policy, leaves only 10-15% of all interstate water transport operations in the reach of the ICC.

4. Freight Forwarder Regulation

The common carrier concept received its present scope in 1942 and 1950 when freight forwarders connected with interstate surface transportation were regulated. This extension apparently was adopted for the benefit of the forwarders. They wanted to be recognized as common carriers so that arrangements entered into with motor carriers for through routes and low joint rates could be legalized and continued under ICC approval. Such arrangements could only be filed as binding with the ICC, if made

180. W. JONES, supra note 100, at 507-510.
181. CORONA COAL CO. v. SECRETARY OF WAR, 69 I.C.C. 389 (1922).
182. KNORST, supra note 143, at 146.
184. For the exemption, see 49 U.S.C. 10542 (Supp. IV 1980). For the cost advantage, cf. PECK, supra note 128, at 81. The estimations of the amount of exempt traffic are taken from PECK, supra note 128, at 78 n.12 and Moerman, supra note 178, at 10.
186. M. FAIR & J. GUANDOLO, supra note 176, at 92. Special low rates for freight forwarders granted by motor carriers had been rejected by the ICC before. See UNITED STATES v. CHICAGO HEIGHTS TRUCKING, 310 U.S. 344 (1940).
between "carriers."\textsuperscript{187}

Even if not enacted on behalf of other common carriers, the freight forwarder regulation is not free of protective concern for them. In particular, the law restricts the forwarders to the use of direct common carriers and, thus, forestalls a partial escape from ICC regulation by joint actions of forwarders and contract carriers.\textsuperscript{188} This regulation casts light upon the intrinsically ambiguous nature of the forwarding agents under American law. They are carriers in relation to the shipping public and shippers in relation to the performing carriers.\textsuperscript{189}

\textbf{D.\hspace{.75em}OCEAN VESSEL REGULATION}

\textbf{1.\hspace{.75em}General Background}

Maritime navigation has been regulated in a different manner and for different purposes. Legislative intervention at first concerned liability and later the control of prices and practices. The charges of maritime transportation were subjected to governmental regulation by the Shipping Act of 1916,\textsuperscript{190} a statute which was essentially an emergency measure to counteract a shortage of tonnage and its detrimental impact on U.S. foreign commerce. Since the Civil War, the U.S. merchant fleet had shrunk due to declining investment, and by 1910, American vessels were carrying only 10\% by volume of U.S. foreign trade.\textsuperscript{191} When the First World War broke out, the European nations withdrew vessels from the U.S. trade. Consequently, freight charges soared in the United States. Rates on grain shipped from the United States to Britain rose from 5\$ to 50\$ a bushel.\textsuperscript{192}

This was a period marked by the domination of liner conferences. In defiance of the Sherman antitrust law,\textsuperscript{193} these shipping cartels operated on nearly every trade route in both the foreign and domestic commerce of the United States. The members of the conferences acted together to control rates, sailing schedules, and the pooling of freight and passenger fares. The competition of outsiders, "tramps" as they were called, was continued by "fighting ships" scheduled to sail in direct competition with an outsider

\begin{itemize}
\item \textsuperscript{187} Acme Fast Freight v. United States, 30 F. Supp. 968, 973 (S.D.N.Y. 1940), aff'd mem., 309 U.S. 638 (1940).
\item \textsuperscript{188} 49 U.S.C. § 10749(b) (Supp. IV 1980); see also Comment, Intermodal Transportation and the Freight Forwarder, 76 Yale L.J. 1360, 1367 (1967).
\item \textsuperscript{189} Ahearn, supra note 46, at 261 (1946).
\item \textsuperscript{192} Mansfield, Federal Maritime Commission, in The Politics of Regulation 42, 47 (J. Wilson ed. 1980).
\item \textsuperscript{193} Lowenfeld, "To Have One's Cake . . . "—The Federal Maritime Commission and the Conferences, 1 J. Mar. L. & Com. 21, 26, 27 (1969-70).
\end{itemize}
at lower rates, or by tying arrangements with shippers which provided deferred rebates to those who would commit themselves to the exclusive use of conference vessels. Before the war, an investigation of the so-called Alexander committee revealed that a vast majority of the shippers, though complaining of discriminatory practices, favored the existence of the conferences which were said to guarantee ample tonnage as well as efficient, frequent, and regular service. 194 Congress responded to the activities of liner conferences by establishing an administrative body, the Shipping Board which later became the Federal Maritime Commission (FMC) 195 to watch over discriminatory practices. This body, however, lacks control over entry, mergers and rates.

The regulation of ocean vessels must be understood in the contexts of antitrust policy and international competition. After the transfer of interstate functions to the ICC in 1940, it had jurisdiction over "common carriers by water in foreign commerce," irrespective of their flag or the nationality of the owners, 196 and over domestic maritime commerce between the American mainland and Hawaii, Alaska, Puerto Rico, and the American territories. 197 Because the Shipping Act did not define the term "common carrier," the courts applied the common law definition in interpreting the Interstate Commerce Act. 198 The Shipping Act narrows this broad definition by requiring transportation "on regular routes from port to port," and by further providing that tramp ships are not deemed common carriers by water in foreign commerce. 199 Tramp ships operate without any prior commitment to certain ports of time schedules and carry mainly bulk cargo under highly competitive conditions. 200

Within the liner market, however, the statute and the enforcing agency have tried to enhance the regulatory power over as many corollary functions as possible. The Shipping Act subjects all kinds of wharfage, dock, warehouse, and other terminal facilities to the control of the Federal Maritime

195. The Shipping Board was reorganized four times and had five different names. See Note, Rate Regulation in Ocean Shipping, 78 HARV. L. REV. 635, 639-640 (1965).
Commission ("FMC"). The FMC has also resisted carriers' attempts to escape from regulation by running a shipping line on the basis of "contract carriage" or tramp shipping. Moreover, the FMC has extended the common carrier status to "nonvessel operating common carriers by water." These carriers are persons who hold themselves out to arrange ocean transportation in their own names without owning or operating the vessel. This includes ocean freight forwarders who are subject to FMC licensing and control and also rail or motor carriers who undertake to carry goods from inland point to inland point.

2. Duty to Serve

Over the years, the conference system seems to have generated a considerable overcapacity of tonnage and, therefore, diminished the motivation of carriers to refuse service. The Shipping Act does not contain an outright codification of the common law duty to carry, but indirectly, it restates this duty. The carrier is inhibited from retaliation against shippers patronizing other carries, and the refusal to carry is expressly listed among the retaliatory measures. More generally, a carrier declining to accept cargo tendered to him in good condition with full payment of freight charges may be refused a clearance for his vessel.

3. Liability

The carrier's liability for loss of and damage to goods during the carriage by water is subject to the 1893 Harter Act. Its historical background stems from the fact that American foreign commerce depended upon foreign, particularly British, tonnage at the end of the 19th century. Unlike American judges, the English courts allowed contractual exemptions from liability for negligence in bills of lading. Under the prevailing conditions of maritime commerce, shifting the risk to shippers gave British carriers an advantage over American carriers. American carriers requested protection and Congress granted it. The Harter Act essentially forbids clauses which relieve the shipowner from liability for negligence in procur-

201. 46 U.S.C. § 801 (Supp. IV 1980) ("other persons subject to this chapter").
202. 9 F.M.C. 56.
203. See the definition in 46 C.F.R. § 510.2(1) (1981).
204. 46 U.S.C. § 841(b) (1976).
205. See G. ULLMAN, supra note 185, at 36-38.
209. G. GILMORE & O. BLACK, supra note 97, at 141-142.
ing a seafaring vessel including crew and outfit or in handling the cargo. Once initial seaworthiness is established, the owner is free from liability for faults and errors in the navigation or management of the vessel.\(^{210}\) This legislation did not remove the differences with England, but rather stressed the need for international uniformity.\(^{211}\) After World War I, this target was met by the so-called Hague Rules, officially named the International Convention for the Unification of Certain Rules Relating to Bills of Lading, signed at Brussels on 25 August 1924.\(^{212}\) These rules follow the Harter Act, but yield to the carrying interests by a limitation of recovery to $500 (100£) per package. In 1936, the United States adopted the Convention and enacted its rules in the new Carriage of Goods by Sea Act ("COGSA").\(^{213}\)

The international uniformity has subsequently given way to divergent national practice brought about by technological innovations, such as the "container revolution". Currency exchange rate developments have also distorted the uniform liability limits fixed fifty years ago. The Visby Protocol of 1968 is designed to overcome interpretive differences in the Hague Rules by some specific amendments. Although it has come into force in some countries, it has not been ratified by the United States.\(^{214}\) Finally, a United Nations Conference held in Hamburg, West Germany, in 1978, adopted a new international convention on the carriage of goods by sea. It does away with the Harter Act scheme and makes carriers liable for the management and navigation of the vessel. Once this convention has received the required number of ratifications, it will replace the Hague Rules as amended by the Visby Protocol among its member countries.\(^{215}\)

**E. AIRLINE REGULATION PRIOR TO THE 1977-1978 DEREGULATION ACTS**

The separation of liability and economic regulation observed with regard to shipping is also true for the carriage by air.

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212. 51 Stat. 233, T.S. No. 931.


1. Rates and Other Economic Regulations

The present system of aviation regulation under the Civil Aeronautics Board (CAB) was established in the Civil Aeronautics Act of 1938 and was renewed with minor differences by the Federal Aviation Act (FAA) of 1958. In order to understand this legislation it is essential to bear in mind the infant state of the airline industry in the 1930’s. Carriers were relied on mainly for the transportation of mail. Airline markets of that time have been characterized as joint-product natural monopolies because "it was economic for only one carrier to transport the mail and impossible for an airline to be viable carrying passenger traffic alone." As a result of this market structure, the Postmaster General was the true regulator and subsidizing promoter of airbound commerce before 1938. Several legislative interventions tried to separate postal activities from the promotion of aviation. The mail was carried by the Army for some time, and after the return to private transportation, the Interstate Commerce Commission was charged with the supervision of airmail rates. But all of these attempts failed because the system of competitive bidding for airmail contracts was subject to repeated abuse in the form of destructively low bidding.

Discontent with the experiences under the airmail legislation was one of the major motives for the Civil Aeronautics Act. Other reasons of some weight were: (1) fear of excessive competition in general, even without the airmail contract bidding system; (2) the desire to stabilize the industry in order to attract investments; (3) the protection of small communities and (4) the protection of small carriers; (5) the determination not to allow chaotic conditions which had prevailed in surface transportation before 1935; and (6) the general propensity towards carrier regulation of the post-depression years.

The statute followed the pattern of the Interstate Commerce Act. It established the Civil Aeronautics Authority, now the Civil Aeronautics Board (CAB) to watch over entry, rates, anticompetitive practices or agree-

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220. For a comprehensive overview of the legislative history, see id. and especially Dempsey, The Rise and Fall of the Civil Aeronautics Board—Opening Wide the Floodgates of Entry, 11 TRANSP. L.J. 91, 95-108 (1979).
221. For a thorough discussion of entry control, see Dempsey, supra note 220, at 91.
ments, rate fixing and pooling agreements. Special regulations put airmail transportation under CAB control.

a. Regulated Carriers. The FAA regulates "air carriers" and "foreign air carriers". The activities governed by the statute, "interstate", "overseas", and "foreign air transportation", are defined as those of a common carrier engaged in the carriage of persons or property by air. Though the distinction of common and private carriage is basic to FAA jurisdiction it has rarely given rise to litigation. In fact, the common carrier concept seems to encompass every possible commercial operation of an aircraft, save a true lease or bare hull charter which confers possession and operative authority to the lessee and his crew. There is no doubt that charter flights, although unscheduled and irregular, are common carriage.

The CAB has made use of its power to exempt certain carriers with these limited operations. When carriers acquired the bigger aircraft available at the end of World War II, their operations expanded and became a serious competitive threat to the licensed airlines. Given the refusal of the CAB to issue new certificates of public necessity and convenience, the exempt carriers had to fight for their existence. After years of investigations, legal and political disputes, the supplemental air carriers were regulated and confined to all-charter and inclusive tour charter operations in 1962. Other groups of carriers operating under exemptions from CAB rate regulations are the numerous air taxis including the commuter carriers and the recently deregulated all-cargo carriers. In both cases, the carriers are only exempt from certain provisions of the FAA.

b. Rate Levels. The structure of rate regulation implemented in the FAA and in force until airline deregulation was commenced in 1977 resembles that under the Interstate Commerce Act. Carriers must file tariffs in-

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222. On the antitrust aspects, see W. JONES, supra note 100, at 1132.
227. Between 1950 and 1974, the Civil Aeronautics Board received seventy-nine applications for the license to provide scheduled domestic service—none were granted; see Dempsey, supra note 220, at 115.
229. 14 C.F.R. § 298.11 (1981). In 1973, there were about 2,900 air taxis. See W. JONES, supra note 100, at 1089.
cluding all classifications, regulations, and practices with the CAB. New tariffs become effective after 30 days notice unless the CAB suspends them for up to 180 more days, pending a hearing. If the CAB finds after hearing that the proposed rates are unjust, unreasonable or discriminatory, it may prescribe a minimum, maximum or precise rate.

In foreign air transportation, the CAB has the power to suspend new rates for a full year. The Board lacks the power to prescribe rates; it may only reject and cancel rates filed by a carrier. The absence of price fixing authority in foreign transportation is due to the post World War II desire to have rates fixed by an international airline cartel ("IATA") to enable smaller national flag carriers to fly in international markets for the sake of national prestige. The conception embraced the idea that the CAB would approve fare agreements and immunize them against antitrust scrutiny. It was embodied in international treaties like the so-called Bermuda Agreement between the United States and Great Britain. Beginning in the late 1950's, non-IATA and charter carriers diverted more and more traffic from the cartelized airlines and provoked a triple reaction. First, the cartel crumbled, its members offering numerous forms of discount fares. Second, the need for control of the non-aligned carriers became more obvious. Third, IATA faced increasing criticism. These motives resulted in the transfer of rate cancellation power to the CAB in 1972.

If the tools of the Board differ with respect to domestic and foreign transportation, the applicable standards are very similar. As laid down by the FAA, "the Board shall take into consideration, among other factors—

1. The effect of such rates upon the movement of traffic;
2. The need in the public interest for adequate and efficient transportation of persons and property by air carriers at the lowest cost consistent with the furnishing of such service;

(3) Such standards respecting the character and quality of service to be rendered by air carriers as may be prescribed by or pursuant to law;
(4) The inherent advantages of transportation by aircraft; and
(5) The need of each carrier for revenue sufficient to enable carrier, under honest, economical, and efficient management, to provide adequate and efficient air carrier service." 240

While the policy standards in foreign aviation are identical so far, here the Board must inquire in addition, "whether such rates will be predatory or tend to monopolize competition among air carriers and foreign air carriers in foreign air transportation." 241

Here again, as in railroad price control, we find potential bases for different rate policies. What the CAB in fact implements is the result of two large investigations, the General Passenger Fair Investigation of 1960, 242 and the Domestic Passenger Fare Investigation of the early 1970's. 243 Under the latter, rate computation proceeds in a classic way from the general revenue requirements of the carriers to the apportionment of these amounts to single operations. The fares must produce revenues sufficient to meet the costs, including a fair rate of return on investment, of the operations of the domestic trunkline industry as a whole. The initial step is therefore the computation not of individual firm costs, but of the industry costs. The fair rate of return is fixed at 12%.

c. Rate Discrimination. The prohibition of discrimination is elaborated in the FAA in a threefold way: (1) carriers must not discriminate against other carriers by prejudicial divisions of joint rates on through routes; 244 (2) carriers must adhere to their filed tariffs and not accord rebates or refunds; 245 and (3) more generally, carriers must not cause undue preference or prejudice to any particular person, port, locality, or description of traffic. 246

2. Duty To Carry

The common law duty to serve every applicant has been codified only with respect to domestic air transportation. 247 Though the point apparently has never been decided, one could argue that air carriers are subject to the

243. See the extensive quotations in W. Jones, supra note 100, at 1185 and the policy statement of February 7, 1975, 40 Fed. Reg. 6643 (codified as amended in 14 C.F.R. § 399.31-33 (1981)).
same duty in outbound foreign transportation. This is the common law rule for international shipping.248

While the FAA extends the duty to all transportation for which the carrier is authorized by certificate, the CAB seems to take a narrower view. Its rules concerning embargoes on property do not cover cases where the carrier refuses to carry goods "in accordance with restrictions and limitations in the tariff or certificate."249 Contrary to what these regulations suggest, it is submitted that the carrier's tariff can delineate his activities only insofar as its rules and regulations are of a technical nature and do not narrow the scope of the duty to serve fixed by the certificate.

3. Liability

The air carrier's liability for personal injury of passengers and loss of or damage to goods has three different bases. Foreign transportation of both passengers and goods is subject to the Warsaw Convention.250 Domestic liability for interstate flights with respect to personal injury and wrongful death claims is based on the common law of torts and the statutory law of the single states. Federal law governs baggage and cargo claims.251 The explanation given for the applicability of federal law is that Congress intended to regulate air transport comprehensively.252 This raises a question as to why state law governs in personal injury and wrongful death actions. The explanation is that the common law regarding carriage of passengers based liability upon negligence and did not allow the carrier to contract out of it. This area remained essentially a matter of tort, and the various wrongful death statutes of the individual states claimed application to aviation accidents. On the other hand, the courts allowed the common carrier of goods to lessen his strict liability by contract and to limit it to certain amounts of money, thereby placing liability for loss of and damage to goods

on a contractual basis governed by the carrier’s tariffs which, in turn, are subject to CAB control.

Under the common law governing the domestic transportation of passengers by air, the difference between common and private carriers is not decisive. Common carriers of passengers are not liable as insurers. Like private carriers, they are liable only for negligence. Yet, the distinction could be important, because some jurisdictions impose a duty of utmost care upon common carriers while private carriers have to exercise only the ordinary care under the existing circumstances. Moreover, in the assessment of the common carrier’s negligence, courts apply the rule of res ipso loquitor which frequently amounts to a reversal of the burden of proof.

In spite of these differences, only a few cases draw a distinction between common and private carriers. "Holding out" to the public is interpreted extensively and embraces scheduled airline flights as well as charter and air taxi operations. The latter may enter the category of private carriage, if performed on the basis of particular contracts. For the rest, private carriage seems to encompass only those flights which the carrier primarily performs for his own purposes.

The domestic transportation of cargo by air is exclusively regulated by the carrier’s tariff which, if valid, is the contract of carriage between the parties. Thus, the shipper-carrier relationship has become a contractual one, not focusing any more on the distinction of common and private carriers. The same is true for the domain of the Warsaw Convention. It applies to "all international transportation of persons, baggage, or goods performed by aircraft for hire," but also to "gratuitous transportation by aircraft performed by an air transportation enterprise."

Airline tariffs governing the domestic air transportation of baggage and cargo were subject to CAB control until 1977. Under the doctrine of "primary jurisdiction" of the Board, the courts abstained from scrutinizing approved tariffs for a long time so that CAB policy had a binding effect

256. See Arrow Aviation, Inc. v. Moore, 266 F.2d 488 (8th Cir. 1959); see generally Speiser & Krause, supra note 249, at 401.
258. Warsaw Convention, supra note 250, at art. 1(1).
260. Lichten v. Eastern Airlines, 189 F.2d 939 (2d Cir. 1951). The doctrine bypasses the scope of this paper; see generally Jaffe, Primary Jurisdiction, 77 Harv. L. Rev. 1032 (1964).
on tariffs. Not until 1976 and 1977, however, did the Board use its power to prescribe liability regulations. Before that time it approved tariffs without an officially formulated policy on this point. According to the approved tariffs, liability for loss and damage was based on the negligence of the carrier who sustained the burden of proving his exercise of due care.261 When the Board finally prescribed rules on liability, it set aside the different versions of negligence and declared a mandatory standard of strict liability subject to a list of exceptions, which embraced the classical common law exceptions as well as perils of the air, but not theft and fire. The deregulation of air transportation of cargo removed the Board’s power to prescribe regulations, and it is now up to the courts to decide upon the lawfulness of the tariff liability provisions. As the common law, though providing for strict liability in principle, does not oppose a contractual exoneration from damages incurred without the carrier’s fault,262 the progressive strict liability approach of the CAB was only an episode.

F. THE DISINTEGRATION OF THE LAW AND THE NEED FOR HARMONIZATION

On the eve of regulation, the growth of transportation firms into large monopolistic corporations had changed the economic and political balance in the carrier-shipper relationship. This change brought about modifications of the law which, as a whole, tended to lessen the rigor of the common carrier’s duties towards the shipper and to strengthen the contractual element and thereby the carrier’s position. The primary purpose of legislation and regulation was to reverse this trend and to protect the shipper. This situation remained unchanged until World War I. In fact, the amendments of the Interstate Commerce Act promulgated from 1887 to 1916 we inspired by the intention to repress the power of the railroads. The ICC received authority to prescribe maximum rates and suspend tariffs of the railroads and an increasing number of railway connected firms; the duty to serve was codified, and liability impeded. The railroads were so heavily regulated that investment declined and equipment decayed.

The state of the industry became obvious when specific transportation needs could not be satisfied in World War I, and an analogous scarcity of tonnage was felt in ocean shipping. Consequently U.S. transportation policy changed radically. Where protection of shippers had been the prevailing motive for decades, promotion of railroads and shipping now became a concern of at least equal force. After a brief and discouraging experience

has recently been rejected in the air carrier liability case Klicker v. Northwest Airlines, 563 F.2d 1310 (9th Cir. 1977).


262. In Klicker v. Northwest Airlines, 563 F.2d 1310 (9th Cir. 1977), the court voided a tariff clause whereby the defendant air carrier exonerated himself from the liability for injury to live animals.
with direct government control over railroads, the Transportation Act of 1920 restored private enterprise and gave the ICC the power to prescribe minimum rates. Similarly, regulation and promotion are interwoven in the official toleration of liner conferences granted by the Shipping Act of 1916.

The entrustment of promotional tasks to the agencies in one sense completed their regulatory power. Striking the balance between shippers and carriers necessarily involved a case-by-case determination of the agency. In the administrative process, some groups of shippers prevailed over their carriers while others succumbed to the carrying interests. While the ICC had been concerned with the services, prices and the apportionment of risks between the shippers and carriers for a long time, it now took over the additional function of distributing transportation resources among different groups of shippers. Every rate proceeding became the potential forum for this general struggle.

This new function was stressed when trucks and barges broke the railroad monopoly in surface transportation in the 1930's. Intermodal competition endangered the cross-subsidization among different shipper groups as the high-charged shippers were induced to patronize cheaper motor or water carriers. As a result, the ICC tried to protect the railroads by the extension of their rate structure to other carriers who were, at least initially, deprived of the possibility to pass on their inherent cost advantages to the shipping public. The ICC consciously grappled with the exceedingly difficult task of promoting economic justice in three different relationships at the same time:

1. between shipper and carrier;
2. between carriers, especially those of different modes;
3. between different groups of shippers such as different industries and different regions.

Except for the absence of intermodal competition, one finds a similar variety of regulatory aims in aviation and ocean shipping. It is easy to understand that whatever action is taken to achieve one of the listed targets, it is likely to have repercussions on the other two levels. It has become clear that economic control by means of transport regulation cannot accomplish all of its ends. This insight provided the impetus for deregulation which will be analyzed in Part II of this article, to be published in volume XIII, No.2.
Rollin' On . . . To a Free Market
Motor Carrier Regulation 1935-1980

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America has always looked to the transportation industry for its heroes. The wagonmaster, the sea captain, the locomotive engineer and the airline pilot all had their place in the spotlight. Today, the popular culture hero, as expressed in country-western music and southern-oriented movies, is the over-the-road truck driver.

This glorification of the truck driver has been accompanied by a lessening of the regulatory shackles which limited the flexibility of the trucking business. Passage of the Motor Carrier Act of 1980\textsuperscript{1} ushered in a new era of free entry and increased competition on our nation’s highways. The industry is far from being deregulated—the ICC is still operating and the tariff principle still stands, but it is clear that following the lead of the Airline Deregulation Act,\textsuperscript{2} Congress has intended to deregulate still another industry in order to eliminate cartel pricing and to check inflation in transportation costs.

\textbf{I. Nature of the Industry}

Over-the-road trucking is a relatively new industry, with a pedigree about as old as the airlines. The condition of roads prior to the First World War made long-distance hauling impractical, and a heavy duty chassis suitable for hauling goods did not appear until the middle 1920’s. Early trucks developed as drayage vehicles, hauling freight to railroads whence the rail-

\begin{itemize}
\item \textsuperscript{1} 49 U.S.C. § 10101 (Supp. IV 1980).
\end{itemize}
roads would carry it on their superior rights-of-way. Railroads at this time had a virtual freight monopoly. The towboat had not yet emerged on the nation’s rivers and the few aircraft which were in service were regarded as passenger and mail vehicles exclusively.

Most railroads viewed the motor carrier as adjunct to their operations. Railroads were quick to establish subsidiary motor carriers which funnelled traffic to the railroads’ routes. These motor carriers often operated buses as well as trucks, and soon were viewed as a replacement for branch lines which were to be abandoned by the railroads.3

Before long, the infant motor carrier industry had reached a level of utility surpassing that of the interurban electric railroads, which had flourished in the earlier years of the century. The interurbans were beaten down by cost of constructing rights-of-way and by the intransigence of the steam railroads, which refused to let them cross their rights-of-way at grade or interchange freight with them. These barriers to entry were not a problem for the trucking lines, which could operate on public highways without the necessity of constructing their own facilities.

The arrival of the Great Depression brought a downturn in production, but did not appreciably slow the growth of intercity trucking. For one thing, an all-weather system of roads was already in place. For another, the slowdown in heavy industry was not paralleled by an equivalent curtailment of light manufacturing, which tended to favor the truckers. Freedom of entry into the market place meant that although some truckers failed, others were able to take their place.

By the 1930’s, it was clear that trucking was much more than incidental-to-rail drayage activities. The motor truck had more than supplanted the horse and wagon; it was in a position to challenge the iron horse as well. This was especially true with respect to high-valued shipments. The truck could go from door to door without any incidental switching. Due to the mobility and efficiency of the tractor-trailer, trucks were better suited to protect valuable shipments and make timely deliveries than were the railroads.

Even at this juncture, there was little thought of the motor carrier operations as a separate industry. Rather, trucking developed in many different categories:

1. Local trucking operations. Dealing mostly with small packages, these smaller trucks handled local delivery, often in connection with rail freight or Railway Express Agency operations.

2. Over-the-road carriage. These companies operated in competition with railroads, specializing in high-class freight on overnight schedules.

They maintained rudimentary terminals in each of the cities, and usually adhered to a regular schedule.

3. Intercity buses. Replacing the interurban electrics and the branchline mixed train, these companies had expanded from the feeder service which gave them birth. They now operated a cheaper, slower service which was nonetheless competitive with railroads between major cities. On the philosophy of if you can’t lick’em, join’em, railroads purchased several of these intercity operations and formed the bases for today’s Greyhound and Trailways systems. Buses have always carried some freight, usually in parcel express service in the same vehicle with the passengers.

4. Railroad subsidiaries. Most railroads by the 1930’s used trucks for pickup and delivery services. In addition, they had substituted trucks for abandoned branchlines. One of the largest of these was the New England Transportation Company, a regional bus and truck system which paralleled and supplemented the routes of the parent New Haven Railroad.

5. Independent truckers. These were the so-called "gypsies", family-owned operations which took on loads wherever they could find them and moved on irregular routes throughout the country. Many of these marginal carriers obtained valuable assets in the form of route rights through the "grandfathering" of authority in the Motor Carrier Act of 1935.

6. The mob. There were plenty of trucks left over from bootlegging and rumrunning operations after the end of Prohibition. The influence of organized crime, which was attempting to get into more legitimate pastimes, was an important factor in the call for regulation of the industry.

7. Agricultural transportation. Although bulk commodities, such as grain, even today can only move economically by train or barge, the emergence of the farm truck made the farmer less dependent upon the local general store and the country elevator. The truck and the rural road improvements of the 1920’s were important elements in freeing the farmer from the dominance of the railroads. As a result of agricultural insistence, transportation of agricultural products has been exempted from economic regulation throughout the history of regulation of motor carriage.

The truck, with its ability to provide door-to-door transportation, became a strong competitor for intercity freight. It remains an expensive mode, however, because of its lack of fuel economy and labor-intensiveness (every load requires at least one driver) as compared to barge and rail transportation. As highway systems improved, the gentler grades of limited-access roads proved to be a boon to truck scheduling. The truck is able to better the time of freight trains, because of the time that freight cars stay in classification yards waiting to be switched. In price, truck delivery is usually lower than air freight and higher than rail.

The trucking system of the United States is privately owned and oper-
ated by non-rail interests. This is somewhat of an anomaly among the world's transportation systems. In some nations, such as Ireland, the government owns both rail and road transportation systems and operates them as an integrated whole. In most Western European countries, private truckers operate under severe restrictions, to prevent siphoning of traffic from the government-owned railways. In Canada, motor carriers are regulated by provincial authorities. There is little transcontinental hauling of freight by truck in Canada.

II. THE CALL FOR REGULATION

Up until 1925, motor carriers, if they were regulated, were totally under state control (very much like the provincial situation in Canada). Carriers operating in different states had to obtain authority from each jurisdiction through which they passed (they still must obtain license plates today).

All this changed with the decision of the Supreme Court in Buck v. Kuykendall.4 This proceeding involved a motor carrier who applied to the state of Washington for authority to operate between Seattle and Portland. The application was denied, with Washington's regulatory commission stating that there was already adequate rail and highway service between the two cities.

The Supreme Court, on appeal, held that such a denial was beyond the authority of the state of Washington. Inasmuch as the trucks crossed the Columbia River into Oregon, they were operating in interstate commerce. Constitutionally, a state could not forbid, limit or prohibit competition in interstate commerce. (At the time, the state of Oregon was willing to grant Buck authority to operate in that state.)

The effect of Buck v. Kuykendall was to eliminate state controls on entry for motor carriers, limiting regulation by states of interstate service to historic police power areas of motor vehicle safety and highway conservation.5 At the time of Buck v. Kuykendall, some forty states required operators of trucks to obtain certificates of public convenience and necessity, regardless of whether they operated in interstate or intrastate commerce. The Buck decision impelled efforts to seek a federal solution to the problem of the regulation of interstate motor carriage. The Interstate Commerce Commission already exerted plenary powers over the operations of railroads. It was logical that Congress should look to that body for the expertise necessary to regulate this new form of transportation.

The rationale which advocates of regulation stressed included several arguments which favored continuity of service over competition. There were few financial barriers to entry into the trucking business such as con-

5. Webb, supra note 3, at 92.
struction in the railroad industry. During the depression years, an unemployed truck owner might drive just for gas money, or to make payments on a truck. When the inevitable happened and the truck needed repairs, the driver might withdraw from the market, but another trucker would be there to take his place. This cut-rate transportation was a threat to established truck lines and railroads alike.

Justifications for entry controls were given in the following order of importance.

A. Prevention of an Oversupply of Transportation. ICC Commissioner Eastman stated in hearings before the Senate Interstate Commerce Committee in 1935:

The most important thing, I think, is the prevention of an oversupply of transportation; in other words, an oversupply which will sap and weaken the transportation system rather than strengthen it. In the case of railroads that was done in 1920 by the provision that prior to any new construction a certificate of convenience and necessity must be secured from the Commission. In my judgment it would have been much better if there had been such a provision many years before. It would have prevented certain railroad construction which tends to weaken the railroad system and situation at the present time. The States have, I think, in all cases, found the necessity in their regulation of motor transportation to provide for that prevention of an oversupply. It is a provision which has been adopted in most of the foreign countries that I have inquired into; in other words, the granting of certificates or permits in order to prevent an oversupply which weakens the situation.\(^6\)

In other words, many experts believed that if too many motor carriers competed on the same route, no money could be made from the service. It was this rationale which caused the ICC, for 45 years, to protect incumbent carriers against new competitors.

B. Equality of Regulation. At this time, railroads were fully regulated. It was thought to be unfair to continue this regulation while the motor carriers, operating on parallel and competing routes, would be unregulated. In addition, intrastate carriers were regulated by the individual states; it seemed unfair to allow the one out of five trucks which crosses a state line to be able to disregard state law.\(^7\)

C. Interdependence of Entry Controls and Enforcement. Suspension or revocation of a carrier’s license is a useful enforcement tool, and most of the studies prior to 1935 which dealt with regulation assumed that control of entry would be part of the system. This was the regulatory scheme under which most states operated.

Interestingly, most of the concern voiced by Congress was about bus operators. The Motor Carrier Act of 1935 required brokers of passenger

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\(^7\) Webb, supra note 3, at 97.
transportation to deal only with certificated carriers. The ICC had found in a 1928 report that, although intercity bus service was generally satisfactory, so-called "wildcatters" were cutting fares below compensatory levels and otherwise engaging in reprehensible practices. Federal regulation was supposed to end such practices but no thought was given to whether such entry control was necessary for the prevention of these practices.

In short, Congress was pressured by the states, most of which had comprehensive schemes for regulating intrastate motor vehicles, to eliminate these "wildcatters." These regulatory systems were in danger of collapse because of the prohibition against states' regulating interstate traffic. In addition, reasons were being offered for departure from a free market. The free market was considered chaotic and prone to cut-throat competition. Shippers were allegedly being victimized by fly-by-night operators.

Lined up behind the state regulatory agencies in calling for a program limiting entry and regulating rates were many groups interested in the motor carriage industry. The railroads, feeling the unfair competition since they were regulated themselves, were prime supporters of putting trucks and buses under the same regulatory umbrella. The "grandfather" provisions of the Motor Carrier Act would protect the operating rights of the rails' motor carrier subsidiaries. At the same time, new entrants in the field would be curtailed, and rates would have to be just and reasonable.

The emerging intercity trucking companies and bus lines also supported regulation for similar reasons. It would grant them rights to serve territories they were already serving. At the same time, regulation would protect their services against "cream-skimming" by operators who would come in to take the excess, profitable traffic. These established carriers were bound by common carrier obligations to take all traffic preferred them, and did not wish to see their position jeopardized by upstart companies which could pick and choose traffic and operate at random.

Agricultural interests saw regulation of trucking as carrying an obligation to serve small towns and local market areas that otherwise might be bypassed in an uncontrolled market. Farm interests, however, lobbied against any regulation of the transportation of agricultural products. The farmers wanted to be free to haul their own, or their neighbor's produce to market without any interference by regulatory authorities. In contrast to rail regulation, where all commodities were regulated, agricultural products were specifically exempted from regulation by the ICC.

One of the interest groups supporting this call for regulation was the small, independent truckers. They realized that the "grandfather" provi-

sion would give them authority to operate over routes which they currently were serving. This would be a valuable, marketable asset in the future and would also protect them against new independent companies. A struggling family-owned trucking operation would suddenly have something of value (operating rights) conferred upon them free of charge. These new entrepreneurs were quick to see the possibilities of the new legislation.

Utility-type regulation was thus adopted for an industry which had few characteristics of a natural monopoly. Continuity of service was one lauded characteristic. The bus rider would rather have the certainty of having the Greyhound every day at a fixed schedule than have rate competition but uncertain service. Small towns would prefer to have a guarantee of service by a single carrier than sporadic competitive efforts by a number of struggling operations. In addition, motor carriers should be sufficiently solvent to pay claims or fix up their equipment. These considerations were important, and regulation had strong appeal due to the economic climate of the 1930's. The best way to implement the regulations that were perceived as being needed was to allow the ICC, with its fifty years of transportation experience, to administer it.

III. THE MOTOR CARRIER ACT OF 1935

Enactment of the Motor Carrier Act of 1935\(^\text{10}\) more than doubled the jurisdiction of the Interstate Commerce Commission and changed its focus from a railroad agency to one concerned with all surface transportation.\(^\text{11}\) As an umbrella agency, the Commission was charged with protecting not only the public but the economic existence of rail, motor and water carriers. Private carriers were exempted from regulation; anyone might haul his own goods in his own trucks. Agriculture was specifically exempted by law, as was local and occasional transportation. Otherwise, the interstate motor carrier industry was subject to strict controls on entry and rates.

Those individuals and firms operating trucks on the highways at the time of enactment of the Motor Carrier Act were grandfathered into certificates and protected from further competition. New carriers would be required to follow ICC procedures to obtain the authority that would allow them to haul for hire. Trucks and buses were considered under the same regulatory scheme, and a similar regime was adopted for entry of air carriers in the Civil Aeronautics Act of 1938.\(^\text{12}\)

\(^{10}\) Act of Aug. 9, 1935, ch. 498, 49 Stat. 543.


A. MOTOR COMMON CARRIERS

A common carrier has the obligation to serve all customers fairly and equally and hold itself open to the general public for carriage of people or goods. This is the same common-law obligation which had attached to the nation's railroads. Common carriers were required to have a certificate from the ICC, stating that the public convenience and necessity require its services. The term "public convenience and necessity" is not defined in the Interstate Commerce Act. In an early decision, Pan American Bus Lines Operations 13 established three considerations to be weighed in determining whether an applicant's proposed operations would satisfy this criterion:

1. Is there a public demand or need for the service?
2. Can this need be served as well by existing carriers?
3. Can the new operation serve the public demand without endangering the operation of existing carriers?

Professor Dempsey suggests that this test boils down to balancing the advantages to shippers or passengers of the new motor carrier as opposed to the actual or potential disadvantages to existing carriers which might result from the institution of particular shipping operations. 14

Under the scheme of the Motor Carrier Act, the typical application involves an applicant who either wants to get into the motor carriage business or to expand present operations. The application is made to the Interstate Commerce Commission, with supporting statements from shippers who say they would use his service if authority was granted. The application is detailed as to what commodities are to be handled and over which routes. Usually, the application is protested by existing common carriers who fear diversion of traffic. Subsequent to a conference with the protesters, the application may be amended to limit the authority sought. The imposition of these limitations may cause the protestant to withdraw his opposition. Even in the absence of opposition, however, the carrier must establish a prima facie case of the need for proposed operations. 15 Protestants must demonstrate their operating authority and their willingness and ability to handle the shipper's traffic. The applicant may, in turn, show that population or business along the route has increased to the extent that there is enough business for the newcomer as well as existing carriers. 16

In addition to the public need for the service, the Commission looks at the services of existing carriers. The Commission has imposed an affirmative duty on shippers to inform themselves about which carriers serve their routes before they seek additional motor carriers. But when a carrier proposed a unique type of transportation service which existing carriers do not

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13. 1 M.C.C. 190, 203 (1936).
or will not offer, the ICC often concludes that the public should have the benefits of the new service, even if it might divert traffic from existing carriers.\textsuperscript{17} However, the general trend at the ICC has been to allow existing carriers to handle the traffic which is within their territory.

The ICC has been wary of allowing too many carriers in a market, for fear of diluting the traffic to the level where no one would survive. This concern, however, has been limited to motor carriers. Railroads have been unsuccessful in blocking competitive motor carrier service, since the Commission has long believed that shippers should have the benefits of both modes, wherever possible.

When there has been an increase in traffic, the ICC has been more ready to allow new carriers to serve a market. The last part of the Pan-American tripartite test is whether new carriers can serve the market without endangering other carriers. Competition has not, until recently, been a major factor in ICC considerations. In Bowman Transportation, Inc. v. Arkansas-Best Freight System, Inc.,\textsuperscript{18} however, the United States Supreme Court decided that the benefits of competitive service to consumers might outweigh the discomforts which existing certificated carriers could feel as a result of new entry, and that a policy of facilitating competitive market structure and performance was entitled to consideration.

\textbf{B. Motor Contract Carriers}

Although the restrictions on entering the field of common carriage were rigorous, the Commission provided for alternative transportation by its issuance of permits for contract carriers. Statutory authority was supplied by Section 203(a)(15) of the Motor Carrier Act, which specifically allowed such a permit for a motor carrier who engages in for-hire transportation;

under continuing contracts with one person 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 needs of each individual customer.\textsuperscript{19}

The policy for allowing such services was to help shippers who might otherwise be forced to buy their own trucks for private carriage. It made allowance for the special needs of shippers which ordinary carriers were unwilling or unable to meet. It was, of course, a departure from the tariff principle, as the contract carrier establishes by contract, rather than by filing a tariff with the ICC, what the service will cost. A contract carrier is not required to serve the general public; rather, the law limited him to "a limited

\textsuperscript{17} Id. at 740; see Kroblin Refrig. Xpress, Inc., Extension—Morrow, 125 M.C.C. 354, 359 (1976).
\textsuperscript{18} 419 U.S. 281, 293 (1974).
\textsuperscript{19} 49 U.S.C. § 309(b) (1970); see Dempsey, supra note 11, at 753 n.110.
number of persons.” For many years the ICC relied upon the "rule of eight" established in the Umthun Trucking case. Under this principle, the operations of a carrier with more than eight contracted shippers would be watched closely to see whether or not it would be more appropriate for the carrier to operate as a common carrier. The United States Supreme Court held in ICC v. J.T. Transport that consideration must be given to the specialized transportation requirements of the supporting shipper, the manner in which the applicant proposes to satisfy them, and whether they may be satisfied as well as protesters.

Contract carriage is a statutorily authorized exception to the cartelization of the industry brought upon by limitation of entry and the grandfathering of early operators. It was perceived as a necessary exception, provided the number of shippers was in fact limited to a minimum. The most persuasive showing was that service would be provided to a single contractual shipper. The larger the number of shippers a carrier served, the less acceptable would be its application. "Dual operations," i.e. the holding of both common and contract carrier authority for the same area by the same carrier, was frowned upon by the Commission, which saw in dual operations the opportunity to discriminate in favor of one large contractual shipper against smaller shippers in the area who would have to abide by a published tariff.

Contract carriage, as well as exempt transportation and private trucking, were exceptions to the utility-type regulation of the industry. Contract carriers were generally smaller operators than the large trucking lines, and provided a specialized service that was often an extension of the production line of the shipper. Since the contract authority often limited such carriers to a plant-site, terminals and other expensive infrastructures were not needed. It was generally easier for a firm to gain entry into the trucking business as a contract carrier rather than as a common carrier.

C. CONTROL OF RATES

Another important factor for stabilizing the structure of the industry is the ICC control of rates as a method to regulate competition. Rate regulation of motor carrier services is based upon the principles of regulating railroad rates, and is similar to utility rate regulation. The Motor Carrier Act provided as follows:

22. Dempsey, supra note 11, at 757.
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.\(^{24}\)

The intent of Congress was that the rate charged reflect the value of service rather than competitive conditions. The antidiscrimination provisions, common in the transportation industry, were intended to insure that no illegal rebates, kickbacks or other practices favoring one shipper at the expense of others were employed in the transportation industry. The result, however, was that estoppel did not exist in the motor carrier business. A moving company would give you an estimate for moving your household furniture to Florida, but when you arrived there, the company had to adhere to the tariff, not a binding estimate. To do otherwise would be giving you an undeserved and illegal rebate.

Former ICC Chairman Daniel O’Neal wrote:

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.\(^{25}\)

The small shippers whom O’Neal writes of are predominantly small businesses, using motor carrier services in an attempt to compete with larger firms. Abandonment of the tariff principle would disadvantage such small shippers. As for the individual, usually the only area where he has much dealing with motor carriers is as a user of bus service, household goods movers, and package express, whether provided by the bus companies or United Parcel Service.

A rate system which avoids fluctuations results in more solvent carriers and more reliable services. It also makes rates a predictable matter in figuring distribution costs. The tariff principle primarily concerns common carri-


\(^{25}\) Id.
ers. Contract carriers must publish their rates and abide by them (until 1957 they were only required to publish minimum rates). The ICC had the power to prescribe minimum rates for contract carriers, but not maximum rates.26

Motor carrier rates are essentially carrier-made rates, subject to the approval of the Interstate Commerce Commission. The carrier initiates a rate by publishing them in tariffs which are filed with the Commission between 30 and 45 days before they are to become effective.27 A protest to this rate may be made by any interested party, except that a rate bureau may not protest a rate filed by one of its members. If the Commission agrees that the proposed rates are reasonable, they go into effect without an investigation. However, if the Commission thinks that the proposal may result in unlawful rates, it can investigate the rate and suspend the change. Where a proposed increase is not suspended but is investigated and later found unlawful, it is ordered to be cancelled. The ICC is without power to order refunds of motor carrier rates.28 After a rate has gone into effect without investigation, shippers may challenge its lawfulness by filing a complaint. If the rate is found to be unlawful, it may be cancelled by the ICC.29

Rates must be "just and reasonable", but those terms are not included in the statute. In the railroad case of United States v. Chicago, Milwaukee, St. Paul & Pacific Railroad,30 Justice Cardozo spoke of a "zone of reasonableness" between maxima and minima rates, and this concept seems to have been brought into motor carrier ratemaking as well. A rate that does not move the traffic may result in an embargo and thus be prima facie unjust and unreasonable. Discriminatory rates are those which give preferential or prejudicial rates to certain shippers. Increased competition has produced a trend toward taking cost, more than value of service, into effect for pricing. But for a long time, trucks could safely price their services considerably higher than railroad rates, and benefit from the lack of competition, thus keeping rates at a higher level than a competitive market would presumably allow.

Rates proposed by carriers fall into two categories: general rate increases and increases on specific commodities. General rate increases are across-the-board raises in tariffs due to general cost factors within the industry. Specific rates apply only to certain movements and are often made for competitive reasons.

As with the railroads, motor carriers have banded together in price-setting conferences called rate bureaus. Rate bureaus started to emerge

26. Id. at 318.
28. O'Neal, supra note 24, at 320.
29. Id. at 321.
immediately after the passage of the Motor Carrier Act. Today there are ten major motor carrier rate bureaus.31 The Reed-Bulwinkle Act of 1948 granted antitrust immunity to those who make, carry out, and act in conformity with the terms of a collective ratemaking agreement if the agreement has been approved by the Interstate Commerce Commission.32 Parties to rate bureaus have the right to take independent action at any time. Whatever the benefits of rate bureaus may be, it is clear that their existence is due to the regulation of the industry by the ICC. Without ICC regulation, the joint actions of rate bureaus would be subject to antitrust laws and individual publishing by truck lines would become the rule, rather than the exception. The benefits of joint ratemaking by connecting carriers might be lost as the carriers would be dissuaded from even discussing rates with one another.

D. REGULATION OF ROUTES

Entry to the trucking business requires ICC authority which specifies what commodities may be handled and what territory may be served. If specific highways and intermediate points are required to be followed, the carrier is considered to be serving ““regulate routes””, while if no particular routing is specified, the carrier is authorized to use ““irregular routes””, i.e. it may take whatever route is convenient.

General commodities carriers and bus lines were limited to regular routes. The philosophy seems to have been that local communities along these lines could thus depend on regular service by the bus or truck for handling small shipments or passengers, usually on a fixed schedule, every day. There were some deviations allowed; a small town within a mile or two of the designated route could be served, and trucks or buses could deviate from the designated highway if a paralleling Interstate highway was built. (Greyhound and many other intercity bus lines did just that, which resulted in an abandonment of service to small towns once located on the Greyhound route).

Carriers of specific commodities generally did not have to adhere to regular routes. The irregular routes could be from or to one particular point (radial authority) or unrestricted operations within a certain territory (nonradial authority) or merely between two designated cities.33 When a carrier had two separate grants of authority, but both included a single point, the operator could ““tack”” the two authorities together through the ““gateway”” city. Thus, a carrier who had rights to operate between New

33. Radial authority could be expressed as: between New Orleans, on the one hand, and, on the other, points in Texas, Mississippi, and Arkansas. Non-radial authority could be expressed as: between points in Alabama, Mississippi, and Georgia.
Orleans and Dallas and who later acquired authority to haul between Dallas and points East of the Mississippi River, could transport freight between New Orleans and the East, providing that he first operated through Dallas. Of course, the carrier would then try to eliminate the Dallas gateway in another ICC proceeding, which would then be contested by other carriers who had direct authority between New Orleans and the East Coast. Authority might be limited to the haul of a specific commodity in one direction only (machine parts from Detroit to the Pacific Coast), impelling the carrier to return empty. Circuitous regular routes, gateway restrictions, and empty backhauls were among the fuel-wasting results of regulation which were so vociferously denounced by advocates of deregulation of motor carriage.

E. Fitness

A threshold qualification for any carrier to receive authority from the ICC is a finding that the carrier is fit, willing and able to perform properly the proposed service and to comply with the provisions of the Interstate Commerce Act. Public need is not enough; there must be some weeding out of carriers whose conduct demonstrates an inability or unwillingness to perform motor carrier operations lawfully. The carrier has the burden of proof in refuting its prior behavior if it is applying for additional authority, despite having formerly been in violation of the Act. Fitness goes to the financial capabilities of the applicant, its willingness to obey the rules of the Commission, and its ability to safely and properly perform the proposed service.

If a shipper needs a proposed service and the ICC denies an application because of lack of fitness, the ICC may grant temporary authority to a motor carrier while questions arising from fitness are resolved. Temporary authority is a useful device by which the ICC awards operating rights for a limited time while certain conditions prevail. A railroad strike or natural disaster might result in temporary authority to motor carriers to provide increased service to an area. In 1979, the ICC granted unrestricted temporary authority to intercity bus operators during a period of acute gasoline shortages.

Permanent authority, on the other hand, is an entitlement that may not be removed without due process being awarded to the licensee. The system adopted by the ICC does not follow the temporary, renewable authority favored by the Federal Communications Commission for broadcasters. Rather, the system represents a permanent entitlement very much like the license a state grants to follow a particular profession.

This operating authority constituted a valuable property right to motor carriers. Many insolvent companies were bought at a good price just be-

34. Dempsey, supra note 11, at 759 & n. 134.
cause of the worth of the operating authority it held. Upon passage of the Motor Carrier Act of 1980, these operating rights were written off by many companies as having a zero value. The increased competition allowed by the new law resulted in a diminution of the value of these operating rights to near zero.

The scheme envisioned by the Motor Carrier Act encompassed a broad regulation of activities of intercity motor carriers, similar to that of railroads and, later, airlines. The highways may have been built with public moneys, but their use was restricted to carriers lucky enough to have received authority from the ICC. Some of the authority was obtained by applications for certificates of public convenience and necessity, but many carriers trace their origin to the fact that an ancestor was running a truck on the highways in early 1935. Similarly, no rhyme nor reason existed for the awarding of most authority, which was fragmented in nature. The original grants of authority coincided with the territories and commodities handled in 1935. Later grants were awarded when there was public need and where the competitive balance was not upset by the new arrival.

Unlike the railroads, regulation of motor carriers was never total. Private carriage and exempt trucking operations have always accounted for a significant part of the nation's freight traffic. Nonetheless, through mergers (for which ICC authority was necessary), local trucking companies grew to an extent where they could provide coast-to-coast service and be major competitors to the railroads. By protecting carriers from new competition and by keeping rates at a level where profits were guaranteed, the ICC helped assure the emergence of a trucking oligopoly.

IV. DEVELOPMENT OF THE INDUSTRY UNDER REGULATION

The lobbying group for the trucking industry is called the American Trucking Associations. The plural form of the name is appropriate, since the motor carrier industry really contains several different industrial groupings and entities, performing all types of different services.

A. COMMON CARRIER TRUCKERS

These include the giants of the industry, the big nationwide trucking companies whose billboard trailers are found on all highways. Common carriers can also be small independent truckers providing a local service which just happens to cross state lines. The largest companies are the carriers of general commodities. They operate semi-trailers, sometimes in double-bottoms (where state laws allow) and sometimes do away with over-the-road trucking altogether, arranging for pickup and delivery and having
intermediate hauling done by the railroads in TOFC\textsuperscript{36} service. Common carriers of general commodities follow regular routes and operate by published schedules.

A constraint in the general-commodities trucking business is the necessity for terminals. The terminal facilities may be less elaborate than railroad yards or airport cargo areas, but they are necessary for the transfer of freight from local delivery trucks to the big semi-trailers, classification of freight, handling of small shipments and consolidating shipments to the main destinations. A concern which has been voiced by representatives of small shippers and small communities is that deregulation would allow new entrants to cream-skim profitable traffic, leaving the major carriers with the expense of operating these large terminals for reduced traffic. Physical constraints of terminals also serve to limit the amount of shipments which can be handled at a given location, and may militate against new entries into a market. If the existing terminal cannot or will not handle your trucks, and if you cannot afford to build or acquire your own, you might think twice about serving a particular community. The existence of adequate terminals has the greatest effect on the small shipper; the large concerns which can fill a daily truckload at its plant site may not worry about such considerations.

Large carriers came about because of consolidation of smaller companies with the approval of the ICC. In passing upon a proposed consolidation, the ICC is required to give weight to such matters as the effect of the proposed consolidation upon adequate transportation service to the public, effect on competing carriers, total fixed charges resulting from the transaction and the interest of the carrier employees affected. In 1944, the Commission authorized the formation of Associated Transport, Inc., which embraced most of the major carriers along the eastern seaboard between Massachusetts and Florida.\textsuperscript{37}

Motor carriers were first subject to regulation by the Motor Carrier Act of 1935 which included Commission power to immunize transactions from the antitrust laws if "consistent with the public interest." In 1940 Section 5(2) of the Act was enacted\textsuperscript{38} which gave the Commission plenary power over consolidations and mergers. Seeking consolidations of terminals and economies of scale, the Commission has favored single-line service and the expansion of major trucking companies in the general-commodity long-haul carrier business.\textsuperscript{39} These companies generally own their own fleets of trac-

\textsuperscript{36} Trailer on flat car. Recently, the ICC has moved to completely deregulate the TOFC (or piggyback) business.

\textsuperscript{37} McLean Trucking Co. v. United States, 321 U.S. 67 (1944).


tors and trailers and deal with drivers who are represented by the International Brotherhood of Teamsters.

B. Owner-Operators

At the other extreme from the Associated Transports are the owner-operators. Special provision for owner-operators was not made until passage of the Motor Carrier Act of 1980.40 As individual entrepreneurs, they owned their own trucks, painted them in decorative color schemes, and operated on irregular schedules. Barred from competing head-to-head with the major trucking companies, owner-operators worked on a number of bases. Some managed to obtain some authority for themselves as contract or even common carriers on limited routes. Some leased their equipment to operators with authority. Others hauled only exempt products, such as agricultural produce. Still others hired themselves out to companies who shipped their own products in interplant hauling, in lieu of private carriage. There were truckers who went through the motions of “buying” the shipment and “selling” it at the other end, so that they could be considered private carriers, handling their own property only. Finally, there was a substantial number of gypsy truckers who operated outside the law, hauling in violation of the Interstate Commerce Act, at whatever rate they could get from a shipper.

With fixed costs to meet, the over-the-road independent trucker was often forced to cut rates low in order to have enough business to make the payments on his truck. He would often write off his own labor as worthless. Owner-operators would also push the hours-of-service law to the maximum without regard to the risks involved.

C. Intrastate Truckers

On a smaller scale than the big interstate trucking companies are the local or intrastate truckers. As operators within a single state, these companies were exempt from ICC regulation, even though many shipments might originate out of state with another carrier.41 In some cases, trailers might be delivered into a state by one carrier, and delivered to a final destination by an intrastate carrier. Since “commercial zones” and “terminal areas” around major cities were exempt from regulation, a carrier might also be able to deliver and pick up in a neighboring state, if it were within the commercial zone of a city within the state for which it had authority. (Kansas City, KS-MO; Philadelphia-Camden, PA-NJ; Portland-Vancouver, OR-WA are examples).

Although exempt from Federal regulation, intrastate truckers needed

41. 49 U.S.C. § 10525 (Sup. IV 1980).
authority from the state in which they operated. Most states had licensing schemes similar to that of the Federal government, calling for certificates of public convenience and necessity and control of rates by the State Public Service Commission or similar body. State regulation of interstate carriers was pre-empted by the ICC in 1935, but the states still retained control over intrastate tariffs filed by these carriers. State regulation is older than ICC regulation, but recently there have been some sunset provisions. In 1979, Florida deregulated all control by the state over intrastate buses and trucks. In that state there is free entry, exit and ratemaking. Other states have considered sunset laws for their motor carrier regulation. State regulation of common carriers cannot be a burden on interstate commerce; i.e. intrastate rates cannot be so low as to discourage the shipment of goods across state lines.42

D. AGRICULTURAL TRUCKING

Farmers are one of the greatest users of trucks for hauling their commodities. With grain, the haul is usually to the nearest elevator, while with many so called "truck garden" crops, the haul is to the marketplace by trucks. Farm vehicles were intended to remain in an unregulated state and Section 10526(a)(4) of the Interstate Commerce Act exempts from economic regulation motor vehicles owned and controlled by a farmer transporting his own agricultural products and supplies.43

Besides the exemption for farm trucks, agricultural products themselves have always been excluded from the regulatory scheme, no matter who hauls them. No one needs a certificate of public convenience and necessity to haul unprocessed agricultural and horticultural commodities.44 The ICC has spent a lot of time and effort in determining what commodities come within the intention of Congress to exempt only those agricultural products which are in their raw or, if not generally marketable in their raw state, have been processed solely for the purpose of making them marketable.45 Truckers, then, could carry these raw agricultural products to market, but the law did not allow a backhaul of a nonexempt product.

Much of the hauling of agricultural products is done by agricultural cooperatives. The larger co-ops have transportation divisions and they function very much as the large interstate truckers. The law allowed co-ops to haul up to 15% of their interstate shipments in non-exempt commodities. Agricultural co-ops, then, seeking a backhaul, would often undercut regular truckers in soliciting business to fill up the empty trailer for gas money. The

Motor Carrier Act of 1980 expanded this non-exempt traffic to 25% of the agricultural co-op's tonnage. During the 1970's, the ICC worried a great deal about the problem of "bogus co-ops", so-called agricultural cooperative organizations that engaged in few marketing activities, but merely sought a backdoor entry into the transportation business.

E. Private Carriage

While driving on the interstate highways, the motorist will notice large semi-trailer trucks marked for retail stores such as Sears and K-Mart. All these are firms which have decided to forgo for-hire carriage and establish their own trucking division to connect their network of stores together. Of the 24.5 million trucks on the highways in 1975, all but a million were operated by private carriers, and even among the big semi-trailer rigs, almost as many are operated by private concerns as by trucking firms. When a shipper operates his own vehicles in pursuit of his own (nontransportation) business, it is clearly as much private carriage as when you or I take our packages home from the department store. The issue has arisen when a corporation leases vehicles (especially from owner-operators) as to whether or not it is engaged in for-hire carriage, which would require authority from the ICC.

The growth of corporate conglomerates has given rise to another question. That question is whether a corporation may haul for its subsidiaries. Generally speaking, a legal entity (such as a corporation) was forbidden to transport for compensation the property of an affiliated, but separate corporation. The Commission did not choose to pierce the corporate veil to find common ownership. This question was answered by the Motor Carrier Act of 1980, which allows intercorporate hauling if there is 100% ownership by the parent corporation of the subsidiary.

This unregulated sector accounted for the bulk of trucking, and few substantial figures were given as to the extent of the industry. Railroads, when complaining about truck competition, focused on the common-carrier industry. The private trucker, who had forsworn common carriage completely, was seldom mentioned.

F. Package Delivery Services

The delivery of parcels is one of the oldest facets of the trucking business. Names like Adams Express and Wells Fargo & Company predated the opening of the West, but were curbed by express statutes instituted to prohibit these companies from competing with the Post Office, which was

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46. Id. at 147.
47. Id. at 124.
48. Id. at 126.
granted a monopoly on carrying the mails. The remaining concerns in the express business were merged into the Railway Express Agency, owned by a consortium of railroads, using trains for intercity service and trucks for local delivery.

Railway Express later forsook the parent rails and concentrated on a motor carrier delivery service, using valuable express company rights granted by the ICC. Renamed REA Express, Inc., the company could not survive and was liquidated in the 1970's. Most package delivery service is handled today by United Parcel Service, a motor carrier with operating authority in all 48 contiguous states granted by the ICC.

UPS sees the Postal Service's Parcel Post as its main competition. Presently the Brown Giant has become the carrier of preference for most businesses and is far more efficient and profitable than the Postal Service. Of course, UPS has few of the service obligations of the Postal Service, and is not required to maintain full-service offices in small towns. Thus, the amount of cross-subsidy is reduced to nil. UPS maintains very simple terminal facilities where package shipments are consolidated and placed on trailers. Although, at one time, UPS was exclusively an over-the-road carrier, but with increasing fuel and labor costs, UPS has turned to shipping its trailers on railroad flat cars, and in some instances, maintains entire trains for coast-to-coast UPS movements.

G. TRUCK RENTAL COMPANIES

Many of the casual movements on the highways are by private individuals driving trucks or hauling trailers owned by U-Haul, Hertz, Jartran, Ryder, or several other truck rental companies. Because the lessee does the driving, controls the movement of the vehicle, and is responsible for damage, this is not considered for-hire carriage. Because auto rentals and their predecessors, the livery stables, were not considered common carriers, truck rentals are also exempt and are considered to be a form of private carriage.

Driveaway and truckaway companies (which haul your own trailer or drive your car to a new destination), however, are considered to be common carriers. Since they hold themselves out to the public as purveyors of transportation, and since they provide the drivers (albeit from a casual list of walk-in drivers in response to ads which read “Drive Free to Florida”), they are as much carriers by motor vehicles as trucking companies, according to the ICC.  

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49. Since 1971, the first-class mail monopoly has been vested in the United States Postal Service, which is technically a government-owned corporation.

50. AAACon Drivers' Exchange, so listed in order to be the first in the New York phone book, was the first and largest such firm to receive authority from the ICC.
H. MOVING VANS

The major moving van companies have licenses from the ICC to operate as "common carriers of used household goods". The structure of the moving van industry is not as monolithic as it might appear. Most of the companies are associations which local agents belong to. When you make a move, an ICC tariff governs what charges are made (despite what the estimate to charges might be), and a local agent arranges the packing and departure. Another local agent at the other end of the line handles the unpacking or storage. Much of the labor used in the packing and moving is not the unionized professional help which you might expect, but casual labor hired by the driver for that day only. Experience with household goods movers was one of the prime horror stories in the Nader Report\(^5\)\(^1\) and eventually led to the Household Goods Transportation Act of 1980.\(^5\)\(^2\)

I. SPECIALIZED CARRIERS

This term is used to denote motor carriers who own specialized equipment rather than the traditional tractor-trailer combination. They usually have broad geographical authority, but limited to a certain type of equipment. Some examples of these would be auto and boat transporters or tank trucks used for hauling chemicals or other hazardous substances. Heavy-haulers, which have heavy-duty equipment for moving construction machinery or other oversized loads are often found in the ranks of specialized carriers.

J. INTERCITY BUS LINES

The growth of the bus industry is rather different from the history of trucking, since it is passenger-oriented and has developed into a duopoly, with Greyhound and Trailways the predominant operators. The Greyhound system began in the Iron Range of Minnesota in the 1920's, and expanded through merger with other bus lines until a nationwide system was formed. Trailways was, until recently, a lose association of once-independent bus lines and many former railroad subsidiaries. Protected from antitrust considerations by law and ICC policy, the two were allowed to expand to the extent where they have national pre-eminence today, with a mere differentiated fringe of local operators. Railroad companies, seeking a solution to the problem of passenger operations, once bought heavily into bus companies, but most have sold their interests to Greyhound or Trailways. Some independent companies have flourished, mostly in North and South Dakota,\(^5\)\(^3\) but most operate as feeders with some affiliation with one or the

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53. Bangor and Aroostook is one of the few railroads that still operate their own bus compa-
other national systems.

Bus companies provide a low-cost, labor-efficient, fuel-efficient system of transportation that unfortunately reached its peak in the early 1970's and is fighting to hold on to its share of the market. By using public highways for transport and very rudimentary terminals (except in major cities), the bus companies have been able to avoid the costly infrastructure that plagued railroad passenger service. There were low costs and high depreciation in the industry, since the major expenses were buses and the costs of drivers. Somehow, the Amalgamated Transit Union and other labor organizations were persuaded to allow the driver to do loading and unloading work on route and thus station costs were minimized. Except for major cities, the bus depot could be an agency station, located in a drug store or gas station, with the agent collecting a commission for bus tickets sold. Development of a long-distance motor coach by General Motors (with the engine underneath the passenger compartment and room for baggage to boot) and the increasing mileage of all-weather highways supplied by the taxpayer gave opportunities for the industry to grow.

For all the advantages, bus travel never achieved its full potential in the United States. Vehicles were often cramped and crowded, unlike the more luxurious European coaches. Bus companies, writing off the luxury market, concentrated on cheap transportation and neglected many amenities. A system of mail buses, such as provides service to German small towns, never developed in this country, and most small communities have no access to intercity buses. Worst of all, the bus industry, unwilling to short-haul itself never moved toward a system of intermodal transportation. It is very difficult to switch from bus to rail or bus to air modes in this country, while most other nations regard all modes as part of an integral system.

Today's intercity bus companies derive much of their earnings from charter service or package express. On many carriers, the intercity carriage of passengers is a marginal activity, maintained to keep the franchise.

All of the motor carriers have benefited from the development of superhighways (built at the behest of motorists but maintained to extra strength for truckers). The debate over whether or not truckers pay anywhere near their fair share of highway costs has been raging for over forty years and will probably never reach a consensus. It is true that there has been cost to local communities due to the necessity of widening city streets and in policing additional traffic for motor carriers, but, as a public good, street use has not generally been measured.

Common carriers have an obligation to the shippers to take all traffic

In North and South Dakota, established firms such as Jack Rabbit Lines, Triangle Transportation and Star Bus Co. operate intercity service, as this area (and northern Minnesota, where Greyhound was born) has not been incorporated into the major bus systems.
rendered on a nondiscriminatory basis. They also act as insurers for the traffic which is in their care. This obligation has been supplied by law on the rationale that the common carrier is in a better position to provide for the shipment than the shipper who has relinquished control of it. Contract carriers have sometimes limited liability by contract; the relationship between large shippers and carriers being on approaching equality of bargaining. With small shippers who use the facilities of UPS, bus express or moving vans there is little or no bargaining power, and contracts of adhesion result. This is one reason given for continually monitoring the activities of carriers who specialize in the handling of small shipments.

In contrast with the rail and air competition, which is governed by the Railway Labor Act, labor relations within the motor carrier industry come under the National Labor Relations Act. Most of the large operators have contracts with the International Brotherhood of Teamsters, while most bus line employees are represented by the Amalgamated Transit Union. Deregulation could expect to meet resistance from these unions, which would fear the entry of non-unionized competitors to jeopardize their wage and benefit scales.

V. EXEMPTIONS TO REGULATION

In addition to the exemptions for private and agricultural transportation, the Motor Carrier Act exempted certain other areas from regulation by the ICC. Within these areas, a more or less free market in transportation flourished.

A. INTRASTATE COMMERCE

Not only does the ICC have no jurisdiction over purely intrastate carriers, but it also considers "land-bridge" traffic to be exempt, where traffic is en route between two foreign countries. This not only exempts traffic between Canadian points passing through Minnesota or Maine, but has been held to apply to Canadian traffic going to a United States port for transshipment to Europe.

B. COMMERCIAL ZONES

Local movements within a municipality and its surrounding commercial zone (the suburbs or contiguous towns) are exempt from regulation. This

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56. Dempsey, supra note 46, at 127.
allows local carriers to serve points within a local area without seeking regulated authority, even if the city is located on a state line.\textsuperscript{58} Closely related is the terminal area exemption, by which a line-haul carrier with authority to serve one point may pick up and deliver anywhere within that one community's terminal area.\textsuperscript{59} The terms "commercial zone" and "terminal area" are not defined in the statute, but the ICC bases the exemption on the size of a municipality. Thus the commercial zone/terminal area of a town of 2,500 is a circle of 3 miles radius, but the exempt area for a city of 1,000,000 souls or more is 20 miles.\textsuperscript{60}

\section*{C. Incident to Air}

Many air freight shipments have a prior or subsequent movement by motor carrier. Most air freight to Milwaukee, for example, is handled through O'Hare Airport and trucked into Wisconsin. The Interstate Commerce Act exempted freight with an immediate prior or subsequent movement by air. Part of the reason for this exemption was that the Civil Aeronautics Board had jurisdiction over surface transportation in connection with air transportation. The two agencies worked out an airport zone limit (similar to the commercial zone), usually of about twenty-five miles from the airport. Within this zone, the CAB had jurisdiction; outside this zone, regulation was the ICC.\textsuperscript{61} If there was one waybill for transportation of freight and the motor traffic was within the terminal area, it was all a CAB matter. Then, in 1977, Congress amended the Federal Aviation Act of 1958\textsuperscript{62} and, following the spirit of the amendment, the CAB eliminated the tariffs for surface carriers incidental to air. Then the Motor Carrier Act of 1980 extended the exemption by effectively deregulating all traffic with a prior or subsequent movement by air.\textsuperscript{63} Apparently there are no geographical limits to this exemption.\textsuperscript{64}

\section*{D. Other Exemptions}

The statute also exempts from regulation the transportation of wrecked vehicles, newspapers, school buses, taxicabs and buses operated by hotels and motels, casual transportation, and movements within national

\begin{footnotesize}
\begin{enumerate}
\item \textsuperscript{58} An interesting situation occurs when the commercial zone runs up against an international boundary, as in Detroit, El Paso, Buffalo or San Diego. This situation has not been completely settled to anyone's satisfaction. See J. Guandolo, supra note 24, at 309-11.
\item \textsuperscript{59} 49 U.S.C. § 10523 (Supp. II 1978).
\item \textsuperscript{60} Dempsey, supra note 45, at 131.
\item \textsuperscript{61} Id. at 131-41.
\item \textsuperscript{62} Act of Nov. 9, 1977, Pub. L. No. 95-163, 91 Stat. 1278.
\item \textsuperscript{63} 49 U.S.C. § 10526(a)(8)(B) (Supp. IV 1980).
\item \textsuperscript{64} Dempsey, supra note 45, at 140.
\end{enumerate}
\end{footnotesize}
VI. PRESSURES FOR Deregulation

A. THEORETICAL CONSIDERATIONS

By 1970, many commentators had remarked upon the inappropriateness of a utility model of regulation for a possibly competitive industry. Trucking just did not seem to have many of the characteristics of natural monopoly. Minority truckers felt left out of a system where all the goodies were divided up in 1935. The industry no longer seemed to be an infant needing protection.

More to the point was the constant reminder that an agency often is said to be captured by those whom it is supposed to regulate. The agency is confronted with industry representatives every day and tends eventually to see the industry point of view. It views continuance of traditional forms of operation as the \textit{sumnum bonum} and views outside competition as a threat to the stability of the system.

This point was brought home by the publication of the first report by Ralph Nader’s organization. Entitled \textit{The Interstate Commerce Omission},\textsuperscript{67} authored by Robert Fellmeth with the assistance of Ralph Nader’s task force on transportation, it called the ICC the administrator of a large cartel of transportation forces, beholden to the railroads and major trucking concerns, and keeping rates artificially high through restriction of competition. Such criticism had been voiced many times before, but mostly from economic or political conservatives. Since Nader was mostly identified with the political left, and espoused government action to correct consumer problems, the report was considered to be an expansion of the consensus in favor of more competition.

The Nader book concentrated on abuses which affected the consumer directly, such as household goods moving and the discontinuance of rail passenger service. But it especially took aim at the lack of competition in the industry. It cited the case of Joe Jones, a black trucker who obtained a loan from the Small Business Administration to enter the trucking business but was unable to operate because of the ICC’s refusal to give him authority. Jones drove his truck to Washington and parked it outside the ICC in protest. The \textit{Omission} book cited Jones as an example of the cartelization of trucking.\textsuperscript{68}

There had been experience with exempt transportation in such areas

\textsuperscript{65} Id. at 148-49.
\textsuperscript{66} Id. at 149.
\textsuperscript{67} R. FELLMETH, supra note 51, at 119-35.
\textsuperscript{68} Id.
as agriculture, commercial zones, and incident-to-air transportation. Few of the dire consequences predicted had, in fact occurred. Further deregulation would not be occurring in a vacuum; we had models of deregulation in exempt transportation, as distinguished from the totally regulated railroad experience.

The 1970’s political climate favored a retreat from regulation. Both Carter and, later, Reagan, were elected on platforms which called for a retreat from regulation, and one could not pick up a newspaper without stories about bureaucratic lag, regulatory inefficiency, or the additional costs incurred by government regulation. Most of this criticism involved agencies responsible for regulation of business practices such as the Occupational Safety and Health Administration, National Labor Relations Board, Equal Employment Opportunity Commission, Environmental Protection Agency and the Federal Trade Commission. Much less frequent was criticism of the utility-type regulatory agencies, but the general distrust of government rubbed off on the transportation agencies as well.

By 1978, Americans had an example of deregulation. The Air Cargo Deregulation Act and the Airline Deregulation Act had been passed, thus creating a sunset law for the CAB. Although there have been many adverse effects on price and service since the passage of these laws, there were enough one-shot benefits with innovative fares by airlines entering new markets to make the idea of deregulation palatable to customers. If air deregulation could bring us Super Saver fares and Freddie Laker, deregulation of surface transportation could only be better.

One of the biggest factors motivating deregulation was the activity of the ICC itself. Its unimaginative utility-type regulation had caused excessive fragmentation of authority and disputes over the nature of commodities to be hauled. With regard to the latter, Representative Millicent Fenwick testified:

The ICC has 36 categories of exempt and nonexempt products listed under the heading of “Milk and Cream.” Buttermilk is exempt, but butterfat and buttermilk with condensed cream are regulated. Concentrated skim milk, and powdered, are exempt, but condensed and evaporated are not.

And believe it or not, Mr. Chairman, manure in its natural state is an exempt commodity but manure, fermented with additives such as yeast and molds, producing a rich liquor which in water solution is used for soil enrichment is not.

Restrictions on routes and backhauls seemed an anomaly at a time

when fuel shortages abounded and Americans were being told to save gasoline. The ICC at one point allowed gateways to be eliminated and shorter routes taken by truckers, so long as they did not shorten the mileage too much, so as to upset the competitive balance.

Finally, the idea of competition and the elimination of cartels had great appeal. In areas where there was considerable competition, such as in dataprocessing equipment, telecommunications and even auto rentals, customers had seen the advantages of competition in the marketplace. Where the market was imperfect, the public saw administered pricing and oligopolistic behavior. The old conservative cry of freedom to operate without restraint had never been overly popular; most people do not have much property or business of their own and such liberty was meaningless. But the neo-conservative philosophy that competition serves the public and that government has a penchant for lousing things up struck a responsive chord, and brought on a new willingness to let competition play a part in the regulation of transportation.

B. Economic Considerations

Beginning with the Ford administration and continuing through the Carter regime, inflation became the principal concern of the American political economy. Increased competition was considered to be a weapon to use against the inflationary forces surrounding us. Regulated industries, because of their controlled oligopolistic position, could pass on increased costs of equipment, fuel and labor by going to the appropriate regulatory agency and gaining permission to increase rates.

Increased competition, however, could act as a brake on these automatic cost pass-throughs. Trucking, with relatively low entry costs, seemed to be a good place to introduce more competition. New, trimmed-down operations should have lower fixed costs than the established truckers. In the labor field, increased competition would have a major impact on the industry by undermining the Teamsters’ Union’s bargaining power. After years of maneuvering, the Teamsters’ Union gained great bargaining leverage by arranging for trucking contracts throughout the nation to expire at the same time. The threat of new, non-union competition by owner-operators if deregulation were enacted, would stand as a threat to convince the Teamsters to moderate their demands.

Coincident with the enthusiasm for competition was the rise in popularity of the Chicago school of economics. By the 1970’s, the most-read economist was Milton Friedman. Friedman opposed any type of market control as ultimately directed against the consumer and brought upon by the desire of the regulatees to gain government assistance in forming a
His Chicago colleague, George Stigler, refined Friedman's teachings into an "Economic Theory of Regulation", which demonstrated how groups sought regulation to enhance their incomes. Professor Richard Posner suggests that regulation of the transportation industry, inasmuch as it preserves certain services which the market would not otherwise produce, is actually a branch of public finance and should be viewed as a tax upon producers. Economist George Hilton called for the complete elimination of the ICC and the treating of the transportation industry like any other business. Hilton predicted that once the ICC was dissolved, the transportation industry would emerge like the hotel-motel business, with some large national chains and some independent operators. Additionally, intermodal companies would rise from the ashes of today's railroads, with strong competition from independent truckers.

To the question, "what will curb the excesses of carriers when regulation goes?", Hilton and the others would calmly answer that the invisible hand of the market place would meet consumer needs. The rollback in transportation regulation is testimony to the strength of the belief that competition, rather than regulation, can better serve the public. Possibly this is not so with true monopolies, (i.e. electric or gas companies) but where competition is possible, the prevailing view was that it should be encouraged.

Economists see certain specific savings if the ICC regulatory scheme was abolished. Costs could be cut by the elimination of gateways and circuitous routes, as well as restrictions on commodities carried and other wasteful practices. Not only was cost to shippers considered, but also energy conservation. Empty backhauls and circuitous routings were seen as contributing to high energy use—a situation that benefited no one, since most of the excess gasoline was just burned up as economic waste. De-regulation was seen as both an inflation-fighting and a fuel-saving move.

C. Political Considerations

By the late 1970's, one industry had been deregulated—air freight. Although prices did not go down, as anticipated, there was an explosion of new entrants to the market, and service competition, as opposed to price competition, resulted. Similar benefits were sought in the deregulation of motor carriage. Visionaries saw service to more localities, and an increased possibility for entry by minorities and others who were willing to get into trucking but had previously been blocked. Competition was an easy concept to sell, and the benefits of freer entry were easily understood. The

73. See generally, M. Friedman & R. Friedman, Free to Choose (1978).
reverse side of the coin: freedom to raise rates and to exit unpopular markets, was seldom discussed.

The political benefits of deregulation could be easily foreseen. Small shippers were often stymied by the insistence on the tariff principle and the inability to hold a carrier to an earlier estimate by estoppel. Everyone was presumed to know the tariff. Large shippers, of course, could dicker in establishing contracts with contract carriers. The new carriers, in order to gain a share of the market, might compete on price. At any case, full deregulation would bring a new environment where there would be no automatic pass-through of fuel or labor cost increases, and thus an incentive to keep those costs down. Furthermore, full deregulation would make rate bureaus and their price-fixing machinery a thing of the past.

Bureaucracy is fair game in all modern nations, and there were perceived political benefits from abolition of another Federal agency. It went along with the war on government waste, and it would eliminate the symbiotic relationship between carriers and regulators. Sunset laws were easily understood by the public, and if deregulation did not work, Congress could always impose reregulation or at least provide minimal service standards for the industry. (It was actually a form of reregulation which carried the day, as there is no sunset law in force for the ICC).

Political moves toward deregulation actually began in the states, which had passed sunset laws for various occupational licensing boards as well as for their regulatory commissions. The typical state sunset law would provide for the demise of regulation unless the legislature renewed the regulators' charter on a periodic basis. In Florida, the legislature could not agree as to what form regulation of motor carriers would take, and the old law was allowed to expire. In Minnesota, motor carrier regulation was taken away from the Public Service Commission and vested in a new independent transportation regulatory agency, but as of this writing the legislature has not appropriated funds for the new body.78

The deregulation drive which resulted in the Motor Carrier Act of 1980 was a strange convergence of the left and the right. Theoretical conservatives and libertarians proceeded on the assumption that economic freedom must be pursued and government control limited. On the left, Senator Edward Kennedy (D-Mass.), saw in deregulation an issue that was at once anti-monopoly and anti-government, thus pleasing both ends of the political spectrum. Against this pressure, the centre, composed mainly of the industry itself and the Teamster's Union, could not mass enough support to prevail against the right and left enthusiasts for deregulation.79

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78. James Hoveland, Remarks at Minnesota Continuing Legal Education Seminar (Nov. 9, 1980).

79. The classical view is that labor organizations support oligopolistic structures for industry
deregulation would codify many of the steps which had already been taken by the ICC in freeing up the industry.

VII. Self-Deregulation by the ICC

Following the publication of the Nader report, there was a decided move within the ICC toward liberalizing entry for motor carriers. Frivolous objections by protestors went unheeded; the Commission began to take a more liberal view about the need for a proposed service. It may have been that ICC commissioners, seeing the handwriting on the wall, moved in the direction of liberalizing entry before Congress abolished the whole works.

Most applications now were handled under modified procedure, which did away with the necessity of a hearing in motor carrier cases unless grave questions of transportation policy were raised or unless credibility of a witness was a factor.

At the beginning of the decade, in these modified procedure cases, the adequacy of existing service was the principal factor considered by the ICC. In 1970 the Commission had so favored incumbents that:

Once an existing carrier showed it was "fit, willing and able" to move freight for which applicant had obtained shipper support, and once the existing carriers demonstrated that some diversion of their present traffic could result and revenue would be lost, the application would, in all probability, be denied. The presumption weighted heavily that existing carriers were entitled to all the freight they could adequately handle. Once adequacy of existing service and potential diversion of traffic were established, there was literally no course of action or evidence that applicant could present to the Commission to convince it that the proposed authority should be granted. If, for instance, a shipper suggested that it needed more efficient or expeditious service, the Commission would determine whether the shipper truly needed the service or whether it would merely be a convenience.80

With the decision rendered in Bowman Transportation, Inc. v. Arkansas-Best Freight System, Inc.,81 the ICC's emphasis began to change to favor competition. Bowman saw the Supreme Court upholding the right of the ICC to weigh the benefits of competition against the detriment to existing carriers. It was not a far-reaching decision, but it is generally considered to be the turning point by the ICC in favoring competition.82 Following the Bowman case was the more definite instruction from the District of Columbia Circuit in P.C. White Truck Line, Inc. v. ICC.83 Here the court stated

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82. Freeman and Gerson, supra note 80, at 19.
83. 551 F.2d 1326 (D.C. Cir. 1977).
that under the Pan American test the Commission must consider competition as a factor in addressing the public need. On remand to the ICC, the Commission decided that increased competition is presumed to be in the public interest, and protesters must be much more specific in pointing out what injury will befall them and the public if the application is approved.\textsuperscript{84}

Increased competition went beyond common-carrier truckers. In Sawyer Transport, Inc. \textit{v.} United States\textsuperscript{85} it was held that a contract carrier could not be denied a permit solely on the grounds of adequacy of existing common-carrier service to the plant. In Highland Tours, Inc. \textit{Common Carrier Application}\textsuperscript{86} the Commission upheld the Pan-American criteria, but found that the diversion of traffic created by a one-bus carrier would not be sufficient to severely threaten the mighty Greyhound Lines.

The ICC's new policy toward liberalized entry and favoring competition was set forth in Liberty Trucking Co., Extension—General Commodities.\textsuperscript{87} Once public need has been demonstrated by an applicant, protesters must show that they can satisfy that need. However, they must go further and assume the burden of demonstrating an interest worthy of regulatory protection from competition. Their burden is to convince the ICC that the newcomer is likely to materially jeopardize the existing carriers' ability to serve the public.\textsuperscript{88}

It is not enough for an existing carrier to be harmed by a new entrant, or even to be forced out of business; the loss has to be shown to be injurious to the public as well. Liberty was one of the Commission's more controversial motor carrier cases and the industry clamored for reconsideration. In Colonial Refrigerated Transportation, Inc., Extension—Florida to 32 States,\textsuperscript{89} the Commission denied an application where competition already existed on the route, and the evidence did not show that increased competition would spur carriers toward greater efforts in providing better service. It is clear that, in the past, the ICC was unwilling to make competition the lone criteria for allowing new carriers to enter the system. Now, however:

All doubt is ended. Despite the Commission's statement that it is not abandoning Pan-American, the traditional method for determining the outcome of motor carrier entry applications is no longer operational. Increased competition is now presumed to be in the public interest to a much greater extent than previously articulated. Mere conflicting authority coupled with traffic abstracts

\textsuperscript{84} P.C. White Truck Line, Inc., 129 M.C.C. 1, 8-9 (1978).
\textsuperscript{85} 565 F.2d 474 (7th Cir. 1977).
\textsuperscript{87} 130 M.C.C. 243 (1978).
\textsuperscript{88} Freeman and Gerson, supra note 80, at 410-411. The authors point out that even "the spectre of bankruptcy or withdrawal of existing carriers from the relevant market may not be sufficient to overcome the presumed benefits of increased competition to the public."
\textsuperscript{89} 131 M.C.C. 63 (1979).
showing speculative revenue losses will not suffice to deny an application. The core of Pan-American has always been to advance the public interest, but the ICC now holds that this is entirely separate and distinct from protecting existing common carriers from competition. In Liberty II, the Commission reaffirmed its earlier position that the benefits of competition and improved service may outweigh even substantial harm to protestants and stated that it "will not deny the public the benefits of an improved service or heightened competition merely to protect the inefficient or to insulate existing carriers from more vigorous competition." 90

Liberalizing entry requirements was one way that the ICC was moving toward self-deregulation in the 1970's. Other areas included eliminating gateways and authorizing backhauls for operating efficiency, 91 allowing deviation to parallel superhighways for regular-route carriers, experimental deregulation of some commodities and expansion of temporary authority, granting broad geographical limitations and avoiding fragmented grants of authority or unduly restrictive commodity descriptions. The ICC was trying to moderate some of its excesses before Congress did it for them.

VIII. THE MOTOR CARRIER ACT OF 1980

Despite the desires of Freidman, Stigler, Kennedy and others for sunset provisions for ICC motor carrier regulation, it looked by 1980 as if the proposed "trucking deregulation bill" would actually be a compromise bill, which would extend the regulatory scheme but correct some of its abuses. What emerged from the Congress was not a deregulation bill, but a law which provided new standards, not termination, for the ICC. The Congressional finding section states that in some cases existing regulation has been counterproductive, that the ICC should be given explicit direction and well-defined parameters for regulation of the motor carrier industry and that the ICC should not attempt to go beyond the powers vested in it by the Interstate Commerce Act. 92 The Act is not a new departure, but a codification of much of what the ICC had done in the past decade. Politically, it was a product of a compromise between advocates of deregulation and those who favored regulation. No one liked the status quo except for industry spokesmen, who saw the rights for which they had fought or purchased reduced to nothing.

The new Act adds to the National Transportation Policy the promotion of competitive and efficient transportation service in order to (1) meet the needs of shippers, receivers and consumers; (2) allow a variety of price and service options; (3) allow the most productive use of equipment and energy

90. Freiman and Gerson, supra note 80, at 413.
resources; (4) enable adequate profits and fair wages; (5) provide and maintain service to small communities and small shippers; (6) maintain a privately-owned motor carrier system; (7) promote minority participation and (8) promote intermodal transportation. These somewhat conflicting objectives show the various interests which were involved in the compromise.

The new Act shifts the burden of proof from the applicant to the protestant and requires the applicant to show (in addition to proving fitness) that his proposed service will serve a useful public purpose and will be responsive to public demand or need. The burden is now on the protestants to show that the service is inconsistent with the public convenience and necessity. This is a drastic change from the former procedure, wherein the applicant had to prove that his service was required by public convenience and necessity.

Additionally, the new legislation permits the Commission to issue "master certificates" wherein the findings of public convenience and necessity are made in a rulemaking procedure. True, the Act prohibits the issuance of a master certificate except in certain areas, but in these areas, only the applicant's fitness is an issue. If the Commission finds the applicant fit, willing and able, he will be awarded authority to serve these markets:

a. where a community is not regularly served by another motor carrier.
b. when rail service to a community has been abandoned.
c. movements of U.S. government property (with some exceptions).
d. small shipments (under 100 lbs.).
e. movements of foodstuffs and fertilizers by an owner-operator, provided that the owner-operator remains with the truck at all times.

This amounts to substantial deregulation of these areas. Protests are of no avail in "fitness" applications, and the Act includes standards designed to assure that only protests of substance can be made in other application proceedings. A protestant must have authority to handle the traffic, and actually has handled such traffic within the last year. Motor contract carriers are now prohibited from protesting common carrier applications.

The Commission is directed to eliminate gateways and circuitous route limitations and to remove operating restrictions in certificates. This directive includes: broadening the restrictive categories of goods allowed to be transported, removing restrictions against serving intermediate points, converting all one-way authority to round-trip authority, to eliminate narrow territorial limitations and other restrictions wasteful of fuel, inefficient, or contrary to the public interest. Thus, if a carrier applies, the ICC must re-

form its certificate to provide for a more comprehensive grant of authority.97

A greater number of commodities now come within the exempt authority category. Fish and shellfish byproducts not intended for human consumption are now exempt, as are livestock and poultry feeds, agricultural seeds, and plants if transported to a farm or a business selling to farmers. In addition, all incidental-to-air motor freight operations are exempt, so are used pallets, shipping containers and devices, natural crushed rock used for decorative purposes and wood chips.98

A new Section 8 permits sellers of food and grocery products to compensate customers who pick up their own products without being guilty of discriminatory pricing.99 Intercorporate hauling for compensation is permitted for wholly-owned subsidiaries, upon notice to the Commission. This intercorporate hauling is now termed private carriage.100

Entry rules are modified for contract carriers by deleting the requirement of a limited number of shippers. The old "rule of eight" is abolished. One-truck companies can obtain master certificates for the carriage of processed foods, and the prohibition against dual operations (common and contract authority) has ended.101

Deregulation of trucking is more than simply easing entry into the field. The new Act creates a ten percent zone of reasonableness, within which rates may be raised or lowered without any investigative or suspension jurisdiction of the ICC. The Commission may, on its own, increase this zone an additional five percent. After two years, this zone would be adjusted to account for changes in the Producer Price Index.102 In addition, there is a new provision for released rates, by which the shipper would get a reduced rate in exchange for reduced exposure to liability by the carrier.103 This is the first crack in the common-carrier liability which has traditionally been imposed by the ICC. However, it remains to be seen whether the trucking industry will follow the lead of the deregulated air freight industry and shift the insurance burden for loss and damage to the shipper.104 The Commission is directed to adopt revenue standards which will provide motor carriers a flow of net income, plus depreciation, adequate to support prudent capital outlays, assure the repayment of a reasonable level of debt, permit the raising of needed equity capital, attract and retain capital "in amounts adequate to provide a sound motor carrier transportation system in the

102. 49 U.S.C. § 10708(d) (Supp. IV 1980).
United States, and take into account reasonable estimated or foreseeable future costs.\textsuperscript{105}

With regard to rate bureaus, the new law prohibits discussion and voting on single-line rates by rate bureaus by 1984. It prohibits rate bureaus from interfering with independent actions, makes rate bureau meetings open to the public, and requires that the bureaus have written authority from carriers being represented for voting purposes.\textsuperscript{106} Rate bureaus are not being phased out but it is clear that their activities have been curtailed.

The law makes ""lumping"" (coercion to employ certain people to load and unload vehicles) unlawful\textsuperscript{107} and requires written contracts to be used in the hauling of exempt agricultural commodities.\textsuperscript{108} It adopts a mere fitness test for the commission to license brokers, thus virtually exempting transportation brokers (except for household goods) from regulation.\textsuperscript{109} Another area of exemption is the issuance of securities by carriers under a $1,000,000 jurisdictional amount.\textsuperscript{110} It provides for expedited consideration of pooling arrangements between carriers,\textsuperscript{111} and allows a trucker to carry mixed loads of exempt and regulated freight together without either category losing its regulated or exempt status.\textsuperscript{112} It also allows freight forwarders to enter into contracts with railroads or water carriers for certain transportation services. Formerly, freight forwarders could contract only with motor common carriers.\textsuperscript{113}

As part of the ease of entry requirements, the Commission is authorized to grant temporary authority for up to two-hundred-seventy days and emergency temporary authority for thirty days. Agricultural cooperatives may now haul up to twenty-five percent of their total interstate tonnage in non-exempt commodities, as opposed to fifteen percent of their tonnage under the 1935 law.\textsuperscript{114} The Commission is authorized to require co-ops to maintain detailed records with the ICC to ensure that the co-ops comply with the tonnage and other requirements of the statute.

With regard to mergers, the Commission must expedite its procedure. Evidentiary proceedings in motor carrier mergers must be completed within two-hundred-forty days and the final decision must be reached one-hundred-eighty days later.\textsuperscript{115} This is intended to speed up merger proceed-

\begin{itemize}
\item \textsuperscript{105} 49 U.S.C. 10701(e) (Supp. IV 1980).
\item \textsuperscript{106} 49 U.S.C. § 10706 (Supp. IV 1980).
\item \textsuperscript{107} 49 U.S.C. § 11109 (Supp. IV 1980).
\item \textsuperscript{108} 49 U.S.C. § 10527 (Supp. IV 1980).
\item \textsuperscript{109} 49 U.S.C. § 10924(b) (Supp. IV 1980).
\item \textsuperscript{110} 49 U.S.C. § 11302 (Supp. IV 1980).
\item \textsuperscript{111} 49 U.S.C. § 11342 (Supp. IV 1980).
\item \textsuperscript{112} 49 U.S.C. § 10528 (Supp. IV 1980).
\item \textsuperscript{113} 49 U.S.C. § 10766 (Supp. IV 1980).
\item \textsuperscript{114} 49 U.S.C. § 10529 (Supp. IV 1980).
\item \textsuperscript{115} 49 U.S.C. § 11345a (1980).
\end{itemize}
ings before the ICC.

Some of the criticism of proposed deregulation was raised by advocates of small towns. These smaller communities were afraid that the carriers might ignore them if rates were to be skewed to more profitable areas, as has happened with airlines since deregulation. Congress insisted that the Commission conduct a study of service to small towns (five thousand or less), including an analysis of the common carrier obligation to provide service to small communities, and an evaluation of whatever effect the new law has on small towns. This report was due on February 1, 1982.116

Authority to require financial responsibility of all carriers was transferred from the ICC to the Department of Transportation.117 This has been a feature of virtually every transportation deregulation scheme enacted to date. This independent regulatory commission is stripped of some of its existing responsibilities, either by total abolition or by transfer to the Department of Transportation. The DOT has steadily gained authority since its inception in 1966 and greatly benefitted from the creation of Amtrak and Conrail and the deregulation of air service. Its authority in the regulatory field has steadily increased since its inception in 1966.

The Motor Carrier Act of 1980, however, substantially leaves the ICC intact. It gives new guidance to that agency and exempts a number of areas for service. It makes entry easier, and makes it more difficult for certificated carriers to protect their market share. It may make some operating rights worthless. But it does not abolish the common carrier principle, nor the binding effects of tariff. It keeps in modified form the Pan-American test of public convenience and necessity, and preserves the necessary oversight function of the ICC. That agency will still be regulating some forms of motor carriage during its centennial in 1987.

IX. THE HOUSEHOLD GOODS TRANSPORTATION ACT OF 1980

A sidelight after the massive deregulation effort of 1980 with regard to motor carriers was passage of the Household Goods Transportation Act of 1980.118 The dynamics of moving van companies are different from those of carriers of general freight. The shipper is not a business entity, but often an individual householder who is usually inexperienced in dealing with such companies.

The moving concerns are not geared to single family units but rather to hauling government shipments, often for relocating personnel changing posts in the military, or handling large moves by corporations. Here, the company or government agency has a certain amount of power to wield in

steering traffic to or from another moving company. Due to their size, these institutional accounts have some equality of bargaining power, and the moving companies are more conscientious about dealing with them.

The companies such as Allied, Mayflower, North American and other national van lines are actually only loosely affiliated with the local agents, and often have not been quick to respond to abuses by such agents. The main consumer complaint has been "low-balling," by which an agent would quote an unreasonably low price in order to gain traffic. Once the shipper signed with the moving company, the tariff principle was strictly applied: no deviation from the tariff was possible, there could be no rebates, and payment must be in cash, cashier's check or certified check. Otherwise the furniture would be carted off to a warehouse, where storage fees would accrue. The customer had no choice but chase around a strange town for his money.119

Since household moving affected members of the public at large, the ICC received an enormous amount of complaints. The ICC tried to meet the situation through rulemaking by requiring the shipper to pay an amount more or less equivalent to the estimate, and giving him time to get up the rest of the cash. But the Commission was unwilling to do away with the tariff principle, and further legislation was necessary to deal with the problem.

The Household Goods Transportation Act is a clarification of ICC authority in home moving. It establishes the authority of the ICC to permit carriers to establish rates which are based upon binding estimates and guaranteed pick-up and delivery times.120 This simple, matter-of-fact statement restores the principle of estoppel to transportation law. The mover can quote an estimate of price and schedule and the company will be bound by it.

This new law establishes the responsibility of the nationwide moving van lines for the acts of their agents. It requires that agents be fit and establishes a tighter control of the arrangement between the agents and the national companies. To this extent it now confers antitrust immunity on certain discussions between agents and the moving companies.121 Reaffirming the ICC authority to protect consumers, statutory guidelines were established to settle disputes between shippers and carriers. Previously the ICC had balked at the idea of becoming a "small claims court."122

The philosophy of the Household Goods Act is the opposite of that of the Motor Carrier Act. Here Congress felt that competition should be cou-

119. Hilton, supra n.76. See generally, Fellmeth, n. 51.
122. Hilton, supra n. 76.
plied by increased oversight. Congress also declared that the function of the ICC was to protect the homeowner and small shipper. Evidently the disparity in bargaining position between the shipper and carrier is responsible for the different concern toward moving vans. It also should be remembered that Congress attempted to meet a major criticism that was voiced about the regulatory scheme of the Motor Carrier Act, and enacted a specific consumer-oriented regulatory law.

X. THE BUS REGULATORY REFORM ACT OF 1982

The Motor Carrier Act of 1980 was applicable only to trucking companies. Buses still remained under the Motor Carrier Act of 1935.\(^{123}\) This anomaly resulted in buses being the only carrier not substantially deregulated in the last decade.

In 1982, however, motivated by pressures from the bus industry for deregulation, Congress passed and sent to President Reagan the Bus Regulatory Reform Act of 1982,\(^{124}\) to bring a liberalized regulatory regime to the intercity motor coach industry. The bill was signed into law on September 20, 1982. It is similar to the new trucking law, in that the Commission is authorized to grant a certificate to any person who is fit, willing and able to provide intercity bus transportation, unless the Commission finds that the transportation is not consistent with the public interest.\(^{125}\) The burden of proof has thus been switched to protesters. The jurisdiction of the ICC is extended to intrastate bus service.\(^{126}\) "Fitness-only" certificates shall be granted to carriers seeking to serve towns with no existing bus service, or for service substituting for discontinued passenger train or airline service.\(^{127}\) Protests are limited to carriers actually serving the applied-for route, or those with rival applications.

A rider to the bus deregulation bill prohibits the ICC from granting certificates for bus or truck service to foreign bus carriers unless the President has certified that the applicants' country does not discriminate against U.S. carriers. This was added in response to complaints by domestic motor carriers that U.S. companies were not being given rights to compete in Canadian and Mexican markets, as those countries had not deregulated entry to the motor carrier system.\(^{128}\)

The Commission has been directed to remove closed-door and other restrictions from existing certificates held by bus carriers. Companies may


mix charter and regular passengers within the same coach.\textsuperscript{129}

Antitrust immunity for rate bureaus is to be whittled down by the Bus Regulatory Reform Act. After January 1, 1983, they may not consider any joint rates. An exception is made for general rate increases or decreases. Carriers are still required to file tariffs and abide by them; and the rate bureaus may still publish tariffs, file independent actions for individual members and provide support services for member carriers.\textsuperscript{130}

A 10% up, 20% down zone of reasonableness is established for ratemaking by this Act. One year after the effective date of the act the zone is expanded to 15% increase and 25% decrease and two years after the law goes into effect, the zone increases to 20% up and 30% down. After three years the Commission may no longer suspend a rate on the grounds that it is too high or too low.\textsuperscript{131}

A new provision of the law provides that a carrier seeking to discontinue intrastate service may petition the ICC if the state has not acted within 120 days of its petition to state authority. Or if the state has denied the bus carrier’s request, the carrier may appeal to the ICC.\textsuperscript{132} The public has no such appeal if the state agency grants the request for discontinuance. (This procedure is similar to that found in old section 13(a)(2) of the Interstate Commerce Act, now 49 U.S.C. 10909, pertaining to discontinuance of intrastate passenger trains. With the advent of the Amtrak system and its freedom from regulation, the latter section is of mostly academic interest). In addition, the Commission is authorized to preempt state authority if it finds there is discriminatory state regulation of rates and practices.\textsuperscript{133}

The major provisions of the new bus law provide for greater freedom to enter markets, flexibility in setting fares, increased ability to exit markets if the service burdens interstate commerce, preemption of certain state regulatory controls and the elimination of antitrust immunity in the discussion of rates.

The law also provides for labor protection similar to that afforded in the rail and airline industries. Laid-off bus drivers and other employees are put on a preferential hiring list.\textsuperscript{134} No substantial displacement allowances are scheduled to be paid to the former employees; evidently, Congress apparently felt stung by the labor protection costs of the Conrail legislation.\textsuperscript{135} Nonetheless, some labor protection provisions were necessary to ensure against labor’s opposition to the deregulation bill. The major opposition

\textsuperscript{129} 49 U.S.C. § 10922(\textit{i})(3).
\textsuperscript{130} 49 U.S.C. § 10706(b)(4)(E).
\textsuperscript{131} 49 U.S.C. § 10708(d)(4).
\textsuperscript{132} 49 U.S.C. § 10935.
\textsuperscript{133} 49 U.S.C. 11501(e).
came mostly from legislators from rural states who rightly feared loss of services to places which had already lost regular-route trucking, railroad branch lines, passenger service, and commercial aviation.

Bus service had not been dealt with in the 1980 law because of such community fears. It was also thought that the bus industry, a duopoly dealing with individual passengers and small shippers, was not conducive to a deregulated environment. Despite the spectre of failures in the airline industry, the spirit of deregulation has continued to roll on, and now the buses will have a go at something approaching a free market. Apparently, if a little deregulation is good, more has got to be better.

XI. AFTERMATH OF DEREGULATION

The first thing to remember about trucking deregulation is that it did not occur in any degree comparable to the deregulation of air freight and airlines. Permission is still needed to enter the business, to change routes, to add commodities handled, and to raise or lower fares. The only parts of reform in trucking that could seriously be labelled "deregulation" are the increase in exempt areas, the "fitness-only" entry program for small shipments and isolated communities, and the zone of reasonableness for changing rates.

Motor carriage seemed like an excellent area for the opening up of the field to new entrants. Rights-of-way are totally provided by government, with government policing of safety standards and weight limitation. Cost of operation mainly go for purchase of equipment, labor and terminal operations. It is less expensive and less complicated to get started in the trucking business than any other transportation endeavor.

The ICC has gone along with the new law in easing entry to the business. In Art Pape Transfer, Inc., Extension—Commodities in End-Dump Vehicles\(^{136}\) the Commission stated:

Under the new entry procedure, the applicant must still come forward with some evidence of the utility of its proposed service. It is clear, though, from both the words of the statute and its legislative history, that Congress is 'lessening the burden of proof on applicants and correspondingly increasing the burden on persons opposing the application . . .'.

Once the applicant has made a prima facie case under the relaxed threshold standard, the burden of proof shifts to persons opposing the application to show that the proposed service is inconsistent with the public convenience and necessity. In sum, once the threshold case is established, the statute, as the legislative history indicates, creates a presumption in favor of entry and competition.\(^{137}\)

\(^{136}\) 132 M.C.C. 84 (1980).
\(^{137}\) Id. at 94.
In *La Bar's, Inc., Extension—Mountaintop Insulation*, the ICC went further, saying that:

Congress, after all, requires us to foster efficiency in motor carrier transportation and there may well be situations in which, considering the transportation industry as a whole, it is preferably to replace an inefficient operator with a more efficient one and promote the introduction of innovative services or prices.

But the changes in entry have not drastically changed the character of the industry. It is true that carriers have written off the value of their operating rights as zero, but this has been largely an accounting gimmick. Despite the opening of the floodgates to new entries, the established carriers have had the benefit of forty-five years of oligopoly, which has allowed them to establish operating patterns and get a headstart on the competition.

There is, of course, much wailing at the bar of the Association of ICC Practitioners and the Motor Carrier Lawyers' Association. Much of the criticism is aimed at the current ICC which, it is claimed, has been overzealous in going beyond the current law in trying to deregulate everything in sight. Motor carrier rate bureaus complain about the uncertainty of the present law and their possible exposure to antitrust sanctions in the future.

Other carriers, notably the railroads, have felt the effect of greater competition as a greater number of motor carrier competitors, and not just the high-rate general commodities carriers, have entered the field. Many of these are former agricultural carriers or co-ops who now find it easier to get backhauls. Their cut rates on backhauls have in many instances been competitive with railroad rates, especially on piggyback traffic.

Further deregulation may have an adverse effect on energy use. More competition means more trucks on the road. This may mean better service, but it also means increased use of diesel fuel. And if freight is diverted from waterways and railways, this can also mean increased use of fuel.

So far, the effects of increased entry on labor organizations have not been adequately demonstrated. All things being equal, unions would prefer an oligopolistic industry with excess profits which could be recaptured through collective bargaining. The Teamsters' Union was an opponent of deregulation and favored a tightly regulated industry. Now the unionized truckers have to face non-union competition, which should have an effect in the upcoming negotiations between the major truckers and their drivers.

There has not been a great downward move in prices to date. Of course, we still are in the theory of an inflationary economy and the independent truckers are still a small force in the industry. As mentioned...

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139. Id. at 272.
140. TRAINS, Apr., 1980, 32.
above, price-cutting has mainly occurred when an operator is seeking a
backhaul for a return move that would otherwise be deadheading. This
should become more common now that agricultural co-operatives can haul
up to one-fourth their tonnage in nonexempt commodities.

Politically, the outlook for deregulation is tied to the Reagan appointees
at the ICC. Authorized at eleven members, the Commission has been
neglected by the last three presidents, who allowed its membership to
dwindle to five Commissioners. President Reagan has vowed to appoint
Commissioners who will uphold the law and not expand on it. He was
elected with the Teamsters providing his only significant labor endorse-
ment, and significantly, did not tout deregulation in his campaign as much
as did President Carter, who was proud of his record in deregulating
transportation.

In the three years since the Motor Carrier Act of 1980 went into effect,
the ICC has embraced competition as its watchword. Congress has fol-
lowed its initiatives for the air, rail and truck industries by substantially
dereregulating the intercity bus industry. This was done by the passage of a law
which essentially duplicates the regulatory role of the ICC toward truckers.
With buses, however, Congress extended the deregulation movement to
carriers whose clientele is overwhelmingly low-income individuals, small
towns, and small package shippers, the very interests least likely to protect
themselves and the ones regulation is designed to protect.

The Motor Carrier Act of 1980, the Household Goods Transportation
Act, and the Bus Regulatory Reform Act were passed to end what many
observers thought were abuses of the regulatory process. Unimaginative
utility-type regulation had been applied to an industry with few of the char-
acteristics of natural monopoly. Congress stopped, however, at a complete
sunset law, knowing that it is important to retain some type of oversight over
the practices of an essential industry. The 1980’s will show if competi-
tion can coexist with a regulatory framework, and if the public will continue
to be well served by our privately-owned motor carriers.

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141. 49 U.S.C. 10301(b) (Supp. IV 1980). Recent legislation has been introduced to reduce
the ICC’s membership permanently to five.
Legal Issues and Answers For Commercial Users of the Space Shuttle

SHEILA FOOTER*

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I. INTRODUCTION

A new age in space exploration has dawned with the first flight of the space shuttle Columbia on April 12, 1981. The success of this revolutionary system of transportation in space has turned a science fiction dream into an incredible reality, confirming the predictions of science fiction writers more than a century ago.\(^1\) Regular trips to the moon, daily journeys into space, and stops at space stations will be routine events before very long.\(^2\) Public enthusiasm for the shuttle program has been phenomenal, and the shuttle is completely booked through 1986.\(^3\)

The space shuttle is being developed with a wide variety of uses in mind—scientific, military, and commercial, for example. Commercial use of the space shuttle by private American or foreign companies presents an unprecedented opportunity for private business to participate in the exploration of space. This participation needs to be encouraged, not only as a source of federal revenue, but also as a source of technological expertise and business management. In order to accomplish this, however, a whole new spectrum of legal issues will have to be faced. Ironically, much of the law is old—contracts, torts, conflicts, insurance, and international law, to name a few. It is the application of the law to advanced technology which is new, and which is now being established as a whole new discipline called "space law." The challenge for the next decade not only will be technological—it also will be legal, for there are few "experts" now in space law.\(^4\) Commercial users are going to require some "experts," however, to answer some difficult questions before they make a substantial financial commitment to use the shuttle.\(^5\) NASA and the legal community must recognize the concerns of the private users, and attempt to resolve them in a manner equitable to all. The future of commercial endeavor in space depends on it.

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1. See, Jules Verne, A Trip to the Moon (1865); see also H.G. Wells, The Time Machine (1895), The War of the Worlds (1898), The First Men in the Moon (1901).

2. The National Aeronautics and Space Administration (NASA) is recommending permanently manned space stations as the next primary focus of the space program. Av. Wk. & Space Tech., July 27, 1981, at 23, and NASA anticipates that it will require only six shuttle trips to build a space station beginning approximately 1989. Young & Crippen, Columbia’s Astronauts’ Own Story: Our Phenomenal First Flight, Nat’l Geographic, Oct. 1981, at 497.


5. Commercial shuttle users will be charged $90 million per flight to occupy the shuttle’s 65,000 pound capacity cargo bay beginning Oct. 1, 1985. Wash. Post, June 17, 1982, at A7.
OPERATION OF THE SPACE SHUTTLE

The space shuttle is part of NASA’s manned space transportation system (STS) and is unique in the history of aviation and space technology in many ways. It has been described as both an “aircraft” and a “space object,” but the distinction thus far has been of little significance. The shuttle is composed of three elements: the orbiter, the external tank, and the solid rocket boosters. The orbiter most resembles an airplane and is about the size of a DC-9 jetliner. It contains the work and living quarters for up to seven people and includes a 60-foot-long payload bay for storing cargo. The orbiter is launched vertically like a rocket, but lands like a glider, and is unique in that it can be reused after each flight. The external tank is initially attached to the orbiter and contains over one million pounds of liquid hydrogen and oxygen which is burned at the time of launching by the orbiter’s main engines. At launching the orbiter rides on its fuel tank, and then just before reaching orbit, drops the empty fuel tank which disintegrates and falls to the ocean. Two solid rocket boosters are bolted onto the external tank to provide over 5 million pounds of thrust to lift the orbiter and the tank off the ground. Once the solid fuel is exhausted, explosives fire the boosters away, and they drop off into the ocean where they are recovered and reused.

Nothing as big as the space shuttle has ever been put into orbit, and nothing with wings has ever flown over 17,000 miles an hour. Yet, it has been said that it is the space shuttle’s brains as much as its brawn that has made it the most ambitious flying machine ever built. From nine minutes before lift-off until just before touchdown, the space shuttle is almost totally automated, and during critical phases of flight, its computers can perform 325,000 operations a second. In addition, a tracking and data relay satellite system will soon be implemented to provide nearly continuous monitoring and help reduce the probability of experiment failure, reduce the need for on-board data storage, and allow for in-flight modifications of experiments.

The technical capabilities of the space shuttle and its cargo are almost

6. The Federal Aviation Administration (FAA) has determined that the space shuttle is not an "aircraft" within the meaning of the FAA Act. Thus, it is not subject to air worthiness, operational, navigational, or economic regulations of the FAA, one of the main concerns of NASA. Robinson, supra note 4, at 604, 605. See also Martin, Legal Ramifications of the Uncontrolled Return of Space Objects to Earth, 45 J. Air L. & Com. 457 (1980); Mosinghoff & Sloup, Legal Issues Inherent in Space Shuttle Operations, 6 J. Space L. 47 (1978).
8. NASA anticipates that the space shuttle launch system may be used for up to 100 missions. Wings for a New Era, SKY & TELESCOPE, June 1981, at 478.
9. Gore, supra note 7, at 327; see also, AV. WK. & SPACE TECH., Apr. 6, 1981, at 41.
11. The sixth shuttle mission due to be launched will combine verification of large new shuttle
beyond the imagination. Whole new vistas in science, medicine, and electronics promise to emerge from the new space law aboard the shuttle. The possibilities are infinite: a communications satellite with a 300-foot antenna can be assembled in space by a shuttle crew and can handle 250,000 calls at once from wrist radios, can relay hundreds of television channels, and can deliver mail electronically.  

Procedures not possible on earth will be simple to accomplish in space: the zero gravity of space will permit industries to make purer crystals for microelectronics, clearer glass for fiber optics, and stronger alloys from metals that refuse to mix in the earth’s atmosphere. One user is already planning to conduct pharmaceutical experiments on the shuttle in the very near future and expects to make drugs in orbit by 1986.  

About 200 other businesses, foreign governments, and individuals have also reserved space for a variety of experiments which can be conducted in self-contained payloads called “getaway specials” that require no shuttle services, such as power or deployment. These experiments for research and development purposes will be flown on a space-available basis provided they weigh less than 200 pounds and occupy less than 5 cubic feet of space. Technology is ready; now only the legal framework remains to be established.

II. Evaluation of Obvious Risks

Although the development of the space shuttle has been accompanied by an unprecedented amount of caution and preparation, it is clear that some risks of personal injury and property damage remain. There are three stages of a shuttle mission: the ascent phase, the orbital phase, and the descent phase. Each stage presents different possibilities of accidental damage or injury. Danger exists in the ascent phase from a catastrophic failure of the shuttle itself, from the jettisoned rocket boosters, and from fragments of the external tank which may not disintegrate into the atmosphere. The likelihood of damage or injury, however, is extremely remote. First of all, the shuttle launch program includes abort plans in which the boosters and external tank can be prematurely jettisoned so that the orbiter can make an emergency landing shortly after take-off. Secondly, falling debris from the rocket boosters or fuel tank are calculated by NASA to fall

program elements with deployment of the first tracking and data relay satellite.  


12. Young & Crippen, supra note 2, at 498.

13. Id.

14. NASA SPACE TRANSPORTATION SYSTEM USERS HANDBOOK, § 1 at 8.


over remote parts of the Indian or South Pacific Oceans so that the possibility of fragments falling on populated areas is very slight. And finally, since the launch ranges for the shuttle are situated over water, the chance of any mishap during the ascent phase is extremely remote.\textsuperscript{17}

During the orbital phase, there is a danger of collision between the orbiter, or an object which the orbiter places in orbit, and an object which is already in orbit.\textsuperscript{18} It is estimated that over 4,000 objects are already in orbit, and this figure will increase substantially in the next decade.\textsuperscript{19} Coupled with the fact that nearly all space activities occur within certain preferred orbital paths,\textsuperscript{20} it appears that the risk of collision will greatly increase. However, the converse is actually true, since the space shuttle system has increased capabilities to avoid space collisions. The orbiter can retrieve endangered satellites by placing them in the cargo bay,\textsuperscript{21} and it can alter a satellite’s orbit by attaching and firing rockets. Furthermore, the ground tracking system can anticipate and avoid collisions by remote control computers, thus reducing the possibility of harm. Therefore, any increased likelihood of collision resulting from the increased number of objects placed into orbit can be offset by the space shuttle’s increased ability to prevent collisions.\textsuperscript{22} Again, the risk of damage or injury during this phase of the space shuttle’s operation is small.

The last phase of the space shuttle’s operation is the descent phase when the orbiter reenters the atmosphere, burns off excess energy, and glides onto earth. The orbiter descends at about 15,000 feet a minute,\textsuperscript{23} and the heat generated by reentry is over 2,000°F. The shuttle is protected, however, by more than 30,000 silica tiles which dissipate the heat and prevent the orbiter from burning up on reentry into the earth’s atmosphere. Risks exist during this phase, however, from the loss of tiles due to the impact of the blast-off and the reentry,\textsuperscript{24} loss of control of the orbiter when entering the earth’s atmosphere at such high speeds, and possible collision with other aircraft located in the path of the descending orbiter. These risks are minimized, however, by the most sophisticated computer systems\textsuperscript{25} and the most comprehensive training programs possible. Most

\textsuperscript{17} Rothblatt, supra note 15, at 474.

\textsuperscript{18} Id.

\textsuperscript{19} 21 NASA SATELLITE SITUATION REPORT 5 (Oct. 31, 1981).

\textsuperscript{20} Rothblatt, supra note 15, at 474.

\textsuperscript{21} A new remote manipulator arm designed to operate from the orbiter’s cockpit can retrieve a satellite or other payload weighing up to 32,000 pounds. Av. Wk. & SPACE TECH., Sept. 7, 1981, at 60.

\textsuperscript{22} Rothblatt, supra note 15, at 475.

\textsuperscript{23} Gore, supra note 7, at 344.

\textsuperscript{24} Some tiles were lost during the launch of the Columbia on Apr. 12, 1981, but apparently no additional tiles were lost during reentry. The tile problem proved not to be as troublesome as originally anticipated. Sci. News, Apr. 18, 1981, at 244. Loss of tiles on the subsequent flights has also proved to be minimal.

\textsuperscript{25} Five complete and independent computer systems control the space shuttle—four main
of the problems which could arise during this phase have been anticipated by NASA and solutions have been provided.26 While no venture such as this can be perfectly fail-safe, the chances of accident or injury during the last phase of shuttle operation are also very small.

III. MAJOR CONCERNS OF COMMERCIAL USERS OF THE SPACE SHUTTLE

The use of the space shuttle by private commercial users27 presents a unique opportunity for private business to advance technology28 as well as to increase profits. Thus private business is eager to play its part in the development of the space shuttle. If the obvious risks, as noted above, are so small, and the liability of the United States Government is so great,29 what are the concerns of commercial users?

A. CONFLICTS IN THE RIGHTS OF MULTIPLE USERS

Private business has been involved in space technology for over 25

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computers, with a fifth as a backup system. If one or more disagree with the others, the majority controls. Av. Wk. & SPACE TECH., Apr. 20, 1981, at 20. See also Gore, supra note 7, at 328.
26. E.g., the reentry flight path is predetermined and cleared of all other aircraft by the FAA, minimizing the risk of collision. Mossinghoff & Sloop, supra note 6, at 51.
27. Technically a "user" is defined in the NASA LAUNCH SERVICES AGREEMENT as any United States Government (including NASA) or non-United States Government person or entity who by virtue of a contract or other arrangement with NASA, has arranged for or otherwise provided payloads or SSUS (Spinning Solid Upper Stages) services or persons to be flown on the shuttle. The "user" is the particular person or entity who is party to this Agreement.

NASA LAUNCH SERVICES AGREEMENT, Art. XII, ¶ 38. The term "private commercial user" is used by the author to mean any party to a NASA Launch Agreement except the United States Government.
28. It is well known in the scientific and business community that the development of many now successful technologies, e.g. micro-electronics, would be years behind in development, but for the impetus of the space program.
years. Satellites have been launched and placed into orbit since 1957, and almost 13,000 space objects have been launched into orbit since then. But all of these launchings have involved one satellite at a time and thus only one responsible party—either the launching government or the manufacturer or owner of the satellite. Now the space shuttle permits more than one satellite, payload, or other technological experiment to be launched and to function simultaneously on a shared shuttle flight. This raises a whole host of questions and problems for individual users: 1) Will one user have priority over another? 2) If so, how will priority be determined? 3) What happens if one payload or experiment delays the scheduled launch, or causes damage to another experiment? 4) How will liability of multiple users be assessed—by percentage of space used in the cargo bay, by percentage of number of users on a particular flight, by cost or risk of experiment? NASA has attempted to answer some of these questions by requiring a no-fault, no-subrogation, inter-party waiver of liability under which each party agrees to be responsible for any damage which occurs to its own property. Thus NASA will be responsible for all damage caused to the space shuttle by either NASA or a user, and all users will be responsible for all damage to their own property. This does not provide all the answers to all the questions, but it does make an attempt to allocate the risks according to who can best bear the burdens.

B. NASA'S RIGHT TO DELAY A LAUNCH OR TO CANCEL OR JETTISON A PAYLOAD

While these particular risks are specifically defined in NASA's Launch Agreement, they are still of concern to the commercial user, and may still be subject to further negotiation if the present terms prove to be unworkable or financially prohibitive. According to present terms, NASA has authority to delay lift-off of a launch for up to 72 hours or to suspend or postpone a

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30. Sputnik I was launched by the Russians on Oct. 4, 1957.
31. NASA SATELLITE SITUATION REPORT, supra note 19.
32. "Shared Shuttle Flight" is defined as "a shuttle flight that may be shared by more than one user." NASA LAUNCH SERVICES AGREEMENT, Art. III, ¶ 26.
33. A modification of 14 C.F.R. §§ 1214.1-1214.2 has been proposed which provides NASA with guidelines to establish priority for one payload over another previously scheduled payload. Priority will be given first to a payload urgently required for national defense or security, and second to a significant experimental or exploratory scientific payload which has a critical launch opportunity. A payload which is critical to the establishment of the Space Transportation System (STS) will also have priority.
34. NASA LAUNCH SERVICES AGREEMENT, Art. V, ¶ 3.
35. NASA will be responsible for damage caused by a user in the space shuttle (which could involve billions of dollars) only while the user is involved in STS operations. NASA LAUNCH SERVICES AGREEMENT, Art. V.
36. Other solutions to these questions will be discussed in § IV, infra.
launch of a payload under certain specifically-described circumstances. These conditions include safety, weather conditions, NASA’s equipment malfunction, failure of the user to meet “significant” obligations under the Launch Agreement, and certain other conditions which may be beyond NASA’s control. NASA may also shift the scheduled launch of cargo from one mission to another mission. A delay in a launch or a need to shift cargo presents a multitude of problems for users as well as for NASA. All cargo must be compatible with each other and must be integrated with the entire shuttle operation. This involves coordinating and orchestrating technical elements, safety, science or defense priorities, and insurance coverage. Insurance arrangements completely satisfactory for one launch, for example, may be wholly inadequate for another launch which contains a different mix of cargo.

NASA has repeatedly attempted to assure users that its authority to suspend and postpone a launch will be reasonably limited, and jettison of a user’s payload will only take place if the particular payload presents an immediate or unresolvable danger to human life, another payload, or the shuttle flight. Furthermore, NASA claims that jettison will occur only after a reasonable attempt has been made to place the payload in a safe configuration, and then only after consultation with the user. Only increased use of the space shuttle by commercial users, however, will prove whether or not NASA’s authority to suspend or jettison payloads will result in abuse or discrimination.

C. NASA’s Right to Terminate the Agreement

NASA reserves the right to terminate the Launch Agreement, in whole or in part, (i) upon a declaration of war by the United States, (ii) upon a declaration of a national emergency by Congress, (iii) upon failure of Congress to provide NASA with "adequate appropriations," and (iv) upon a written declaration by NASA that launch services are "beyond NASA’s control." While users have not expressed serious concern over termination because of war or national emergency, they have expressed concern over the latter two reasons. NASA has indicated that it will not terminate the agreement frivolously, but users are not satisfied with the escape language—"adequate appropriations" and "beyond NASA’s control"—since they are obligated to reimburse NASA for all amounts due under the

37. NASA LAUNCH SERVICES AGREEMENT, Art. IV, ¶ 4.
39. Id.
41. Hosenball, supra note 38.
Launch Agreement for launches which have actually occurred and for optional shuttle services requested by them which were actually provided or for which costs were actually incurred. NASA claims its right to terminate is equitably balanced by the right of the user to terminate the agreement at any time for any reason. While the user does have such a right, the equities still lie in favor of NASA since it will be easier for NASA to secure an alternate user, than it will be for a user to secure an alternate launch system.42

D. COSTS FOR SERVICES AND PROVISIONS FOR RELIGHT AND FOR ORBIT

The Launch Agreement is supplemented by a Payload Integration Plan (PIP) which provides a detailed technical statement of work to be performed by NASA, including a description of all "standard" and "optional" services. "Standard" services are those which are included by NASA in a basic fixed price, and "optional" services are those "extra" services for which a user must pay an additional amount.43 NASA claims that prior to gaining experience in actual operation of the space shuttle, it is unable to provide a comprehensive list of what is "standard" and what is "optional." Thus it still reserves the right to make that determination throughout negotiations with a commercial user. This, of course, places the user in a difficult and uncertain position faced with spiraling costs which are not yet defined.

Another problem related to "standard" vs. "optional" services concerns NASA's guarantee for relight. As part of the "standard" flight price, NASA has included a fee for a relight guarantee, which means that if the first scheduled launch of a payload is "unsuccessful," NASA will provide a relight of that payload at no additional cost to the user.44 NASA, however, defines the success of the launch to be that the payload reaches the orbit of the shuttle mission—not the higher orbit required for the payload. A guarantee for the higher orbit would require an additional cost to be sustained by the user by an additional fee for "optional" services or by an additional premium for insurance. Either way, it means an additional cost to the user to get his payload into the proper orbit, even though the failure of the first launch was not the user's fault.

42. The United States is also operating the Delta Launch System, and the European Space Agency (ESA) offers the Ariane. A private German company, OTRAG, has conducted some private commercial launches. Space Services, Inc., an American company, also recently launched a Minuteman booster off the coast of Texas. Other private companies are also attempting to enter the field. Address by Bockstiegle, Present and Future Regulation of Space Activities by Private Industries, AII-ABA Int'l. Conf. on Doing Bus. in Space: Legal Issues & Prac. Probs., Washington, D.C. (Nov. 12-14, 1981).

43. NASA LAUNCH SERVICES AGREEMENT, Art. II, ¶ 1. See also, NASA SPACE TRANSPORTATION USER HANDBOOK, § 3, at 1.

44. The guarantee is not applicable if the first launch attempt is unsuccessful due to the fault of the user. NASA LAUNCH SERVICES AGREEMENT, Art. II, ¶ 1. See also, 14 C.F.R. § 1214.103 (1982).

E. NASA'S EXPRESS LIMITATION OF LIABILITY FOR BREACH OF CONTRACT

NASA has expressly provided in the Launch Agreement that no action may be brought against it or its contractors for damages or for other relief for any delay in launch services.\footnote{There are two exceptions in this provision: (1) if NASA fails to obtain from all users, and certain other parties, a waiver of liability against negligent users who damage property or injure employees, a claim may be brought against NASA for this breach of contract; (2) if NASA fails to protect a user's "trade secrets" in data furnished to NASA pursuant to the Launch Agreement, an action may also be brought. Hosenball, supra note 38.} NASA agrees in the Launch Agreement to use its "best efforts" to provide proper and timely launch services, and anticipates that this language is sufficient and equitable since NASA only charges a user for actual or projected costs for launch services. There is no protection for the user, however, for costs resulting from delay, non-performance, or mal-performance, and it is clear that these costs may be considerable since many experiments may involve critical time elements, and many users may have enormous investments of capital tied up in these projects. Additionally, there may be a problem defining the term "best efforts" with NASA demanding the most liberal interpretation, and the users claiming the contrary. In order for commercial users to secure full protection of their contract rights, it appears that they will have to make arrangements for private insurance coverage, again, at additional expense.

F. THIRD-PARTY LIABILITY

Perhaps the paramount concern of commercial users of the space shuttle is their liability for injuries to third parties. Even though statistically the probability of injury is low, the possibility is always present, and if an accident occurs, there is a potential for a multi-billion dollar claim. The NASA Launch Agreement requires all commercial users to obtain third-party liability insurance naming both the user and the United States Government as insureds.\footnote{NASA LAUNCH SERVICES AGREEMENT, Art. V, ¶ 2.} The user is obligated to protect NASA and itself from third-party liability until the orbiter lands without causing damage to third parties or until the payload impacts the earth without causing damage to third parties, whichever occurs last.\footnote{Hosenball, supra note 38.} The amount of insurance and the terms and conditions of insurance must be approved by NASA, and NASA obligates each user to obtain the maximum available in the world market up to $500 million, provided that amount can be obtained at a reasonable premium.\footnote{NASA LAUNCH SERVICES AGREEMENT, Art. V, ¶ 2.} If NASA determines that it is not feasible for the user to obtain such insurance or that the user is unable to obtain adequate insurance,
NASA has the authority to provide for commercial insurance and/or indemnification and charge the user a reasonable fee. The big question is: how much insurance is available in the world market? There is some controversy as to the maximum available at the present time, but many in the insurance community believe the maximum to be $500 million per user, per shuttle mission. This poses a serious problem for multiple users on shared shuttle flights, since sufficient insurance may not be available for all users. NASA has agreed to indemnify all users for liability in excess of the amount of insurance they are able to secure, but this indemnification is not absolute. Additionally, the proposed users' insurance policies contain various exclusions, which, again, subject the users to additional liability. Thus, if the user obtains an insurance policy with exclusions, the user is a self-insurer up to $500 million, to the extent of the exclusions, and NASA will not indemnify the user until the $500 million mark is exceeded. While certain users will not be required to purchase liability insurance and will be indemnified by NASA, it is clear that the majority of commercial users are extremely concerned over insurance and indemnification issues, and further negotiation between NASA and the users is absolutely required so that the risks involved in the development of the space shuttle will be equitably apportioned.

The development of any new industry which benefits the entire public requires government subsidy or indemnification at least during the early stages of development. The space program is no exception. Without adequate government indemnification, contractors, subcontractors, and users of the space shuttle will not be able to provide the creative ideas and research and development which are necessary for the establishment of a safe and profitable space transportation system. Therefore, insurance and indemnification issues must be resolved promptly to assure dynamic commercial participation in the space shuttle program.

51. Some solutions to this problem will be discussed in § IV, infra.
52. NASA LAUNCH SERVICES AGREEMENT, Art. V, ¶ 2e(2).
53. First of all, NASA believes that the amount each user is able to secure is $500 million; therefore, NASA will not indemnify a user until the $500 million liability mark is exceeded. Additionally, indemnification is not provided if a user is negligent or is guilty of willful misconduct, and indemnification is not available to contractors or subcontractors of users. NASA LAUNCH SERVICES AGREEMENT, Art. V.
54. Hosenball, supra note 38.
55. They include: (1) those flying small self-contained payloads; (2) those providing payload specialists under NASA contracts; (3) those exempted by NASA for public interest reasons; and (4) agencies of the United States Government. 45 Fed. Reg. 74,500 (1980).
IV. SOME SOLUTIONS FOR FINANCIAL PROTECTION OF COMMERCIAL USERS

A. PROVIDE FOR PRIVATE INSURANCE AND CENTRALIZE THE INSURANCE OPERATIONS

An obvious solution for limiting financial liability is private insurance. Insurance is presently available to the commercial user and is certainly a viable answer to many problems discussed earlier. At present there are several different types of insurance on the market: 1) ground property or preignition insurance, 2) launch insurance, 3) satellite life insurance, and 4) liability insurance.\footnote{56 Marsh & McLennan, Satellite Insurance: An Overview; see also, Margo, Some Aspects of Insuring Satellites, Ins. L.J., Oct. 1979, at 555; and Johnson & Higgins, A Report on Spacecraft Insurance ( ).}

Satellite ground property insurance has been available for individual users and satellite owners for some time to protect against loss or damage during the manufacture, storage, transit, and launch site assembly phases. Coverage is also available to protect against launch delays and for launch delay penalties which may be incurred by the satellite owner. Coverage terminates with intentional ignition of the launch vehicle. Launch insurance is then available to cover loss or damage due to "launch failure." This is the most exposed phase of any satellite project, and indemnity is usually provided for the cost of a replacement spacecraft, the cost of re-launch services, and the cost of delay expenses.\footnote{57 Johnson & Higgins, supra note 56.} Users must carefully define "launch failure" and secure coverage for all necessary contingencies, such as failure to achieve proper orbital position, failure to be at proper longitude, failure to maintain proper fuel and power supplies, and failure to orbit or sustain the payload in good physical condition. Launch coverage usually extends 180 days in order to cover both the movement of the satellite from transfer to the final geosynchronous orbit and roughly the first 160 days of the satellite at the final station—a period usually devoted to the testing and final check-out of the satellite before operational use. The user will then be interested in satellite life insurance to insure that the satellite or other experiment, will function as planned once it is placed in proper orbit. Again, it will be necessary for the insured to carefully define the conditions under which a loss occurs in order to maximize protection. Finally, the commercial user must provide for third-party liability coverage. In the space business, liability insurance is the most difficult area to provide adequate protection. There are two basic factors involved. First is the fact that the history of the space transportation system is extremely limited, and the exposure in the event of a loss is enormous. Second is NASA's requirement, as mentioned above, that each user secure on each shuttle mission $500 million worth of
insurance. These problems are not insurmountable, however, and the insurance industry is anxious to participate in the commercialization of space.

What is necessary is to define the capacity of the world insurance market and to create a system to disseminate information to and from insurance agents and brokers. This means establishing a centralized insurance group which will specialize in underwriting space risks and which will register and keep on file the names of all insurance companies who wish to participate in insuring space projects. Each insurance company can register the amount of funds available at a particular time to insure a particular mission, and all information can be entered on computers and can easily be retrieved. NASA and all commercial users, contractors, and manufacturers will then know what is available, when it is available, and who wants to participate. Financial and risk analysis can be performed at this central clearinghouse, and risk and rate information can easily be made available to all potential customers. NASA and the commercial users would then know what the maximum insurance capacity is at any given time; all responsible insurance companies would be given the opportunity to participate in the risk management of the space program; and a space risk expertise would be developed which would benefit both the insurers and the insureds.

B. **Broker the Shuttle Operation**

Centralizing the shuttle insurance business solves the problem of how much insurance is available and who is willing to participate. But it does not solve the $500 million insurance requirement for each multiple user on each mission and the priority and risk allocation problems inherent in shared shuttle flights. These problems call for one private company or a joint venture of several companies knowledgeable in space shuttle operations to purchase each shuttle mission and to “broker” the entire operation. One centralized source then would pay for an entire mission, and would be responsible for the $500 million maximum insurance as the sole “user,” and would subcontract out the mission to various users allocating the cargo space and the insurance premiums among them. The “broker” would be a “mission manager,” or “commercial cargo consignee” and would be responsible for the entire technical operation of the mission, the compatibility of the various payloads, the allocation of the risks, and the priority as to who

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58. Some proposals for insurance “pools” or “consortiums” or “facilities” have been discussed by individual insurance companies or brokers, but to date no central space risk facility is operational. Insurance has been provided for early satellites through the London Aviation Market, the Associated Aviation Underwriters (AAU), and the United States Aviation Underwriters (USAU). The Marine Market has now entered the satellite launch and life insurance field, and other insurance markets are investigating entering the space risk business.
flies. No responsible user would be denied access to a shuttle mission, and professional technical management would result. NASA would be relieved of tedious day-to-day operational decisions, such as deciding which services are standard and which are optional, and NASA could concentrate on the launch services and on basic research and development, leaving the payload integration and management problems to the commercial mission manager. NASA’s budget problems would also be relieved, as the commercial manager would assume responsibility for a variety of tasks such as assuring the safety of the individual cargo elements, allocating the shuttle resources, and negotiating the individual launch agreements. Centralized brokering of a shuttle mission would result in no overlapping or wasted insurance coverage since one “user” would purchase a more efficient umbrella policy covering all risks. Costs would be reduced and users would benefit from such a brokered flight since each user would pay only for his allocated share of the entire cargo launch package, and the coverage for each launch would be more easily coordinated by the mission manager or commercial cargo consignee. Also, the liability would be more clearly focused on the one mission manager rather than on multiple users with different insurers who may attempt to disperse their responsibilities.

Private business has demonstrated its success in the past in developing new industries in the public interest, and the commercialization of space should be no exception. A commercial mission manager, created by a consortium or joint venture of private aerospace companies with technological and management expertise, would greatly advance the space program. Private brokering of the space shuttle, therefore, should be given serious consideration by NASA.

C. CHANGE NASA’S REQUIREMENTS

If the insurance and management problems of the space shuttle cannot be resolved by centralizing the insurance operations and brokering the shuttle operations, then certain requirements presently proposed by NASA must be changed. Since the capacity of the world insurance market seems to be at or near its maximum and multiple users are each required to obtain

59. Of course priority would always be given to payloads affecting national defense or security.

60. NASA Administrator, James M. Beggs, has stated that he wants to divest the agency of shuttle operational responsibility starting about 1985. “NASA is not an operating agency.” he has said; “we are in the research and development business.” AV. WK. & SPACE TECH., Mar. 1, 1982 at 20.

61. From railroads to automobiles to airlines, the success story is clear. Now it is predicted that industries as diverse as engineering, advertising, manufacturing, repair, communications, and sales, among others, will benefit from ventures into outer space. Barham, Count-Up For Space Insurance, J. Ins., Jan.-Feb. 1982, at 26.
that maximum, the conflict must be resolved. There is no problem, however, as the NASAct and corresponding regulations do authorize alternative actions. 62 1) NASA can purchase an insurance policy for each mission of the space shuttle and can allocate the premiums among the users on that mission; 2) NASA can designate one user to purchase a single insurance policy for all the users on a particular flight and, again, allocate the premiums; and 3) NASA can indemnify all the users on a particular mission and charge a fee for the indemnification. 63 The only difficulty with these solutions is that they may present certain administrative problems, and they could result in putting NASA in the insurance business—a position NASA, at present, rejects. 64 The solutions are feasible, however, and are clearly authorized by law. They do warrant careful consideration as a means of providing financial protection to commercial users of the space shuttle.

V. CONCLUSION

The space shuttle Columbia has now flown 6 successful missions. The next flights are already scheduled to include commercial payloads. Therefore, the time is now to resolve the legal issues and to provide for the financial protection necessary for commercial use of the space transportation system. The concept of scheduled travel in space, conceived a century ago and popularized only recently by all the “Star Trekkies” is really not a surprise. We all knew it would happen; the only question was—when? Now the dream of spaceships and space stations is a reality, and we must deal with the consequences. If science can create the product, then surely law can protect the system. Continued exploration in space depends on it. 65

63. The premiums could even be placed in an indemnification fund to pay future claims.
65. At the time this article went to press, 6 space shuttles had been launched. The sixth shuttle mission on the space shuttle Challenger is due to be launched in late March or early April, 1983, as soon as cracks in the main engine can be repaired. AV. WK. & SPACE TECH., Mar. 7, 1983, at 23.
Medical Certification of Flight Crews: Standards and Procedures

J. SCOTT HAMILTON*

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I.  INTRODUCTION

The number of active civilian aviators in the United States licensed by the Federal Aviation Administration (FAA) is rapidly approaching the one million mark, and over fifty thousand new airmen are earning FAA certification each year. In order to exercise the privileges of an airman certificate, such as a pilot’s license, each of these individuals must also hold a currently valid FAA airman medical certificate. On the average, the FAA presently refuses medical certification to one applicant out of every hundred. Loss of the medical certificate can sound the death knell on a professional aviator’s career or a recreational flyer’s pursuit of a favorite avocation. Several legal alternatives are available to frustrated applicants for aviation medical certification. A few published scholarly writings have addressed the


3. "Airman" means an individual who engages, as a person in command or as pilot, mechanic, or member of the crew, in the navigation of aircraft while under way; and... any individual who is directly in charge of the inspection, maintenance, overhauling or repair of aircraft, aircraft engines, propellers, or appliances; and any individual who serves in the capacity of aircraft dispatcher of air-traffic control-tower operator. 49 U.S.C. § 1301 (as amended, 1958).

4. 14 C.F.R. § 61.3(c) (1981) applies this requirement to all pilots except those piloting balloons and gliders. 14 C.F.R. §§ 63.3(a) and (b) (1982). Apply these requirements to flight engineers and flight navigators. 14 C.F.R. §§ 65.31(c) and .33(d) (1982). Apply this requirement to the operators of air traffic control towers except those employed by the FAA. Thus, it is only those airmen whose duties involve serving as a member of a flight crew or operating a non-FAA air traffic control tower who are required to hold an airman medical certificate in addition to their operating certificate.


6. See generally Notes 209-278, infra, and accompanying text.
procedural aspects of these cases, but the applicable underlying substantive law has not yet benefited from such elucidation.

The National Transportation Safety Board (NTSB), which is entrusted with the responsibility of administrative review of certain of these cases, has cautioned that precedent in aviation medical cases is of little value and that each such proceeding must be determined on its own merits on the basis of the individual's medical record, expert medical testimony presented at hearing and statistics relating the individual's medical condition, age, lifestyle and other risk factors to safety in the flight environment. While that caveat must be borne in mind, the value of precedent in these cases cannot be wholly discounted. In all probability, no two factually-identical cases have ever been tried in any area of the law, and it is a most basic legal doctrine that, within the bounds of constitution, statute, regulation and precedent, the outcome of each case, regardless of its nature, must ultimately turn upon its own facts.

In these cases, as in other areas of litigation, counsel cannot hope to provide adequate legal representation without first determining the answer to each of the following questions:

What are the facts?
What is the applicable substantive law?
What is the applicable procedural law?

Additionally, if either the existing substantive or procedural law is adverse to a decision in favor of one's client, the following additional questions must be satisfactorily answered:

What ought the law be, and why?
What is the procedure for seeking such a change in the law?

This article will attempt to address each of these questions in the greatest possible detail and in so doing provide counsel representing individuals in aviation medical certification cases a chart by which to navigate this heretofore largely uncharted area of the law.

II. Standards

The standards for issuing medical certificates to airmen appear in the Federal Aviation Regulations (FARs) at 14 C.F.R. §§ 67.1-.31. The regulations set out the standards for issuance of three different classes of medical

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8. 49 U.S.C. §§ 1422(b) and 1429(a) (as amended, 1958).
certificates. The first-class medical certificate, which is required of persons exercising airline transport pilot privileges, involves the most stringent standards. The second-class medical certificate, required of those persons exercising commercial pilot and air traffic control tower operator duties, is based upon somewhat less rigorous standards. Finally, the third-class medical certificate, required of persons exercising private pilot or student pilot privileges, is based upon the most lenient standards.

The regulations governing the issuance of each type of certificate prescribe minimum standards for visual acuity, ears, nose, throat and equilibrium, mental and neurologic, cardiovascular, and general medical condition of the applicant. Additionally, a separate FAR governing airman and crew member requirements for air carriers engaging in interstate or overseas air transportation under a certificate of public convenience and necessity or other appropriate economic authority issued by the Civil Aeronautics Board (CAB) prohibits persons over the age of sixty years from serving as pilots of aircraft engaged in such operations. Because this so-called "Age Sixty Rule" has been historically justified on the basis of health considerations, it will also be discussed here.

The aeromedical certification standards are largely concerned with three areas:

13. 14 C.F.R. § 61.123(c) (1982), which excepts commercial glider and balloon pilots, who are only required to certify that they have no known medical defect which would make them unable to pilot a glider or balloon.
14. 14 C.F.R. §§ 65.31 and .33 (1982), which excepts air traffic control tower operators employed by the FAA.
16. 14 C.F.R. § 61.103(c) (1982) which excepts private glider and balloon pilots, who are required only to certify that they have no known medical defect which would make them unable to pilot a glider or balloon.
17. 14 C.F.R. § 61.83(c) (1982) which also excepts student pilots of gliders and balloons. Student pilots are not required to obtain a student pilot's certificate and class III aviation medical certificate until ready to operate an aircraft in solo flight. 14 C.F.R. § 61.87(a) (1982).
19. See notes 34-48, infra, and accompanying text.
20. See notes 49-55, infra, and accompanying text.
21. See notes 56-68, infra, and accompanying text.
22. See notes 69-73, infra, and accompanying text.
23. See notes 74-83, infra, and accompanying text.
27. 14 C.F.R. § 121.363(c) (1982).
Can the person be expected to accurately perceive the sensory clues necessary to control the aircraft, to see and avoid other aircraft, and to follow the directions of air traffic controllers? 28

Is the person likely to unpredictably experience a suddenly incapacitating medical event in flight? 29

Is the person likely to operate aircraft irresponsibly so as to endanger other people? 30

The certification standards are structured so that any medical condition which should result in an unfavorable answer to any of these basic questions should trigger an initial denial of medical certification. 31

As will be shown later, 32 such an initial denial is not necessarily the last word. Rather, an individual may be able to receive an aviation medical certificate notwithstanding his inability to meet the letter of the certification standards if the particular circumstances of the individual's current medical condition would indicate favorable answer to each of these three questions. 33

It is necessary to begin the discussion of certification criteria by examining in detail the specific regulatory medical standards for issuance of the three different classes of aviation medical certificates.

A. Vision

1. Distant Vision: The airline transport pilot is required to demonstrate distant visual acuity of 20/10 or better in each eye separately, without correction; or of at least 20/100 in each eye separately corrected to 20/20 or better with corrective lenses (glasses or contact lenses). Where corrective lenses are required, it is also required that the pilot wear them while performing pilot duties. 34 The distant visual acuity standards required

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28. These concerns are reflected particularly in the standards for vision and hearing discussed at notes 34-53, infra, and accompanying text.

29. This concern is particularly reflected in the neurological and cardiovascular standards discussed at notes 66-73, infra, and in the rules governing diabetes discussed at notes 74-75, infra, and accompanying text.

30. These concerns are particularly reflected in the mental and neurologic standards discussed at notes 56-65, infra, and accompanying text.

31. See notes 98-117, infra, and accompanying text.

32. See notes 119-121, infra, and accompanying text.

33. For example, pilots who have suffered a heart attack or other evidence of coronary artery disease and who are therefore specifically disqualified from aviation medical certification (see notes 69-73, infra, and accompanying text) have been certified by exemption (see notes 209-231, infra, and accompanying text) where subsequent events such as successful coronary artery bypass surgery have reduced the likelihood of any sudden and incapacitating repetition of that medical event to a statistically acceptable level. See, e.g., Petition of McDonald, Grant of Exemption, Federal Aviation Administration, U.S. Dept. of Transp., Exemption No. M-14690, Regulatory Docket No. 19551 (issued by the Federal Air Surgeon on February 26, 1981).

of commercial pilots are identical to those for airline transport pilots.\textsuperscript{35} Private and student pilots, however, are required to demonstrate a minimum distant visual acuity of only 20/50 or better in each eye separately, without correction; or if the vision in either or both eyes is poorer than that, it must be corrected to 20/30 or better in each eye with corrective lenses (glasses or contact lenses).

2. \textbf{Near Vision}: The airline transport pilot must demonstrate near vision of at least \( v = 1.00 \) at eighteen inches with each eye separately, with or without corrective lenses.\textsuperscript{36} The commercial pilot is only required to demonstrate enough near vision accommodation to be able to read official aeronautical charts,\textsuperscript{37} while the private or student pilot is not required to demonstrate any specific near vision capability.\textsuperscript{38}

3. \textbf{Color Vision}: The airline transport pilot is required to demonstrate normal color vision, while commercial, private and student pilots are only required to demonstrate the ability to distinguish between the red, white and green colors used in aviation signal lights.\textsuperscript{39}

4. \textbf{Peripheral Vision}: Airline transport and commercial pilots are required to demonstrate normal fields of vision.\textsuperscript{40} No similar requirement is imposed on private or student pilots.

5. \textbf{Pathology}: The airline transport pilot must have no acute or chronic pathological condition of either eye or related glands which might interfere with proper functioning or which might progress so as to interfere with its proper functioning or might be aggravated by flying.\textsuperscript{41} The commercial pilot is allowed no pathology of the eye,\textsuperscript{42} and the private and student pilot is allowed no serious pathology of the eye.\textsuperscript{43}

6. \textbf{Binocular Vision}: Both the airline transport pilot and the commercial pilot are required to demonstrate a bifoveal fixation\textsuperscript{44} an vergencephoria\textsuperscript{45} relationship sufficient to prevent a break in fusion under


\textsuperscript{36} 14 C.F.R. § 67.13(b)(2) (1982).


\textsuperscript{38} Compare 14 C.F.R. § 67.17(b) (1982) to the regulations cited in the two preceding footnotes. Note that the latter regulation does not specifically address any performance requirement for visual accommodation.


\textsuperscript{40} 14 C.F.R. § 67.13(b)(4) (1982). Note that no similar language appears in §§ 67.15(b) or 67.17(b).

\textsuperscript{41} 14 C.F.R. § 67.13(b)(5) (1982).

\textsuperscript{42} 14 C.F.R. § 67.15(b)(4) (1982).

\textsuperscript{43} 14 C.F.R. § 67.17(b)(2) (1982).

\textsuperscript{44} See generally W. DeHaan, \textit{THE OPHTALMOLOGIST'S GUIDE TO PILOTS' VISION} 36-38 (1982).

\textsuperscript{45} Id. at 135-138.
conditions normally occurring during the performance of pilot duties. Typically, however, these pilots are not actually required to submit to testing to determine these capabilities unless screening tests indicate more than one prism diopter of hyperphoria, six prism dipters of esophoria, or six prism dipters of exophoria. No comparable binocular vision capability is required to be demonstrated by private or student pilots.

B. Hearing

1. Acuity: The airline transport pilot must demonstrate the ability to hear a whispered voice at a distance of at least 20 feet with each ear separately or demonstrate a hearing acuity of at least fifty percent of normal in each ear throughout the effective speech and radio range as shown by a standard audiometer. The commercial pilot need demonstrate only the ability to hear the whispered voice at a distance of eight feet with each ear separately, while private and student pilots need only demonstrate the ability to hear the whispered voice at three feet.

2. Pathology: The airline transport pilot and the commercial pilot are not permitted to be certified if they have any acute or chronic disease of either the middle or the inner ear, mastoid or open perforation of the eardrum. Private and student pilots, however, are medically disqualified only upon the basis of acute or chronic disease of the inner ear.

47. Id. Procedures for administration of the screening tests are described in Federal Aviation Administration, U.S. Dept. of Transp., Guide for Aviation Medical Examiners, 54-61 (1970) [hereinafter cited as Guide for Aviation Medical Examiners].
50. 14 C.F.R. § 67.15(c)(1) (1982). The National Transportation Safety Board has questioned the validity of the whispering test, due to such variables as the background noise level in the examining room, the tonal quality of the whispered words, the examiner's difficulty in maintaining a constant volume throughout the test, and the examiner's voice inflections, and recommended that the FAA require all applicants for first and second class medical certificates be periodically administered an audiometric hearing test. National Transportation Safety Board Safety Recommendation (A-77-7 (February 17, 1977)). The FAA has reportedly rejected that recommendation, pending development of a simplified hearing screening device now under development at the FAA Civil Aeromedical Institute in Oklahoma City. AVIATION DAILY, June 20, 1977 at p. 278.
C. NOSE AND THROAT

Any disease or malformation of the nose or throat that might interfere with or be aggravated by flying is disqualifying for all classes of aviation medical certificate. 54

D. EQUILIBRIUM

Any disturbance in equilibrium is disqualifying for all classes of aviation medical certificate. 55

E. MENTAL AND NEUROLOGIC

Included under this broad general category of standards are standards for mental and personality disorders (including psychoses, neuroses, alcoholism and drug dependence) and neurologic disorders including epilepsy and other convulsive disorders.

1. Psychoses: An established medical history or clinical diagnoses of a psychosis is disqualifying for any class of aviation medical certificate. 56

2. Alcoholism and Drug Dependence: An established medical history or clinical diagnosis of alcoholism 57 or drug dependence 58 disqualifies

54. 14 C.F.R. §§ 67.13(c)(5), 67.15(c)(5) and 67.17(c)(3) (1982).
55. 14 C.F.R. §§ 67.13(c)(6), 67.15(c)(6) and 67.17(c)(4) (1982). No specific testing is required to be performed however to screen applicants for disturbances in equilibrium.
56. 14 C.F.R. §§ 67.13(d)(1)(i)(b), 67.15(d)(1)(i)(b) and 67.17(d)(1)(i)(b) (1982). The generally accepted diagnostic criteria for distinguishing between categories of mental disorder, such as between psychoses, neuroses, and personality disorders, are those recognized by the American Psychiatric Association and published in its Diagnostic and Statistical Manual of Mental Disorders. See, e.g., Administrator v. Doe, 2 N.T.S.B. 59, 74 (1973), n.31 and associated text. This manual is periodically updated by the Association in consultation with the Academy of Psychiatry and the Law, the American Academy of Child Psychiatry, the American Academy of Psychoanalysis, the American Association of Chairmen of Departments of Psychiatry, the American College Health Association, the American Orthopsychiatric Association, the American Psychoanalytic Association and the American Psychological Association to reflect growing ability within the discipline to more precisely refine diagnostic criteria. American Psychiatric Association, Diagnostic and Statistical Manual of Mental Disorders (3d Ed. 1980) [hereinafter cited as DSM-III] at 1-12. As a result, mental standards for aviation medical certification are continually revised to reflect the latest consensus for diagnostic criteria without going through the often cumbersome Administrative Procedure Act process for amending the rules, themselves. See, e.g., Deposition of Lloyd D. Montgomery, M.D., in Administrator v. Wendler, N.T.S.B. Docket SE-4887 (October 16, 1980).
57. Unless there is established clinical evidence, satisfactory to the Federal Air Surgeon, of recovery, including abstinence from alcohol for not less than the preceding 2 years. "Alcoholism" implies something more than overindulgence, generally a pattern of use in which a person's intake of alcohol has been great enough to damage his physical health or personal or social functioning or where the individual has become dependent upon alcohol. Petition of Ray, 2 N. Trans. S. Dec. 768 (1974); DSM-III (n.56, supra) at 170.
58. Drug "dependence" is a more severe diagnosis than drug "abuse" and generally is characterized by tolerance (the need for markedly increased amounts of the drug to achieve the desired effect, or markedly diminished effect with regular use of the same amount of the drug) or by withdrawal after cessation or reduction in use of the drug. DSM III (n.56, supra) at 163-179.
the individual for all classes of aviation medical certification. 59

3. Neuroses, Personality Disorders, and Other Disqualifying Mental Conditions: The standards become more nebulous in this area. For all classes of aviation medical certificates an individual is disqualified by an established medical history or clinical diagnosis of a personality disorder60 that is severe enough to have repeatedly manifested itself by overt acts51 or by any other personality disorder, neurosis,62 or mental condition63 which the Federal Air Surgeon64 finds (based on the individual’s case history and appropriate, qualified medical judgment) disables the individual from safely performing pilot duties or is reasonably expected to so disable the individual within two years.65

4. Epilepsy: An established medical history or clinical diagnosis of epilepsy disqualifies the individual from holding any class of aviation medical certificate.66


No person may be denied or deprived of Federal civilian or other employment or a Federal professional or other license or right solely on the grounds of prior alcohol abuse or prior alcoholism.


60. Personality traits are enduring patterns of perceiving, relating to, and thinking about the environment and oneself, and are exhibited in a wide range of important social and personal contexts. It is only when personality traits are inflexible and maladaptive and cause either significant impairment in social or occupational functioning or subjective distress that they constitute "personality disorders". DSM-III (n.56, supra) at 305.


62. At the present time, however, there is no consensus in the field of psychiatry as to how to define "neurosis". DSM-III (n.56, supra) at 9. That manual therefore deletes the diagnostic class of "Neuroses" which had previously appeared in the second edition (DSM-II) and uses only the phrase "neurotic disorder", and uses that only descriptively to refer to a mental disorder in which the predominant disturbance is a symptom or group of symptoms that is distressing to the individual and is recognized by him or her as unacceptable and alien even though the individual's reality testing is grossly intact and their behaviour does not actively violate gross social norms, but the disturbance is relatively enduring or recurrent without treatment and is not limited to a transitory reaction to stressors and there is no demonstrable organic etiology or factor.

63. Presumably what DSM-III (n.56, supra) refers to as a "mental disorder". That manual, however, although providing a classification of "mental disorders" states (at p. 5) there is no satisfactory definition that specifies precise boundaries for the concept "mental disorder".

64. At this writing, the current Federal Air Surgeon is Homer L. Reighard, M.D., a full-time employee at FAA Headquarters in Washington, D.C.


5. Unconsciousness: An episode or episodes of disturbance of consciousness is disqualifying for all classes of aviation medical certificate unless there is a satisfactory medical explanation for the cause of the event.\textsuperscript{67}

6. Other Convulsive Disorders, Disturbances of Consciousness and Neurological Abnormalities: Individuals may be denied any class of aviation medical certification if they have an established medical history or clinical diagnosis of some other convulsive disorder, disturbance of consciousness, or neurological condition which the Federal Air Surgeon finds (based on the individual’s case history and appropriate, qualified medical judgment) disables the person from safely performing as a pilot or is reasonably expected to so disable the person within two years.\textsuperscript{68}

\section*{F. Cardiovascular}

1. Heart Attack: The medical standards disqualify a person who has an established medical history or clinical diagnosis of myocardial infarction from any class of aviation medical certificate.\textsuperscript{69}

2. Coronary Artery Disease: Similarly, angina pectoris\textsuperscript{70} or a history or diagnosis of coronary artery disease that the Federal Air Surgeon finds has been clinically significant\textsuperscript{71} disqualifies the person from holding any class of aviation medication certificate.\textsuperscript{72}

3. Additional Cardiovascular Testing Required of Airline Transport Pi-


\textsuperscript{68} 14 C.F.R. §§ 67.13(d)(2)(ii), 67.15(d)(2)(ii) and 67.17(d)(2)(ii) (1982). In order to be disqualifying, such a condition must substantially increase the individual’s risk of sudden and unpredictable incapacitation in flight. Petition of Mosely, 2 N.T.S.B. 1824 (1975).

\textsuperscript{69} 14 C.F.R. §§ 67.13(e)(1)(i), 67.15(e)(1)(i) and 67.17(e)(1)(i) (1982).

\textsuperscript{70} Severe pain radiating from the heart, generally to the shoulder and down the left arm, symptomatic of a heart attack in progress.

\textsuperscript{71} As demonstrated by arteriography or significant electrocardiographic changes, for example. Petition of Dillahunt, 1 N.T.S.B. 202 (1968).

\textsuperscript{72} 14 C.F.R. §§ 67.13(e)(1)(ii) & (iii) (1982). Until recently, coronary artery disease itself, unless it had progressed to such a point that it could be reasonably expected to lead to a heart attack, was not disqualifying, and the Federal Air Surgeon’s finding in such a case was subject to review (see generally note 147 and notes 224-255, infra, and accompanying text). On review, the National Safety Board interpreted the “reasonably be expected” test as one under which the individual would be disqualified if and only if there were a reasonable expectation of a heart attack, and not merely some greater chance of a heart attack. Petition of Levin, 2 N.T.S.B. 298 (1973); Petition of Ewing, 1 N.T.S.B. 1192 (1971). In a highly-controversial amendment published April 15, 1982, however, the “reasonable expectation” standard was dropped in favor of this apparently stricter standard. 47 Fed. Reg. 16298 (1982). There is presently confusion over whether this change precludes effective NTSB review in these cases, and the amendment is the subject of a petition for judicial review now pending in the U.S. Court of Appeals for the District of Columbia Circuit. Schwartz v. Helms, Civil Action No. 82-1527 (D.C. Cir., filed May 11, 1982).
lots: Additionally, airline transport pilots (but not commercial, private or student pilots) are required to submit to periodic electrocardiographic (EKG) examinations\(^\text{73}\) and are subject to maximum blood pressure limits for their age (see Table 1).

G. General Medical Condition

1. Diabetes: A person who has an established medical history or clinical diagnosis of diabetes mellitus that requires insulin or any other hypoglycemic drug for control is disqualified from holding any class of aviation medical certificate.\(^4\) However, diabetics who are able to control their dis-


\(^{74}\) 14 C.F.R. §§ 67.13(f)(1), 67.15(f)(1) and 67.17(f)(1) (1982). The Federal Air Surgeon has never granted an exemption (see notes 211-223, infra, and accompanying text) to an individual whose diabetes is controlled by medication. Letter from Basil G. Maile, Director, Medical/Technical Assistance Department, Aircraft Owners and Pilots Association to Phillip E. Morris (July 25, 1978). This policy is rigid, and is said to be based upon recommendations from a panel of specialists in the fields of diabetes and aviation medicine convened by the Flight Safety Foundation and reviewed by the American Diabetes Association. Petition of Poole, Docket No. Sm-2752, NTSB Order No. EA-1649, slip op. (July 24, 1981); and Aviation, Space, and Environmental Medicine, November, 1978, at 1357. These recommendations, however, are rather ancient, the Flight Safety Foundation recommendations having been the result of a study contracted for by the Civil Aeronautics Administration (precursor to the FAA) in June of 1956 and implemented in October of 1959. Letter from Stanley R. Mohler, M.D., Director, Aerospace Medicine, Wright State University School of Medicine (December 5, 1978). The position of the American Diabetes Association was stated in 1965 and reaffirmed in 1970. Letter from J. Richard Connelly, Executive Director, American Diabetes Association to H.L. Reighard, M.D., Deputy Federal Air Surgeon (January 19, 1965) and letter from J. Richard Connelly, Executive Director, American Diabetes Association to Jon L. Jordan, M.D., Chief, Projects Development Branch, Office of Aviation Medicine, Federal Aviation Administration (October 12, 1970). Since that time, the American Diabetes Association has, however, repeatedly indicated its willingness to re-evaluate that position, especially for non-commercial pilots. Letter from Ernest M. Frost, Executive Vice President, American Diabetes Association to R.V. Siegel, M.D., Federal Air Surgeon (August 22, 1974) and letter from Dorothy M. Born, Coordinator of Patient Education, American Diabetes Association to J. Scott Hamilton (November 20, 1978), which describes a March 29, 1977 inquiry to the FAA on this point. The FAA did not respond at all to the first of these suggestions to reconsider the policy, and rather brusquely dismissed the second. Interestingly, the ICAO Standards and Recommendations (note 51, supra) at 41 do not recommend disqualifying diabetic non-commercial pilots whose disease is controlled by oral drugs administered under medical supervision and control. The supposed basis for the Federal Air Surgeon’s policy is concern over the potential for a hypoglycemic reaction. Attachment to letter from Audie W. Davis, M.D., Chief, Aeromedical Certification Branch, Civil Aeromedical Institute, Federal Aviation Administration to J. Scott Hamilton (December 4, 1978). However, the Federal Air Surgeon has refused to grant an exemption even to a 44-year old man who had been diagnosed as diabetic at age 14 and whose disease had been controlled by medication for 30 years without a single incident of reaction and who had successfully flown gliders without incident for years (see note 16, supra) and who only sought to fly private aircraft, non-commercially. Petition of Morris, Denial of Exemption, Federal Aviation Administration, U.S. Dept. of Transp. Exemption No. M-13326, Regulatory Docket No. 18854 (issued by the Federal Air Surgeon on June 27, 1979) and supporting medical records and correspondence in that file. In these circumstances, such an inflexible rule seems arbitrary and capricious to this author.
ease by diet are not disqualified from certification.\textsuperscript{75}

2. \textit{Other Physical Deficiencies}: Finally, the medical standards contain a catch-all provision for each class of aviation medical certificate allowing the Federal Air Surgeon to deny aviation medical certification to a person for any organic, functional, or structural disease, defect or limitation other than those listed above if he finds (based on the person’s case history and appropriate, qualified medical judgment) that the particular deficiency disables the individual from safely performing airman duties or is reasonably expected to so disable the individual within two years.\textsuperscript{76}

3. \textit{"Disqualifying Medication"}: The regulatory standards do not address the subject of medication and do not provide for disqualification of individuals from certification based on prescription of medication by their physicians. Yet, the FAA continues to regularly refuse to issue aviation medical certificates based on the applicant’s use of a "disqualifying medication",\textsuperscript{77} while readily admitting that there is really no such thing and that no standards therefore have been prescribed or published,\textsuperscript{78} as would clearly be required by the provisions of the Administrative Procedure Act.\textsuperscript{79} It appears that what the FAA is really trying to do in these cases is to diagnose the underlying physical condition from the medication prescribed.\textsuperscript{80} In no other situation is this considered acceptable medical logic.\textsuperscript{81} This whole area of "disqualifying medication" has created a quagmire of illogical thinking\textsuperscript{82} which undermines the FAA’s medical credibility.\textsuperscript{83}

\begin{itemize}
\item \textsuperscript{75} \textit{Aviation, Space, and Environmental Medicine}, November, 1981, at 713.
\item \textsuperscript{77} This is generally done under the catch-all provisions of subsection (f)(2) of the regulation, note 76, \textit{supra}, and accompanying text. Letter from Audie W. Davis, M.D., Chief, Aeromedical Certification Branch, Civil Aeromedical Institute, Federal Aviation Administration to Robert L. Clark, dated May 24, 1979 and letter from Dr. Davis to George Lebsack (December 27, 1979); \textit{Aviation, Space, and Environmental Medicine}, February, 1981, at 130; \textit{Aviation, Space, and Environmental Medicine}, September, 1977, at 866.
\item \textsuperscript{78} Letter from Audie W. Davis, Chief, Aeromedical Certification Branch, Civil Aeromedical Institute, Federal Aviation Administration to J. Scott Hamilton (November 16, 1977).
\item \textsuperscript{79} 5 U.S.C. §§ 551-559 (Supp. IV 1980).
\item \textsuperscript{80} Petition of Simmons, N.T.S.B. 1431 (1975).
\item \textsuperscript{81} Interview with Richard L. Masters, M.D., Medical Director, Airline Pilots Association and Ann McFarlane, M.D., Medical Consultant, Hamilton & Hill, P.C., in Denver, Colorado (December 9, 1981).
\item \textsuperscript{83} \textit{id}. In the letter cited therein at note 124, Dr. Coffelt goes on to say, "I have never been
H. Age

Another area in which the FAA’s medical credibility is in jeopardy is in its rigid adherence to the so-called “Age Sixty Rule” which prohibits persons over the age of sixty from piloting airliners and air freighters. Although this rule survived the last round of court challenges, its justification appears more dubious with the subsequent publication of several more sophisticated and statistically valid studies of the relationship between chronological age and physical health. The coincidence of publication of these studies with a growing public awareness of and concern for the problems of unjustifiable age discrimination sets the stage upon which the FAA must choose between playing the role of an enlightened leader by deleting this arbitrary rule or maintaining and enforcing a rule no longer justified in light of advancing medical knowledge.

III. Procedure

The aviation medical case may arise in a variety of ways, and the manner in which it arises can be a determining factor in the procedure to be followed to resolve the controversy. Typically, an aviation medical case arises upon the occurrence of one of the following events:

A. The person initially applying for an aviation medical certificate is refused certification.

B. An aviator holding an aviation medical certificate is denied recertification

4. See notes 24-27, supra, and accompanying text. The FAA admittedly denies all petitions for exemption from the Age 60 Rule. Gray v. FAA, 594 F.2d 793 (10th Cir. 1979).

5. Gray v. FAA, note 4, supra; Rombough v. FAA, 594 F.2d 893 (2d Cir. 1979); Starr v. FAA, 589 F.2d 307 (7th Cir. 1978), and cases cited therein. Justification offered by the Administrator for this inflexible rule is studies indicating that “sudden incapacity due to . . . medical defects becomes significantly more frequent in any group reaching age 60” and the alleged infeasibility of attempting to individualize assessments of pilots medical qualifications without regard to chronological age. 24 Fed. Reg. 97-9768 (December 5, 1959). The latter part of that argument seems incongruent when one considers that the Federal Air Surgeon and his consultants routinely individualize assessments of pilots' medical qualifications without regard to chronological age in considering petitions for exemption to other regulatory standards, such as cardiovascular cases. See notes 223-224, infra, and accompanying text.

6. W. DeHaan, The Optometrist's and Ophthalmologist's Guide to Pilots' Vision 112-113 (1982); Mohler, Reasons for Eliminating the “Age 60” Regulation for Airline Pilots, 52 Aviation, Space, and Environmental Medicine, 445 (August, 1981); Mohler, Aircraft Accidents and Age, 4 Aging and Work 54 (Winter 1981). See also notes 200-201, infra, and accompanying text.

7. See notes 98-149, infra, and accompanying text. While only twenty-eight percent of all applications for aviation medical certificates (both new and renewals) are made by new airmen coming into the system (see note 2, supra, and accompanying text), fifty percent of the denials are attributable to these new applicants. The Philosophy and Limitations of FAA Aeromedical Standards note 2, supra, at 2.
upon periodic re-examination. 88

C. The FAA discovers that a person has made a false statement on an application for an aviation medical certificate. 89

D. The FAA discovers that an Aviation Medical Examiner 90 has made an error or omission in the conduct of an aviation medical examination. 91

E. An aviator holding a current aviation medical certificate experiences a medical event which calls into question their ability to safely continue to perform pilot duties. 92

F. The FAA requests that the holder of a current aviation medical certificate submit to re-examination, 93 additional medical testing, 94 or provide additional medical records. 95

G. The FAA initiates proceedings to suspend or revoke an individual’s current aviation medical certificate. 96

H. An airline pilot reaches the sixtieth anniversary of his birth. 97

A. DENIAL OR DEFERRAL OF CERTIFICATION ON INITIAL APPLICATION

Virtually all initial applications for aviation medical certification and periodic renewal of certification are first presented to a physician in private practice who has been designated by the FAA as an aviation medical examiner (AME). 98 The AME gathers the person’s medical history and conducts a physical examination and laboratory testing. 99 The AME then initially issues 100 or denies 101 aviation medical certification, based upon

88. See notes 150-163, infra, and accompanying text.
89. See notes 164-170, infra, and accompanying text.
90. See note 98, infra, and accompanying text.
91. See notes 171-178, infra, and accompanying text.
92. See notes 182-187, infra, and accompanying text.
93. The Federal Aviation Act of 1958 provides, at 49 U.S.C. § 1429(a) (1976) that:
   The Secretary of Transportation may... re-examine any civil airman.
94. For example, where a cardiac arrhythmia is noted on examination, a cardiologic evaluation including electrocardiography and chest X-ray will be requested. Guide for Aviation Medical Examiners, supra note 47, at 41. See also infra notes 190-195 and accompanying text.
95. For example, where the individual has an established medical history or clinical diagnosis of a previous heart attack, angina, or other evidence of coronary artery disease, the FAA will require the individual to furnish the agency with summaries and records of previous related hospitalizations, observation and treatment periods and internal follow-up data, including history, physical findings, laboratory examinations, chest x-ray reports, and copies of all relevant electrocardiograms. Guide for Aviation Medical Examiners, supra note 47, at 51. See also infra notes at 188-195 and accompanying text.
96. See infra notes 196-202 and accompanying text.
97. See supra notes 24-27 and 84-86 and infra 203-208 and accompanying text.
99. Id. at 566-571.
100. Issuance of a certificate by an AME will be reviewed by the FAA Aeromedical Certification Branch in Oklahoma City. The Philosophy and Limitations of FAA Aeromedical Standards, supra note 2, at 2. The FAA has the statutory authority to reverse that action upon such review and recall the certificate within 60 days of its issuance. 49 U.S.C. § 1355(b). But see Hamilton, Administrative Practice in Aviation Medical Proceedings, supra note 7, at 576-577.
the medical history collected and examination conducted by reference to standards furnished to the physician by the Federal Air Surgeon,102 particularly the FAA Guide for Aviation Medical Examiners,103 (Guide).

The Guide directs the AME to initially deny an aviation medical certificate to any applicant whose history or examination indicates a background or presence of one of the following nine conditions:104

1. Myocardial infarction,105
2. Angina pectoris or other evidence of coronary heart disease,106
3. Psychosis,107
4. A character or behavioral disorder manifested by repeated overt acts,108
5. Epilepsy,109
6. A disturbance of consciousness without satisfactory medical explanation,110
7. Drug addiction,111
8. Alcoholism,112 or
9. Diabetes requiring insulin or another hypoglycemic drug for control.113

Additionally, the Guide directs the AME to initially deny aviation medical certification to any applicant who is undergoing continuous treatment with antihistamine, narcotic, barbiturate, mood-amelioration, tranquilizing, motion sickness, steroid, and anti-hypertensive or ataraxic drugs.114

Furthermore, the Guide states that it is "considered advisable" for the AME to either deny or defer certification in a considerable variety of clinical conditions which may require the exercise of medical judgment.115 In such cases, the AME is directed to refer the case up through FAA channels to the Chief of the FAA Aeromedical Certification Branch in Oklahoma.
City.\textsuperscript{116} Conditions for which such denial or deferral is recommended by the Guide are almost encyclopedic in scope, extending far beyond the standards and nine specific disqualifying conditions appearing in the regulations.\textsuperscript{117}

The Guide does, however, permit the AME, in the exercise of his own best medical judgment, to issue an airman medical certificate to a person whose vision is defective in certain respects, so long as specific limitations set forth in the Guide are added to the face of the certificate.\textsuperscript{118} No similar exercise of medical judgment is encouraged with respect to any other area of physiological or psychological deficiency listed in the Guidé.

The denial or deferral of the application by the AME is not a final agency action which is ripe for review.\textsuperscript{119} Rather, the person must first formally request reconsideration of the denial by the Federal Air Surgeon.\textsuperscript{120} Failure to request reconsideration by the Federal Air Surgeon is deemed a withdrawal and abandonment of the application and precludes any subsequent appeal.\textsuperscript{121}

If an attorney has the good fortune to become involved in the case at this early stage, he can help expedite the administrative process of reconsideration by arranging for his client to undergo a complete current evaluation by a qualified medical expert or group of experts specializing in the area or areas upon which the denial or deferral was based.\textsuperscript{122} For the most

\textsuperscript{116} Id. at 39.

\textsuperscript{117} Id. at 39-48 (list of 222 additional conditions of the head, face, neck, scalp, nose, sinuses, mouth, throat, ears, eyes, lungs, chest, heart, vascular system, abdomen, viscera, anus, rectum, endocrine system, genitourinary system, upper and lower extremities, spine, musculoskeletal, skin, lymphatics, body marks, scars, tattoos, neurologic, psychiatric, general systemic, hearing, vision, blood pressure, pulse, urinanalysis, and electrocardiogram for which such denial or deferral is recommended).

\textsuperscript{118} Id. at 12.

\textsuperscript{119} Under the Federal Aviation Act of 1958, denials of certificates by the Administrator may be reviewed by the National Transportation Safety Board. 49 U.S.C. § 1422(b) (1976). However, denials of certificates by AMEs are not considered denials 'by the Administrator' under the regulations. Denials by the Federal Air Surgeon are the only denials considered final and thus subject to review.

\textsuperscript{120} 14 C.F.R. § 67.27(a) (1982). Under the recent amendments, in certain cases a denial by the Chief, Aeromedical Certification Branch, Civil Aeromedical Institute (presently Audie W. Davis, M.D., of Oklahoma City) or a Regional Flight Surgeon may be considered a final denial for appeal purposes. 14 C.F.R. § 67.27(b)(3) (1982), as amended by 47 Fed. Reg. 16,309 (1982).

\textsuperscript{121} Id. at Kovarik, supra note 7, at 34.

\textsuperscript{122} Counsel should bear in mind from the outset that in the case of a final denial by the Federal Air Surgeon, he or she will ultimately face the burden of proving to the National Transportation Safety Board, by a preponderance of reliable, probative and substantial evidence, that the client is in fact qualified under the regulations to receive an aviation medical certificate. This will ultimately turn on conflicting expert medical testimony, and the more logical, persuasive and in-depth expert testimony can be expected to prevail. In such a case, the specialized credentials of the witnesses, such as board-certification in their area of expertise, can be expected to be a factor in a Board Administrative Law Judge's determination of persuasiveness. Dodson v. National Trans-
common areas of concern, the FAA has standardized the minimum additional testing required and will provide counsel with copies of these minimum standards upon request.\textsuperscript{123} It is important at this stage to select the best-qualified physician available in the field,\textsuperscript{124} even if this initially requires some travel by and additional expense to the client. Counsel should furnish the client and evaluating physician a copy of the appropriate FAA standards (if any) for the particular evaluation and impress upon the physician selected the importance of meticulously covering every item listed therein in their evaluation and report. Many aviators have suffered denial of or delay in certification as a result of an omission of some item listed in these standards from the report submitted to the FAA.\textsuperscript{125} Counsel must insure that the physician performing this evaluation has the benefit of a full and complete medical history and that the client is totally candid with the physician.\textsuperscript{126} Counsel can help expedite the evaluation by obtaining a written authorization for release of medical records from the client and corresponding with all physicians and hospitals where the client may have previously received examination and treatment relating to the condition in question.\textsuperscript{127} Counsel should arrange for the evaluating physician to forward the original of his

\textsuperscript{123} See supra note 122. Many physicians are reluctant to testify in legal proceedings of any kind. Because the outcome of one of these cases, on appeal, may ultimately turn upon a choice between the persuasiveness of expert witnesses, it is essential that the airman’s physician be willing to testify on his behalf, and to face cross-examination on his or her testimony: In selecting a physician to perform this early evaluation, it is best to apprise the physician of this need beforehand and ascertain his or her willingness to testify on the patient’s behalf, if in the physician’s best medical judgment, the patient’s medical condition does not contraindicate flight. If the physician would be unwilling to testify, counsel should continue to search for a qualified specialist who would ultimately be willing to testify, for the Board will afford little, if any, weight to mere medical records unsupported by expert medical testimony given under oath and subjected to cross-examination. See, e.g., Petition of Blaetz, NTSB Order No. EA-964, slip op. (February 24, 1977).

\textsuperscript{125} AOPA Pilot, March, 1982, at 51 & 54.

\textsuperscript{126} See infra notes 164-168 and accompanying text.

\textsuperscript{127} It is the practice in our office to obtain an authorization for release of medical records from the client, together with a list of all physicians and hospitals where the client has previously received any examination, diagnosis or treatment relating to the condition, along with the approximate dates of such medical attention and the client’s date of birth and social security number (which are often used in indexing medical records) and to then obtain all of these records directly from the sources, arrange them in chronological order and forward them to the evaluating physician along with a cover letter and checklist for performance of the particular special evaluation deemed appropriate under the circumstances.
report, together with all supporting laboratory data, to the attorney, rather than directly to the Federal Air Surgeon. Thus, counsel can assemble the entire medical history and evaluation and insure its completeness prior to transmittal to the Federal Air Surgeon. Counsel should also take this opportunity to realistically evaluate the case and make a threshold determination as to whether it is appropriate to press the issue with the Federal Air Surgeon at this time, or whether some additional testing, change in lifestyle, or passage of time would substantially improve the client's chances of certification. If the evaluation reveals that the client's condition is one in which even such additional testing, treatment, change in lifestyle or passage of time could not render the person certifiable, the client should be so advised in the greatest possible detail at that time, to avoid raising or prolonging unwarranted hopes.

Once the attorney has marshalled the client's entire medical history and current evaluation of the problem condition and made the threshold determination that the time is ripe for filing, all of the documents in support of the request for reconsideration should be sent in a single mailing. Budgetary constraints on the FAA have resulted in a situation in which the Federal Air Surgeon's office is woefully understaffed with secretarial, clerical and administrative personnel to such an extent that unless everything

128. Such as coronary artery cineangiography or thallium 201 scintigraphy in the case of an individual denied on the basis of arteriosclerotic heart disease.
129. Such as reduction of blood pressure through a program of antihypertensive therapy.
130. For example, the person having arteriosclerotic heart disease may slow or even halt the progress of the disease and thereby substantially reduce the risk of myocardial infarction (heart attack) resulting from the disease by quitting smoking, moderating alcohol consumption, and carefully adhering to a clinically-recommended and supervised diet, rest and exercise program. The Cardiovascular Fitness of Airline Pilots, Report of a Working Party of the Cardiology Committee of the Royal College of Physicians of London, BRITISH HEART JOURNAL Volume XL, no. 4, pp. 346-368 (1978).
131. For example, in individuals who have undergone coronary artery bypass surgery, the likelihood of a bypass graft failing has proven virtually statistically insignificant if all the grafts are open and functioning properly more than six months after the surgery. Similarly, where an individual has experienced an episode of unconsciousness without a satisfactory medical explanation of the cause (see supra note 67 and accompanying text), the individual may be considered an appropriate candidate for aviation medical certification after an interval of two years has passed without further symptoms, if neurological evaluation including electroencephalogram (EEG) and computerized axial tomography (a "CAT scan") do not show any abnormalities. Daly, Bennett, Crandall, Mattson, Penny & Rasmussen, Seizure Disorders and Disturbances of Consciousness, 36 ARCHIVES OF NEUROLOGY 782, 783 (1979).
132. A client who had been accurately clinically diagnosed as epileptic on the basis of more than a single seizure or of a single seizure occurring at or after age 5 cannot expect aviation medical certification, under the present state of knowledge of that disorder. Daly, Bennett, Crandall, Mattson, Penny & Rasmussen, supra.
133. In our office, it is our practice to send this with a letter of transmittal highlighting what we believe to be the most salient points of the medical history and specialists' evaluations and to suggest factors usable of the Federal Surgeon to justify certification as being in the public interest.
relating to the particular case arrives in one package, there is a substantial
risk that documents arriving later, under separate cover, may not find their
way into the file before the ultimate decision is made (with increased result-
ing potential for an adverse decision).\textsuperscript{134}

One method of organizing the medical history and evaluations is to
place them in reverse chronological order (with the most recent evaluation
at the front and the initial onset of the condition at the rear) and to index and
bind the entire package into a volume or set of volumes, depending on the
bulk. Regardless of the method employed, anything the attorney can do to
aid the Federal Air Surgeon and his panel of consultants in organizing these
typically voluminous records into a logical, manageable data base can only
expedite administrative decision-making.\textsuperscript{135}

If the Federal Air Surgeon denies the application upon request for re-
consideration, the case becomes ripe for review.\textsuperscript{136} Although in the vast
majority of cases, an appeal must first be taken to the National Transpor-
tation Safety Board (NTSB),\textsuperscript{137} some cases may be directly appealable to the
appropriate federal court of appeals.\textsuperscript{138} In many cases, the circumstances
will make it more appropriate to file a petition for special issue (exemption)
with the FAA, rather than to pursue either of these appeal rights or to do so
simultaneously with the prosecution of an appeal.\textsuperscript{139} Occasionally, it may
even be appropriate to arrange for the client to submit to additional medical
testing and either request further reconsideration of the denial based upon
that or, if a substantial period of time has passed in the interim, to repeat
the entire application and petition for reconsideration process.\textsuperscript{140} Of

\textsuperscript{134} Interview with Edna B. Lamb, Medical & Appeals Specialist, office of the Federal Air Sur-

\textsuperscript{135} For example, at the quarterly meeting of the panel of consultants held June 3-4, 1982,
206 cases were reviewed and the consultants’ recommendations on each prepared for the Federal
Air Surgeon. Telephone interview with William H. Hark, M.D., Chief, Aeromedical Standards Divi-
sion, Federal Aviation Administration (June 8, 1982). Assuming that the panel devoted normal 8-
hour working days to that task, the average case would have received less than five minutes of the
panel’s attention. Under such circumstances, the importance of a highly-organized and cogent
medical history is obvious.

\textsuperscript{136} \textit{But see supra} note 120. The Federal Air Surgeon is not bound by the recommendations
of the panel of consultants in reaching his ultimate decision to grant or deny certification. \textit{Things
Your Air Surgeon Never Told You, Aviation Consumer,} April 1, 1982, at 14, 19.

\textsuperscript{137} Exhaustion of this administrative remedy is generally a prerequisite to judicial appeal. Mc-
Ghee v. N.T.S.B., Case No. 78-1039 (10th Cir. June 29, 1978) (order dismissing appeal). For a
discussion of this intermediate administrative appeal process, see infra notes 224-255.

\textsuperscript{138} See infra notes 149 and accompanying text.

\textsuperscript{139} The Board’s Rules of Practice allow you to file the appeal with the Board, the request that
the Board hold in abeyance any action on the Board appeal for 180 days in order to allow time for
the matter to be resolved by a simultaneous petition for exemption to the Federal Air Surgeon. 49

\textsuperscript{140} Occasionally, for example, in the borderline coronary artery disease case, the Federal Air
Surgeon will, upon the applicant’s submission of favorable coronary artery cineangiography films,
course, there will always be some cases in which further efforts would simply not be justified by any reasonable expectation of success.141

In order to determine what course of action to take next, counsel should at this point answer the following questions:

Is the denial based upon a finding of a medical history or clinical diagnosis of one of the nine specific disqualifying conditions?142

Is the finding based upon substantial evidence contained in the FAA's medical record of the individual?143

If so, can that evidence be impeached or rebutted?144

Is the validity of the regulation itself dubious?145

If the basis for the denial is one of the nine specific disqualifying conditions and there is substantial evidence in the record evidencing a medical history or clinical diagnosis of that condition, then the only route along which one can hope to find ultimate success lies through the special issue (exemption) process.146 If the basis for the denial was one of the nine specific disqualifying conditions, but the evidence upon which the Federal Air Surgeon made his finding of a medical history or clinical diagnosis of that condition is either insubstantial or subject to successful impeachment or rebuttal by superior medical evidence, an appeal to the NTSB may succeed.147 An NTSB appeal may also be successful in a case where the Federal Air Surgeon's denial was based upon some condition other than one of the nine specific disqualifying conditions and the appellant can muster qualified and convincing medical opinion to the effect that, notwithstanding the condition, the individual should be able to safely pilot an airplane.148 Only where the validity of the regulation relied upon by the Federal Air Surgeon to deny certification can be challenged is it appropriate to take the case directly to the federal courts of appeal.149

certify a person he would not otherwise have certified. Petition of McCord, NTSB Order No. EA-1149 (June 22, 1978). Additionally, cardiovascular test results which are more than six months old are considered stale and of little diagnostic value. The initial standard examination by the AME must have occurred within the time period of the duration of the class of medical certificate sought, for that exam to be current.

141. This is particularly so where your own expert medical specialists have reservations about the individual's ability to safely perform in a flight environment with his particular current medical condition and there is no reasonable expectation of improvement in that condition.

142. See supra notes 104-113 and accompanying text.

143. To answer this question, counsel should obtain and review certified copy of the FAA's entire medical records file on the individual.


145. See e.g., Jensen v. Administrator, 641 F.2d 279 (9th Cir. 1981).

146. For a description of this process, see infra notes 203-223.


149. The Board has ruled that it lacks jurisdiction to entertain attacks on the validity or reasonableness of regulations promulgated by the FAA, or on the constitutionality of such rules. See Ham-
B. DENIAL OR DEFERRAL OF RECERTIFICATION ON PERIODIC RE-EXAMINATION

Aviation medical certificates (unlike pilots' licenses) are of limited duration. Unless previously suspended or revoked, the first-class medical certificate required for airline transport pilots expires at the end of the last day of the sixth month after the month the pilot was examined by the AME. The second-class medical certificate required for the exercise of commercial pilot or air traffic control tower operation certificate privileges expires at the end of the last day of the twelfth month after the month of the AME's examination. The third-class medical certificate required for the exercise of private or student pilot privileges expires at the end of the last day of the twenty-fourth month after the AME's examination of the pilot.

Individuals wishing to continue their flying or employment as air traffic controllers without interruption must file a new application for aviation medical recertification and submit to examination by an AME on or before the date of expiration of their current medical certificate. The application form and content of the physical examination are identical for both the initial application and periodic recertification application.

As in the case of the denial or deferral of an initial application, the person who is denied a medical certificate by an AME on periodic reexamination must first formally request reconsideration of the denial by the Fed-

150. The Federal Aviation Act of 1958 provides, at 49 U.S.C. § 1429(a) (1976) provides, in part that:

The Administrator may, from time to time, re-examine any civil airman. If, as a result of any such re-examination, or if, as a result of any other investigation made by the Administrator, he determines that safety in air commerce or air transportation and the public interest requires, the Administrator may issue an order amending, modifying, suspending, or revoking, in whole or in part, any airman certificate.

151. 14 C.F.R. § 61.23(a)(1) (1982), which further provides that the certificate continues to be valid for operations requiring only commercial, private, or student pilot certificates for the normal duration of a second-class or third-class certificate, as appropriate.

152. 14 C.F.R. § 61.23(b)(1) (1982), which provides for an additional year's validity for operations requiring only a private or student pilot certificate.

153. 14 C.F.R. § 61.23(c) (1982).

154. Where there is any basis upon which to anticipate any question as to their certifiability arising on re-examination under the extremely broad guidelines contained in the Guide for Aviation Medical Examiners supra (notes 47 and 103-117 and accompanying text), counsel should recommend the individual apply for recertification well in advance of the expiration of their existing certificate, in hopes that any such questions can be resolved prior to the expiration of that certificate, so that their employment may continue uninterrupted. If, however, the condition is one of the nine specific disqualifying conditions (supra notes 104-113 and accompanying text) then the client must be counselled that this unexpired certificate is invalid and that it would be a violation of 14 C.F.R. § 61.53 (1982) to continue to act as pilot in command or in any other capacity as a required pilot flight crew member.

155. FAA Form 8500-8 (1-67).
eral Air Surgeon or waive all appeal rights.\textsuperscript{156} The attorney whose client has been denied a medical certificate on recertification or whose AME has deferred the matter for decision by the Aeromedical Certification Branch should assure that a formal written request for reconsideration is filed in a timely manner and should immediately commence work to develop the same sort of medical history and thorough current evaluations by medical specialists recommended above in the case of a denial on initial application.\textsuperscript{157}

From this point forward, the alternatives of special issue (exemption), NTSB appeal, or appeal to the federal courts of appeal are the same as in the case of an initial denial, and the election among these remedies should be based upon the same considerations.\textsuperscript{158}

Additionally, where counsel has the benefit of a continuing personal or professional relationship with a pilot or air traffic controller and has the good fortune to learn of a potential problem on recertification well in advance of expiration of the individual’s existing certificate, valuable opportunities for preventive legal counselling are presented. If the condition is one of the nine specific disqualifying conditions listed earlier,\textsuperscript{159} counsel can preclude FAA action to suspend or revoke the existing certificate\textsuperscript{160} and establish a foundation of good faith and professional responsibility which can be a helpful factor in subsequent efforts to regain the client’s medical certificate through the special issue (exemption) process.\textsuperscript{161} This can be done by arranging for the client to immediately surrender his current medical certificate for cancellation, making a full disclosure of the reasons for that voluntary surrender.\textsuperscript{162} If the intervening medical event does not fit within one of these nine specific disqualifying conditions, it is prudent to recommend that the client apply and submit to re-examination for renewal of the medical certificate as soon as possible, in hopes that any problems that may raise with obtaining the new certificate may be resolved before expiration of the existing one.\textsuperscript{163} In every event, the client must be carefully counselled to be truthful in completing the application for the certificate in order to avoid the potentially-disastrous problems described in the next paragraph.

\textsuperscript{156} See supra notes 119-121 and accompanying text.
\textsuperscript{157} See supra notes 122-135 and accompanying text.
\textsuperscript{158} See supra notes 136-149 and accompanying text.
\textsuperscript{159} See supra notes 104-113 and accompanying text.
\textsuperscript{160} See supra note 150.
\textsuperscript{161} In such a subjective decision-making process, the agency’s assessment of the individual’s attitude toward compliance with the regulations, cooperation with the bureaucracy and desire to work within the system can be crucial. Pangia, \textit{Handling FAA Enforcement Proceedings: A View from the Inside}, 46 \textit{J. Air L. \\& Com.} 573, 610-612 (1981).
\textsuperscript{162} See, e.g., letter from the author to Audie W. Davis, M.D., Chief, Aeromedical Certification Branch, Federal Aviation Administration (May 18, 1982).
\textsuperscript{163} See supra note 154.
C. **CONSEQUENCES OF MAKING A FALSE STATEMENT ON AN APPLICATION FOR AVIATION MEDICAL CERTIFICATE**

The professional aviator who gains airline employment has typically invested many years and many thousands of dollars in obtaining the requisite certificates, skills and experience. Flying, for such an individual, is typically not only a profession but also a passion. Yet, the continuation of pilots’ careers depends entirely upon their ability to successfully pass each periodic medical re-examination. Thus, the system places each airline transport pilot’s career on the line at least every six months.

Under these circumstances, the pilot may be understandably tempted to understate, omit, or even lie in response to questions on the application form when he fears a truthful answer might jeopardize his career.

While such lack of candor may be understandable, its consequences are likely to be far more catastrophic than a disqualifying truthful answer.

The Federal Criminal Code provides:

> Whoever, in any matter within the jurisdiction of any department or agency of the United States knowingly and willfully falsifies, conceals or covers up by any trick, scheme, or device a material fact, or makes any false, fictitious or fraudulent statements or representations, or makes or uses any false writing or document knowing the same to contain any false, fictitious or fraudulent statement or entry, shall be fined not more than $10,000 or imprisoned not more than 5 years, or both.\(^{164}\)

Felony convictions have been obtained under this statute for falsifications and omissions in applications for aviation medical certificates.\(^{165}\)

Additionally, the FARs provide\(^{166}\) that the making of any fraudulent or intentionally false statement on any application for a medical certificate is a basis for suspending or revoking not only that medical certificate but also any other certificates or ratings held by that person, including pilot’s licenses and ratings and even a ground instructor rating.\(^{167}\) This regulation is also strictly enforced.\(^{168}\)

Thus, it is in the client’s ultimate best interest to be absolutely truthful with the FAA in completing each periodic application for renewal of the medical certificate. While a truthful answer may precipitate denial or deferral of the application, the individual may still be recertifiable on reconsideration or by special issue (exemption).\(^{169}\) If, however, the individual gains or

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167. See, e.g., Cowell v. N.T.S.B., 612 F.2d 505 (10th Cir. 1980); Hart v. McLucas, 535 F.2d 516 (9th Cir. 1976).  
168. AVIATION, SPACE, AND ENVIRONMENTAL MEDICINE, supra note 165.  
169. For the procedures for reconsideration, see supra notes 119-135 and accompanying text. For procedures for special issue (exemption), see infra notes 209-231 and accompanying text.
attempts to gain renewal of the medical certificate by fraud, this indiscretion may ultimately result in a felony, suspension or revocation of all FAA-issued certificates and even bar them forever from recertification as an airline transport pilot.\textsuperscript{170}

Thus, the importance to the client of fully and truthfully answering all questions on each application for a medical certificate cannot be overemphasized.

\textbf{D. ERRORS AND OMISSIONS OF THE AVIATION MEDICAL EXAMINER}

Each report of an examination which has resulted in the issuance of an aviation medical certificate is reviewed by the FAA Aeromedical Certification Branch. The report is first screened by computer and any errors or omissions noted will result in the report being flagged for human review.\textsuperscript{171}

If the error or omission is discovered within sixty days after issuance of the certificate, the Federal Air Surgeon may reverse the AME's decision to issue the certificate and write the airman requesting its return.\textsuperscript{172} However, as a result of the agency's clerical understaffing problem\textsuperscript{173} it is increasingly rare for such errors and omissions to be discovered in the higher echelons of the FAA within sixty days after issuance of the certificate by the AME.

If more than sixty days have expired before the error or omission is discovered, the FAA must initiate administrative action to suspend or revoke the certificate unless the airman is willing to voluntarily surrender the certificate.\textsuperscript{174} Counsel representing a client who has been requested to surrender a certificate under these circumstances should closely examine the medical reason for the request. If the AME has erred in issuing the aviator a medical certificate despite a medical history or clinical diagnosis of one of the nine specific disqualifying conditions listed above,\textsuperscript{175} immediate voluntary surrender is appropriate. Such action will establish a foundation

\textsuperscript{170} Ordinary, an airman whose certificate has been revoked must wait one year before reapplying for certification, and if then qualified should be recertified. 49 U.S.C. § 1422(b) (1976). Administrator v. Wronke, N.T.S.B. Order No. EA-1211 (Nov. 16, 1978). One qualification unique to the airline transport pilot certificate, however, is that the individual must be of good moral character. Conviction of such a felony might well be considered by the FAA and NTSB as demonstrative of a lack of good moral character which could be perpetually disqualifying, at least absent some showing that the individual has rehabilitated himself in this regard. See, e.g., Administrator v. Doppes, 2 N.T.S.B. 2306 (1976) and Administrator v. Roe, 45 C.A.B. 969 (1966).

\textsuperscript{171} The Philosophy and Limitations of FAA Aeromedical Standards, supra note 2 at 2.


\textsuperscript{173} See supra note 134 and accompanying text.

\textsuperscript{174} For the procedure governing suspension or revocation of existing certificates, see infra notes 196-202 and 224-270 and accompanying text.

\textsuperscript{175} See supra notes 104-113 and accompanying text.
of good faith and professional responsibility which can be a helpful factor in subsequent efforts to regain the aviator’s medical certificate through the exemption process.\textsuperscript{176} If, however, the basis for the request for voluntary surrender is something other than one of the nine specific disqualifying conditions, it may be appropriate to decline voluntary surrender and force the FAA to issue an order of suspension or revocation against the certificate in order to set the appeal process in motion.\textsuperscript{177}

One of the greatest concerns to the FAA is a situation in which an AME who may be a lifelong friend of the aviator might, out of misguided sympathy for the aviator, deliberately fail to report a disqualifying disability which is observed in the course of the examination. It is the avowed policy of the FAA to forward all such cases to the Department of Justice for criminal prosecution under the felony false statement provisions cited above.\textsuperscript{178}

E. \textbf{EFFECTS OF INTERVENING MEDICAL EVENTS UPON EXISTING AND OTHERWISE VALID MEDICAL CERTIFICATES}

The Federal Aviation Regulations provide that “No person may act as pilot-in-command, or in any other capacity as a required pilot flight crewmember while he has a known medical deficiency, or increase of a known medical deficiency, that would make him unable to meet the requirements for his current medical certificate.”\textsuperscript{179}

Similarly, those same regulations provide that “No person may serve as a flight engineer or flight navigator during a period of known physical deficiency, or increase in physical deficiency, that would make him unable to meet the physical requirements for his current medical certificate.”\textsuperscript{180}

Similar language governing air traffic controllers provides:
An air traffic control tower operator may not perform duties under his certificate during any period of known physical deficiency that would make him unable to meet the physical requirements for his current medical certificate. However, if the deficiency is temporary, he may perform duties that are not affected by it whenever another certificated and qualified operator is present and on duty.\textsuperscript{181}

Thus, when counsel is presented with a client who is in possession of an aviation medical certificate which has neither expired nor been suspended or revoked, but who has experienced some medical event since the issuance of the certificate which throws its validity\textsuperscript{182} into doubt, coun-

\textsuperscript{176} See supra note 161 and accompanying text.
\textsuperscript{177} See infra notes 232-255 and accompanying text.
\textsuperscript{178} Supra notes 165 and accompanying text. Guide for Aviation Medical Examiners, note 47, supra, at 2.
\textsuperscript{179} 14 C.F.R. § 61.53 (1982).
\textsuperscript{180} 14 C.F.R. § 63.19 (1982).
\textsuperscript{181} 14 C.F.R. § 65.49(d) (1982).
\textsuperscript{182} 14 C.F.R. § 61.53 (1982).
sel should obtain the detailed medical history of the condition from the examining and treating physicians and hospitals and compare it to the physical standards for issuance of the particular class of certificate involved.\textsuperscript{183} If the new condition would disqualify the individual from being issued a medical certificate under those standards, and especially if one of the nine specific disqualifying conditions\textsuperscript{184} is involved, then the aviator should be counselled that it would be a violation of one of the above-quoted regulations if the individual were to continue to exercise the privileges of the certificate. As in any other FAR violation case, this would expose the individual to administrative prosecution which could include suspension or revocation of any and all FAA-issued certificates held by the person or substantial fines.\textsuperscript{185}

When the condition is clearly disqualifying, voluntarily surrendering the client’s current medical certificate for cancellation can establish the foundation of good faith and professional responsibility which can be a helpful factor in subsequent efforts to regain the client’s medical certificate through the special issue (exemption) process.\textsuperscript{186}

However, when the intervening medical condition is not one which disqualifies the aviator from receiving a new medical certificate, then the individual’s present medical certificate remains effective. Thus, it will not be a violation of any of the above-quoted regulations for them to continue to exercise its privileges. However, it may be prudent to recommend in such a case that the client apply and submit to re-examination for renewal of the medical certificate as early as six months prior to the scheduled date of expiration of the existing certificate, in hopes that any problems which may arise out of the intervening condition on application for recertification may be resolved before expiration of the existing certificate. Once again, the importance of full and truthful disclosures on that application should be firmly stressed.\textsuperscript{187}

\section{F. Duty to Provide Additional Medical Information or History to FAA Upon Request}

The regulations permit the FAA to request that an applicant for an aviation medical certificate or the holder of an existing aviation medical certificate furnish to the FAA any additional medical information deemed necessary to determine whether the individual meets the medical standards for that certificate or to release to the FAA any available information or

\textsuperscript{183} See \textit{supra} notes 34-76 and accompanying text.
\textsuperscript{184} See \textit{supra} notes 104-113 and accompanying text.
\textsuperscript{185} See generally authorities cited in note 7, \textit{supra}.
\textsuperscript{186} See \textit{supra} notes 159-162 and accompanying text.
\textsuperscript{187} See \textit{supra} notes 165-170 and accompanying text.
records concerning that history. The regulations go on to provide that:

If the applicant, or holder, refuses to provide the requested medical information or history or to authorize the release so requested, the Secretary may suspend, modify, or revoke any medical certificate that he holds or may, in the case of an applicant, refuse to issue a medical certificate to him.

This regulation was adopted pursuant to the statutory authority to re-examine airmen contained in the Federal Aviation Act of 1958, as amended. While it is by no means clear either from the language of this enabling Act or from the language of the regulation itself, the FAA has taken the position that these sources of power also permit them to require that holders of aviation medical certificates or applicants for aviation medical certificates submit to additional testing by medical specialists in the private sector, at the individual’s own expense, upon request by the FAA.

The NTSB, which has initial administrative appellate jurisdiction over FAA orders denying, suspending or revoking medical or other certificates, has consistently held that any such request by the Administrator must be reasonable and that, in an enforcement action under this section of the regulations, the burden of proof rests with the FAA to prove that the history, information or testing requested was reasonable and neither arbitrary nor capricious. The NTSB has also held that if the airman makes the additional medical information requested available to the FAA at any time during the pendency of the appeal of an enforcement action for such a violation, the proceeding becomes moot and the order of suspension or revocation will be dismissed.

G. SUSPENSION OR REVOCATION OF AVIATION MEDICAL CERTIFICATES

Whenever, as a result of such a re-examination or other investigation, the FAA determines that the holder of an aviation medical certificate is not qualified to hold that certificate, they may issue an order suspending or revoking that certificate. Such orders are appealable to the NTSB and the completion of this NTSB appeal process is ordinarily a prerequisite to judicial appeal. Skipping the NTSB appeal process and taking the case

188. 14 C.F.R. § 67.31 (1982).
190. See supra note 150.
193. See infra notes 226 and accompanying text.
194. Petition of Wyche, 2 N.T.S.B. 325, 326 note 4 and accompanying text (1973), and cases and authorities cited therein.
196. See supra notes 150.
197. See supra notes 131 and infra 233-278.
directly to the appropriate federal court of appeal is appropriate only where the validity of the regulation which forms the basis for the action is challenged.\(^{198}\)

Appeal should not, however, be reflexive. If it is apparent ab initio that the individual does have a medical history or clinical diagnosis of one of the nine specific disqualifying conditions and that this history or diagnosis is not vulnerable to impeachment or rebuttal by superior medical evidence, surrender of the certificate should be evaluated as an alternative to appeal. In the absence of aggravating circumstances, FAA counsel will often agree to withdraw the order of suspension or revocation in exchange for a voluntary surrender of the certificate for cancellation (rather than suspension or revocation) and a stipulation that the individual will not re-apply to an AME for recertification without notice to the FAA attorney on the case and full disclosure of the underlying medical history.\(^{199}\) If the suspension or revocation is based upon the individual's failure or refusal to provide some additional medical information requested by the FAA, promptly providing that information may moot the case, resulting in the withdrawal of the order by the FAA or dismissal of their complaint early in the process of NTSB appeal.\(^{200}\)

If, however, appeal to the NTSB appears justified by the facts and circumstances of the particular case, then a notice of appeal must be filed with the Board within twenty days after the airman's receipt of the order of suspension or revocation.\(^{201}\) Procedures for pursuing review from this point are discussed below.\(^{202}\)

H. THE "AGE SIXTY RULE"

Although age does not disqualify anyone from obtaining any class of aviation medical certificate, the FARs' "Age Sixty Rule"\(^{203}\) prohibits persons over that age from piloting airliners and air freighters.\(^{204}\) Although this rule has thus far been judicially upheld as valid,\(^{205}\) advancing medical knowledge in the field of gerontology suggests that future litigation on this point may yield a different result.\(^{206}\) Indeed, as justification for the rule wanes, hope must rise that the day will come when the FAA will respond

\(^{198}\) See supra note 149.


\(^{200}\) See supra note 195.

\(^{201}\) 49 C.F.R. § 82.30(a) (1981).

\(^{202}\) See infra notes 233-278.

\(^{203}\) 14 C.F.R. § 121.383(c) (1982).

\(^{204}\) See supra notes 24-26.

\(^{205}\) See supra note 85.

\(^{206}\) See supra note 86; Mohler, *Aircraft Accidents by Older Persons*, AEROSPACE MEDICINE May, 1969, at 554.
favorably to a petition for rulemaking\textsuperscript{207} to delete this rule without the need for a judicial determination of invalidity.

Additionally, counsel should be aware that even as the law presently stands, the rule does not necessarily spell the end of the aviator's career. The rule only prohibits these individuals from serving as pilots, and some airlines have permitted these individuals to continue to work after age sixty in the role of flight engineers.\textsuperscript{208}

IV. **THE SPECIAL ISSUE (EXEMPTION) PROCESS**

A pilot can receive aviation medical certification from the FAA despite a medical history or clinical diagnosis of one of the nine specific disqualifying conditions listed above,\textsuperscript{209} through the discretionary special issue (formerly called "exemption") process.

The FAA's enabling legislation, the Federal Aviation Act of 1958, as amended, provides that: "The Secretary from time to time may grant exemptions from the requirements of any rule or regulation prescribed under this title if he finds that such action would be in the public interest."\textsuperscript{210}

The "public interest" proviso of this regulation was the focus of a recent court decision\textsuperscript{211} which has resulted in major delays in the already painfully slow process of resolving petitions for exemption.\textsuperscript{212} Prior to the decision in \textit{Delta Airlines v. United States}, the Federal Air Surgeon had routinely issued exemptions and denials of exemption on single page form letters in which the name of the individual and regulation waived (or refused to be waived) were filled in.\textsuperscript{213} The form letter for the grant of exemption simply contained a statement that the Federal Air Surgeon found the exemption to be in the public interest, while the form letter for denial simply contained a statement that he found that granting of the petition would not be in the public interest.

\textsuperscript{207} 14 C.F.R. § 11.25(a) provides in part, that:
Any interested person may petition the Administrator to issue, amend, or repeal a rule.

The FAA has issued an advance notice of proposed rulemaking to solicit comments relating to the "Age 60 Rule." 47 Fed. Reg. 29782 (1982).

\textsuperscript{208} Morgan, \textit{The Young and the Restless}, \textit{Flying}, April 1982, at 112, 113.

\textsuperscript{209} See supra notes 104-113 and accompanying text.

\textsuperscript{210} 49 U.S.C. § 1421(c) (1976).


\textsuperscript{212} As a direct result of this decision, the number of exemptions granted in 1980 decreased to 205, compared to 316 granted in 1979. Federal Aviation Administration, U.S. Dep't. Transp., Aeromedical Certification Statistical Handbook 25 (1981). The process was already averaging 4-8 months from petition to decision. \textit{Things Your Air Surgeon Never Told You}, \textit{Aviation Consumer}, April 1, 1982, at 14, 20. There is presently a backlog of approximately 700 petitions awaiting decision. Telephone interview with William H. Hark, M.D., Chief, Aeromedical Standards Division, Federal Aviation Administration (June 8, 1982).

\textsuperscript{213} See e.g., Bosso v. Helms, No. 81-1311 (10th Cir. March 24, 1982) (Denial of Exemption, Exhibit A to Petition for Review).
interest.\textsuperscript{214}

In neither case would the Federal Air Surgeon divulge any factual basis or findings of fact to support the grant or denial of the exemption. An effort to persuade the Federal Air Surgeon to make a practice of including such disclosures in the decision letters was rejected as it was feared that it would create an intolerable bureaucratic workload.\textsuperscript{215} Where efforts at reasoned persuasion had failed, however, litigation prevailed, for the Court in Delta enjoined the FAA, its Administrator, and the Federal Air Surgeon from issuing any medical certificates by the exemption that is considered to be in the public interest.\textsuperscript{216} An excerpt from the decision on that point merits reproduction here:

By the plain wording of the regulation, the Administrator can grant exemptions to airmen possessing any of the absolutely disqualifying conditions, and this court so holds. However, the court further holds that any exemption granted must be done with strict adherence to the FAA's own regulation that the exemption be "in the public interest." This requirement assures that the objec-


\textsuperscript{215} Correspondence between the author and H.L. Reighard, M.D., Federal Air Surgeon, Federal Aviation Administration.

\textsuperscript{216} See supra notes 211. The FAA recently amended its medical certification rules in response to this and the Jensen decision (supra note 59 and infra notes 225-226 and accompanying text). Ironically, the effective date of the amended regulation was two years to the day from the date of the District Judge's order in the Delta case. 47 Fed. Reg. 16,308 (1982) (to be codified in 14 C.F.R. §§ 67.13-27). The essence of the changes to the procedural rules there appears to be no more than a re-naming of the process from "exemption" to "special issue," and appears to be a rather blatant and transparent effort to avoid the effect of the Delta and Jensen decisions by enshrining in the regulation the unbridled discretion previously enjoyed by the Federal Air Surgeon, but under a different name. In its summary of the new rule, the FAA states that the practice of granting relief through the exemption procedures will be discontinued in favor of the new "discretionary special issuance" procedures: 47 Fed. Reg. 16,298 (1982). The purpose of this is ostensibly to avoid the "complex administrative procedure...involved in processing a formal petition for exemption from the medical standards of the Federal Aviation Regulations." Id. at 16,299. Motivation aside, the rule change appears of dubious legality. While the authority to grant exemptions appears clearly in the agency's enabling act (see supra note 210 and accompanying text), authority to accomplish the same purpose through a more informal, simple and discretionary process under a different guise ("special issuance") does not clearly appear in the agency's enabling act. The most that can be surmised from the amendment (id. at 16,309) is that the agency believes this power is included in the vague general grant at 49 U.S.C. § 1354(a) (196), which provides that:

The Secretary of Transportation is empowered to perform such acts, to conduct such investigations, to issue and amend such orders, and to make and amend such general or special rules, regulations, and procedures, pursuant to and consistent with the provisions of this Act, as he shall deem necessary to carry out the provisions of, and to exercise and perform his powers and duties under, this Act.

That appears to be grasping at semantic straws. Because of this uncertainty (which will hopefully be resolved in the pending action of Schwartz v. Helms, supra note 72) I will, throughout this paper, use the phrase "special issue (exemption)" to describe this process as it has existed since May 17, 1982, and simply "exemption" to describe the same process prior to that date.
tive of the Act and the Regulations (to promote air safety) will not be defeated and further assures that the Regulations themselves will not be rendered meaningless by virtue of constant and pro forma exemptions. See Utah Agencies v. CAB, 504 F.2d 1232 (10th Cir. 1974), and Island Airlines, Inc. v. CAB, 363 F.2d 120 (9th Cir. 1966), wherein the courts noted that exemptions should be used sparingly and only in very limited and unusual circumstances. This court finds that the defendants have been improperly granting exemptions in two very significant ways: (1) the grants of exemption routinely recite that they are "in the public interest" with no supporting facts whatsoever for that determination and (2) the Federal Air Surgeon has totally misconceived what is meant by the "public interest."

It is basic to judicial review of administrative action that the agency "must find what the statute [or regulation] requires it to find, not in conclusory fashion in the statutory language but in such fashion that a reviewing court can test the validity of the finding." American Airlines, Inc. v. CAB, 235 F.2d 845, 853 (D.C. Cir. 1956). "The necessity for administrative agencies to provide a statement of reasons, especially in cases ... where the public interest demands close scrutiny of an agency action, is a fundamental principle of administrative law." Brooks v. Atomic Energy Commission, 476 F.2d 924, 926-27 (D.C. Cir. 1973). See also SEC v. Chenery Corp., 332 U.S. 194 (1947). Mere recitation that a grant of exemption is in the public interest gives the court no basis by which to judge the FAA's action and falls far short of the requirement of Chenery that the basis for an agency's decision must be set forth with such clarity that the court is not left to speculate as to the theory, rationale, or facts underlying the agency's determination. For the FAA to grant an exemption to the medical standards promulgated in the Regulations it must specify why such exemption is in the public interest. 217

A. THE PETITION FOR SPECIAL ISSUE (EXEMPTION)

Counsel representing airmen seeking aviation medical certification through the special issue (exemption) process should marshal medical history and opinion to substantiate the proposition that the client, notwithstanding a history of one of the nine specific disqualifying conditions, does not pose an unacceptable risk to flying safety. 218 The petition for special issue (exemption)219 should also furnish the Federal Air Surgeon with persuasive language suitable for incorporation into a grant for exemption showing why it is in the public interest to grant a special issuance (exemption) to the


218. For example, a third-class airman medical certificate was issued under the new special issuance procedures to an individual who had a history of myocardial infarction and other evidence of coronary artery disease which required triple-vessel coronary artery bypass surgery. The surgery was successful and effectively bypassed all of the diseased areas, providing adequate blood circulation within the heart muscle, rendering it no more likely that the individual would suffer another heart attack than would the average man of his age (fifty-seven) not having his medical history. Letter from H.L. Reighard, M.D., Federal Air Surgeon, to James F. Glenn (June 28, 1982).

particular individual under the facts and circumstances of the case.\textsuperscript{220}

The documented medical history should be as thorough, detailed, and organized as possible,\textsuperscript{221} and ideally should accompany the petition in a single package to minimize the clerical workload on the Federal Air Surgeon's office and the concomitant risk of some portion of the supporting documentation simply not getting into the file.\textsuperscript{222}

\textbf{B. The Decision Process}

At this point, all similarity to the familiar adversary "due process" method of decision-making abruptly ends. When the petition and supporting medical information are received in the Federal Air Surgeon's office, the file is referred to a panel of consulting physicians for review and recommendation. While these consultants are said to be specialists who have a high degree of personal interest in the medical aspects of aviation safety,\textsuperscript{223} the agency will not divulge their identity, nor will it allow the petitioner to be present during the panel's deliberations or to have any type of hearing.\textsuperscript{224}

\textsuperscript{220} In the interim between the Delta decision and the recent rule amendment, the Federal Air Surgeon was going to considerable effort to provide in each grant of an exemption a detailed recitation of the supporting facts and policy considerations upon which he had relied to find the particular grant of exemption to be in the public interest. See, e.g., Petition of Brannon, FAA Exemption No. M-14460, Regulatory Docket No. 21529, Grant of Exemption (April 7, 1981). During that same time, however, the Federal Air Surgeon failed to make findings of fact relied upon in denying exemptions as being not in the public interest, continuing instead to utilize an uninformative form denial, but appending thereto a so-called "Working Paper/ Specialists' Recommendation," an unsigned document purporting to be an extract of the medical information reviewed by the Federal Air Surgeon's anonymous consultants and their recommendation to him. This procedure is challenged in several cases now pending in the United States Court of Appeals, See, e.g., Smith v. Helms, No. 82-1629 (D.C. Cir. filed June 7, 1982); Holmes v. Helms, No. 81-7578 (9th Cir. filed September 4, 1981); and Lenhardt v. Helms, No. 81-7740 (9th Cir. filed October 29, 1981). After adopting the recent rule change cosmetically renaming the procedure from "exemption" to "special issuance," the Federal Air Surgeon abandoned his short-lived efforts to recite in grants of medical certificates through this process the factual basis and rationale for arriving at the decision to issue the certificate and has ceased making any findings of or reference to the issuance being "in the public interest." See, e.g., letter from H.R. Reighard, M.D., Federal Air Surgeon to James P. Glenn (June 28, 1982); letter from Dr. Reighard to Robert P. Shallenberger (June 15, 1982).

\textsuperscript{221} See supra notes 122-135.

\textsuperscript{222} See supra notes 133 and 134.

\textsuperscript{223} Representing the Medically Disqualified Pilot, address by Mark T. McDermott, Law of Aviation Symposium hosted by the FAA Office of Chief Counsel in Washington, D.C. (December 1, 1981) (an outline of this speech was published in the Syllabus of the Symposium). Recent efforts by the author and physicians working with our law firm to gain entry to panel deliberations for an aviator's treating physician have been ignored by the agency. See, e.g., letter from Richard D. Spangler, M.D. to H.L. Reighard, M.D., Federal Air Surgeon (May 18, 1982).
C. JUDICIAL REVIEW

Although one court has held that this exemption procedure does not comport with the requisites of due process, the Federal Air Surgeon has made no substantive change in the exemption process as a result of that decision. The decision charts a clear course for future judicial challenges to the legality of this secret decision process, and thus, a portion of the court’s opinion merits reproduction here:

The FAA apparently now concedes that the Alcoholism Act applies to the disqualifying regulations. But it contends that although an applicant with a history of alcoholism is automatically disqualified from obtaining a medical certificate, he can apply for an exemption from the rule under the "two-tiered" system. The FAA administrator may grant an exemption from any FAA rule or regulation if he decides that to do so would be "in the public interest," and would not adversely affect safety." 14 C.F.R. § 11.27(e) (1980). The FAA argues that this procedure negates the contention that the Administrator denies certificates solely on grounds of prior alcoholism. This argument is without merit. First, the decision to deny Jensen’s application for an exemption is not before this court because Jensen did not appeal. Second, even if we were in a position to consider the "second tier" exemption procedure as a limitation on the "first-tier" certification process this would not cure the direct conflict between the "first-tier" and the Alcoholism Act.

Third, even if this court accepted the FAA’s "two-tier" argument, the exemption procedures do not comport with due process. The FAA need not grant an

226. Minor cosmetic changes made since and attributed to the Delta decisions are described and discussed in notes 211-220, supra. These recent amendments did, however, contain a substantive change in the standards for disqualification on the basis of alcoholism. The regulatory standard governing alcoholism was itself amended as part of those changes. Whereas previously any history or diagnosis of alcoholism was one of nine specific disqualifying conditions, the amendment makes alcoholism disqualifying only in the absence of established clinical evidence of recovery, including sustained total abstinence from alcohol for not less than the preceding two years. 47 Fed. Reg. 16,308 (1982) (to be codified at 14 C.F.R. §§ 67.13(d)(1)(i)(c), 67.15(d)(1)(i)(9c) and 67.17(d)(1)(i)(c)). The summary and background to those changes further indicate that the Federal Air Surgeon will consider granting a medical certificate by special issuance (exemption) within an even shorter period, and enumerates the factors which he will consider in evaluating such petitions. These include:

1. The period of the applicant’s abstinence from alcohol;
2. The severity of the problem and how long it has existed;
3. The number of times treatment was sought and relapse occurred;
4. The quality of the final treatment effort;
5. The presence of residual medical complications, especially neurologic manifestations;
6. Progress in marital, social, vocational and educational areas, as appropriate, since rehabilitation began;
7. Commitment to rehabilitation by virtue of continuing contacts with social or professional agencies, or both, and their opinions and recommendations;
8. Any underlying personality difficulties that would either be disqualifying independently or adversely affect sustained abstinence; and
9. The findings of a recent psychiatric and psychologic evaluation.

applicant a hearing before passing on the application, see Coppenbarger v. FAA, 558 F.2d 836 (7th Cir. 1977) and the decisions are reviewable under the arbitrary and capricious standard, see Keating v. FAA, 610 F.2d 611 (9th Cir. 1979).

Due process requires that for a meaningful review of an agency decision, the agency must have articulated standards governing its determinations. See Matlovich v. Secretary of the Air Force, 591 F.2d 852, 857 n.11 (D.C. Cir. 1978).

Here, the FAA's only standards for an exemption are that it would be "in the public interest" and "would not adversely affect safety." These standards do not give the court a sufficient basis for review. Neither do they give the applicant any basis for "planning his course of action (including the seeking of judicial review)." Id. at 857.

In the absence of articulated guidelines, the FAA's statements about Jensen's one year period of abstinence being insufficient to demonstrate a "cure" do not foreclose the ability of the FAA to apply standards other than a period of abstinence. See Id.; White v. Roughton, 530 F.2d 750, 753-54 (7th Cir. 1976). In Graham v. National Transportation Safety Board, 530 F.2d 317 (8th Cir. 1976), the Federal Air Surgeon approved Graham's second-class certificate because he had demonstrated a sufficient period of abstinence by remaining sober for six months. Here, Jensen's one year period of abstinence was considered insufficient. This indicates that the FAA probably considers factors other than the period of remission in the exemption determination.

We hold that the disqualifying regulations are invalid.227

The court now has before it at least three cases which present the opportunity to incorporate what was dicta in Jensen into res judicata.228

If the petition for special issue (exemption) is denied, the denial is subject to judicial review in the appropriate federal court of appeals,229 but the standard of review is the arbitrary and capricious abuse of discretion standard.230

A question now before the federal courts is whether the Federal Air Surgeon is required to set forth in a denial of a petition for special issue (exemption) the same qualitative and quantitative basis for that decision as is necessary to allow the reviewing court to test the validity of an issuance under Delta.231


228. Smith, Holmes, and Lenhardt. Smith v. Helms, No. 82-1629 (D.C. Cir. filed June 7, 1982); Holmes v. Helms, No. 81-7578 (9th Cir. filed September 4, 1981); and Lenhardt v. Helms, No. 81-7740 (9th Cir. filed October 29, 1981).

229. Coppenbarger v. FAA, 558 F.2d 836 (7th Cir. 1977).

230. Keating v. FAA, 610 F.2d 611 (9th Cir. 1979).

231. Smith, Holmes, and Lenhardt. Smith v. Helms, No. 82-1629 (D.C. Cir. filed June 7, 1982); Holmes v. Helms, No. 81-7578 (9th Cir. filed September 4, 1981); and Lenhardt v. Helms, No. 81-7740 (9th Cir. filed October 29, 1981).
V. THE NTSB APPEAL PROCESS

The aviator who has been either denied an aviation medical certificate on reconsideration by the Federal Air Surgeon or who has received an order of suspension or revocation of such a certificate may appeal that decision to the NTSB. The procedure in such an appeal varies according to whether the case originated as a denial (commonly called a "Section 602" case) or a suspension or revocation (commonly referred to as a "Section 609" case) and, if the latter, whether the FAA has also invoked its emergency powers in connection with the order.

A. ADMINISTRATIVE LAW JUDGE HEARING

In every such case, a hearing will first be held before an administrative

232. See supra notes 120-135 and accompanying text.
233. See supra notes 196-201 and accompanying text.
234. The National Transportation Safety Board (NTSB) was established by the Department of Transportation Act of 1967, Pub. L. No. 89-670, 80 Stat. 931 (codified at 49 U.S.C. § 1651, et seq.) as an agency within the U.S. Department of Transportation. The Board became an independent agency on April 1, 1975, as a result of the Independent Safety Board Act of 1974, Pub. L. No. 93-633, 88 Stat. 2166 (codified at 49 U.S.C. § 1901). The Board has two basic functions: first, it investigates accidents in aviation and other forms of public mass transportation and determines the probable cause thereof; and, second, it serves as an administrative appellate review board which is the first level of review of actions by the FAA and Coast Guard revoking, suspending, or denying certificates. The Board’s qualifications and procedures have been the subject of considerable controversy. See, e.g., Steenlik, Reforming Aviation’s Supreme Court, AIRLINE PILOT, April 1982, at 6.
236. Id. (codified at 49 U.S.C. § 1429 (1976)).
237. U.S.C. § 1485(a) (1976) provides, in part that:

   Whenever the Secretary of Transportation is of the opinion that an emergency requiring immediate action exists in respect of safety in air commerce, the Secretary of Transportation authorized, either upon complaint or his own initiative without complaint, at once, if he so orders, without answer or other form of pleading by the interested person or persons, and with or without notice, hearing, or making or filing of a report, to make such just and reasonable orders, rules, or regulations as may be essential in the interest of safety in air commerce to meet such emergency: Provided further, That the Secretary of Transportation shall immediately initiate proceedings relating to the matters embraced in any such order, rule, or regulation, and shall, insofar as practicable, give preference to such proceedings over all others under this Act.

The Board has characterized this as "extraordinary authority" which "it would be irresponsible for the Administrator to invoke . . . unless grounded only through investigations." Administrator v. Air East, Inc., 2 N.T.S.B. 870, 881 (1974). The agency’s election to invoke the emergency power makes the suspension or revocation ordered effective immediately, prior to a due process hearing on the merits (which must then follow in expeditious manner). See infra note 249 and accompanying text. The agency’s decision to invoke the extraordinary emergency power is subject to judicial review (see generally infra notes 264-278 and accompanying text). The standard for review of such emergency determinations, however, is whether the Administrator’s finding of an emergency was arbitrary and capricious, an abuse of discretion, or otherwise not in accordance with law. Nevada Airlines, Inc. v. Bond, 622 F.2d 1017 (9th Cir. 1980) and Air East, Inc. v. N.T.S.B., 512 F.2d 1227 (3d Cir. 1975), cert. denied, 423 U.S. 863 (1975).
law judge of the NTSB.\textsuperscript{238} The Federal Rules of Civil Procedure do not apply to these cases\textsuperscript{239} and the Board's Rule of Practice in Air Safety Proceedings (Rules of Practice)\textsuperscript{240} make little provision for discovery. Since the Board has stated a policy of encouraging pre-hearing discovery (including both formal and informal discovery),\textsuperscript{241} one wonders why the Board has failed and refused\textsuperscript{242} to provide by rule for customary civil discovery in these actions, independent from case-by-case exercise of judicial and prosecutorial discretion (especially considering that the FAA maintains the power throughout the action to discover the individual's medical records under the provisions of FAR § 67.31.\textsuperscript{243} A pre-hearing conference\textsuperscript{244} can be useful to narrow the issues for hearing and to resolve controversies over the scope of discovery.

The NTSB administrative law judge will schedule a hearing at a time and place convenient to the aviator.\textsuperscript{245} Where out-of-town medical specialists are involved, counsel may find it more economical and practical to request that an additional hearing or hearings be scheduled in a location or locations convenient to such witness or witnesses.\textsuperscript{246}

The hearing before the administrative law judge is in the nature of a trial de novo. In a "Section 602" case, the burden of proof is on the aviator to establish as an affirmative fact that he is qualified under the appropriate medical standards to hold the class of aviation medical certificate which has been denied him on reconsideration by the Federal Air Surgeon.\textsuperscript{247} In a "Section 609" case, however, the burden of proof rests with the FAA to prove that the individual is not qualified to hold the class of aviation medical certificate which is the subject of the order of suspension or revocation.\textsuperscript{248} In a "Section 609" case, the filing and pendency of the appeal stay the effectiveness of the order of suspension or revocation, unless the FAA has invoked its emergency authority in the issuance of that order.\textsuperscript{249}

\textsuperscript{238} At this writing, the Board has three offices of administrative law judges. These are located in Washington, D.C.; Denver, Colorado; and Los Angeles, California. Judges from these offices "ride circuit," traveling extensively to conduct these hearings at locations convenient to those involved. See infra notes 245 and 246 and accompanying text.

\textsuperscript{239} Administrator v. Cockes, 1756, 1758--59 (1975).

\textsuperscript{240} 49 C.F.R. §§ 821.1--63 (1981).

\textsuperscript{241} Administrator v. McClain, 1 N.T.S.B. 1542 (1972).

\textsuperscript{242} Petition of Hamilton, N.T.S.B. Order No. EA-1615 (June 4, 1981).

\textsuperscript{243} See supra note 188 and accompanying text.

\textsuperscript{244} 49 C.F.R. § 821.35(b)(8) (1981).

\textsuperscript{245} 49 C.F.R. § 821.37(a) (1981).

\textsuperscript{246} 49 C.F.R. § 821.37(b) (1981).

\textsuperscript{247} 49 C.F.R. § 821.25 (1981).

\textsuperscript{248} 49 C.F.R. § 821.32 (1981). In either event, the burden of proof is one of a preponderance of reliable, probative, and substantial evidence. 49 C.F.R. § 821.49(a) (1981).

\textsuperscript{249} The Federal Aviation Act of 1958, as amended, provides, in part, at 49 U.S.C. § 1429(a) (1976):
These hearings typically revolve around a contest between expert witnesses for both sides and are ultimately decided by balancing the weight of conflicting expert medical opinions. Generally, the FAA’s expert will not have examined the individual, but only the documented medical history, and the testimony of the airman’s attending physician may be entitled to some additional weight (especially where the latter physician’s testimony elucidates an incomplete documentary history). Greater weight is given to the testimony of an expert medical witness who testifies at the hearing, subject to cross-examination, than to written reports. All other factors being equal, the testimony of a medical expert who is Board-certified in the area of medical specialty at issue may be afforded greater weight than that of a similar witness not so certified.

In the vast majority of cases, the administrative law judge will render an initial decision orally at the close of the hearings. In unusually complicated cases, however, a ruling may be reserved until a later date and appear only as a written decision. This initial decision must contain findings of fact and conclusions of law, including the grounds therefor, and address issues of the credibility of witnesses and exercises of discretion presented by the case.

B. FULL BOARD REVIEW

The rendering of this initial decision still does not constitute “final agency action” subject to judicial review. Rather, appeal from this decision must next go to the full NTSB (the five political appointees actually constituting the Board). This appeal must be commenced by giving notice of appeal within ten days after an initial oral decision has been rendered or, if no oral initial decision was delivered, after a written decision or order has been served. Timely filing of this notice of appeal continues to stay the effectiveness of the Secretary of Transportation’s order unless the Secretary of Transportation advises the Board that an emergency exists and safety in air commerce or air transportation requires the immediate effectiveness of his order, in which event the order shall remain effective and the Board shall finally dispose of the appeal within sixty days after being so advised by the Secretary of Transportation.

252. Petition of Spivey, N.T.S.B. Order No. EA-1440 (August 6, 1980).
254. Id., except in cases where the Administrator has exercised his emergency authority, in which case the administrative law judge is required to render his initial decision orally on the record at the termination of the hearing. 49 C.F.R. § 821.56(b) (1981).
255. 49 C.F.R. § 821.42(b) (1981).
256. Because of the general requirement for exhaustion of administrative remedies.
the government's order of suspension or revocation in a "Section 609" case, unless the order was issued under the emergency power.260

The issues on appeal to the full Board are narrow,261 and the appeal is typically decided by the Board solely on the basis of the record and written appeal briefs, although the Board has the authority to grant oral argument where it is deemed necessary.262 The decision of the full Board is always rendered only in writing as an "Opinion and Order," which is typically quite detailed in its findings of fact, conclusions of law, and supporting rationale.263

C. JUDICIAL REVIEW

The issuance of this decision by the full Board finally makes the case ripe for judicial review which, unlike many other administrative appeals,264 lies within the jurisdiction not of the federal district courts, but of the federal courts of appeal.265 Only the individual aggrieved by the agency action has standing to pursue judicial appeal of a decision of the full Board; the government lacks such standing.266 The appeal must be filed within sixty days of the entry of the Board's final order.267

While in a non-emergency case brought under Section 609 the pendency of this appeal process will have automatically stayed the effectiveness of the government's order of suspension or revocation, that automatic

260. 49 C.F.R. § 821.43 (1981). However, if the order was issued under the emergency power, it continues in effect during this appeal process, which is accelerated by the Board's rules. In such an emergency case, notice of appeal must be given within 2 days after the oral initial decision, followed by filing of the appeal brief within 5 days after filing the notice of appeal. 49 C.F.R. §§ 821.57(a) and (b) (1981).

Issues on Appeal.

On appeal, the Board will consider only the following issues:

(a) Are the findings of fact each supported by a preponderance of reliable, probative, and substantial evidence?
(b) Are conclusions made in accordance with precedent and policy?
(c) Are the questions on appeal substantial?
(d) Have any prejudicial errors occurred?

262. 49 C.F.R. §§ 821.47(g) and 821.57(b) (1981).
267. 49 U.S.C. § 1486(a) (1976), which also grants the court discretion to permit filing of a petition after that time period, by leave of court, upon a showing of reasonable grounds for failure to file a petition within the statutory time limit.
stay expires upon issuance of the full Board’s order. Counsel must take affirmative action to secure a stay order at this point, if the client’s existing medical certificate is to continue to remain in effect during the pendency of the judicial appeal. Application for such a stay order pending judicial review is required to be made first to the Board, if practicable. The Board has the authority to postpone the effective date of its order, pending judicial review, upon a finding that justice so requires. If the Board denies the motion for a stay order, then the Court may grant such an order upon a showing of good cause and after reasonable notice to the Board. The Board typically refuses to grant stays in cases where the appellant’s qualifications to hold the certificate are at issue (which is the case in the vast majority of medical certification actions).

Except for challenges to the constitutional validity of the underlying regulation, no objections may be raised upon judicial appeal which were not previously argued before the Board. The Court’s scope of review is narrow, and it is bound by the Board’s findings of fact, provided they are supported by substantial evidence. Challenges to the sufficiency of the evidence are extremely unlikely to be successful.

The court is empowered, upon review, to affirm, modify, or set aside the Board’s order, in full or in part and, if need be, to order further proceedings by the Board or by the FAA.

The judgment and decree of the court of appeals is finally subject to review by the United States Supreme Court but only upon certification or by the grant of a writ of certiorari, which is a most unlikely event.

VI. Equal Access to Justice & Federal Tort Claims Act Aspects

Final resolution of a medical certificate action may take several years and involve attorney fees and expert medical witness fees which are quite burdensome to the individual. Where the individual is a professional aviator

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272. 49 U.S.C. § 1486(e) (1976). *See also supra note 149.*
273. The applicable standard of review is whether the Board’s decision is supported by substantial evidence. *Loomis v. McLucas,* 553 F.2d 634 (10th Cir. 1977).
278. This review power has existed at least since passage of the Air Commerce Act of 1926, ch. 344, 44 Stat. 568. The author has found no aviation medical certification case in which the Court has granted certification or certiorari in the ensuing fifty-six years.
who has been without a medical certificate (and therefore without his usual source of income) for that time period as a result of a "Section 602" denial or "Section 609" emergency action, that individual may be financially ruined even if he eventually prevails in regaining his medical certificate.

In cases arising under Section 609, at least, the new Equal Access to Justice Act (EAJA)\textsuperscript{279} may provide some recompense.\textsuperscript{280} At this writing, the first of these cases is now pending before an administrative law judge of the Board.\textsuperscript{281}

While the EAJA appears inapplicable to aviation medical certificate denial cases arising under Section 602, the Federal Tort Claims Act (FTCA) may provide a tenable cause of action for recompense in certain of these cases.\textsuperscript{282} In an FTCA action, the burden would be on the aviator to prove negligence on the part of the government (or its designee AME),\textsuperscript{283} whereas in an EAJA action, the burden is on the agency to prove its actions were reasonable and its position to have been substantially justified.\textsuperscript{284}

VII. CONCLUSION

Aviation medical certification cases rank among the most hypertechnical cases in which private counsel are called upon to provide advice and advocacy.

A multidisciplinary approach in which the aviator’s legal counsel works closely with the aviator’s physicians is an absolute prerequisite to ultimate success.

Even then, the unbridled administrative discretion inherent in the highly subjective and secretive off-the-record decision making process, together with the heavy case loads assigned the FAA decisionmakers provides an


\textsuperscript{280} The Act provides for reimbursement of attorney fees and costs to an individual who has been the subject of an adversary adjudicative proceeding brought by an agency, where the agency’s position was not substantially justified. Pub. L. No. 96-481, 94 Stat. 2325 (to be codified at 5 U.S.C. § 504). The Act applies to suspension or revocation cases (see supra notes 196-202 and accompanying text) but not denial cases (see supra notes 98-163 and accompanying text) because the Act excludes from its coverage an adjudication for the purpose of granting or renewing a license. Pub. L. 96-481, 94 Stat. 2325 (to be codified at 5 U.S.C. § 504(b)(1)(C)).


\textsuperscript{283} Id.

\textsuperscript{284} The National Transportation Safety Board has adopted Rules Implementing the Equal Access to Justice Act. These provide, in part, at 49 C.F.R. § 826.5(a) (1981); . . . the burden of proof that an award should not be made to an eligible prevailing party is on the agency counsel, who may avoid an award by showing that the agency’s position was reasonable in law and fact.
atmosphere conducive to arbitrariness. This has resulted in a situation in which aviators are highly suspicious of the fairness and impartiality of these decisionmakers who wield, in the language of one critic, "an executioner's power over the pilot's legal ability to fly." 285 The seemingly interminable bureaucratic delays and unpredictability of results further aggravate the situation, resulting in a process which may prove extraordinarily, if not prohibitively, expensive to the aviator and ultimately prove a classic and monumental exercise in frustration not only to the aviator, but to his counsel and personal physicians as well.

This is intolerable in what is intended to be a democracy governed by laws, and not by the whims of bureaucrats. Aviation medical standards contained in the FARs should be updated to reflect advances in medical knowledge and treatment capabilities and should reflect the highest possible specificity, both for ordinary certification and for certification in special cases. The decision-making process should be opened to the light of public hearing, on the record, with the opportunity for confrontation and cross-examination.

We have come a long way from the early romantic days of airline flying, when it was said of airline pilots that: "They are the picked men of the country. These men must not only be perfect mentally and physically, but the art of flying a plane must be born in them." 286

Today, almost a million rather ordinary (though well trained) Americans possessing a rather wide variety of physical imperfections are doing a very presentable job of flying planes. Medical knowledge continues to advance, with increasing precision in diagnosis and new methods of treatment yielding concomitant increases in pilot health and longevity. In such times, the standards and procedures for medical certification of flight crews must also progress to keep abreast of these developments. Indeed, at this writing, such a review has begun. 287 The medical standards and procedures which result from such periodic reviews must always reflect a careful balancing of the public interest in maintaining an air transportation system which provides the highest possible degree of safety for the traveling public against the individual liberties of professional aviators and recreational flyers.

<table>
<thead>
<tr>
<th>Age Group</th>
<th>Maximum readings (reclining blood pressure in mm)</th>
<th>Adjusted maximum readings (reclining blood pressure in mm)</th>
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<tr>
<td></td>
<td>Systolic</td>
<td>Diastolic</td>
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<td>20-29</td>
<td>140</td>
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<td>30-39</td>
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<td>92</td>
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<tr>
<td>40-49</td>
<td>155</td>
<td>96</td>
</tr>
<tr>
<td>50 and over</td>
<td>160</td>
<td>96</td>
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\(^1\)For an applicant at least 30 years of age whose reclining blood pressure is more than the maximum reading for his age group and whose cardiac and kidney conditions, after complete cardiovascular examination, are found to be normal.
**Note:** Outer Continental Shelf Oil and Gas Pipeline Regulation: Federal and State Interaction

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The coastal regions and the Continental Shelf of the United States are unique, fragile environments that contain a variety of resources, both living and non-living. Outside of fisheries and other living resources, the Outer Continental Shelf (OCS) has vast reserves of natural resources. Recent estimates show at least half as much oil and a third as much natural gas as the entire United States onshore reserves.\(^1\) Recent advances in technology allow for possible exploration and discovery at greater ocean depths,\(^2\) which make it possible to place offshore facilities further from adjacent shorelines. As a consequence, meeting the transportation needs of the offshore development facilities will become more complex as the search for oil and natural gas takes place in deeper waters further out to sea.

This paper will address the evolving state of the law concerning regulation of oil and gas pipeline transportation in the OCS and coastal areas. The statutes and regulations controlling the lease for exploration and development of OCS areas must be examined. A discussion of rates, ratemaking and accounting will not appear here, but emphasis will be placed upon examining the interaction between federal, state and local regulations that determine the location, placement, and control of energy facilities, especially oil and gas pipelines, in the OCS. Emphasis will also be placed upon locating points of overlap between the regulating governmental agencies, and their effect on national energy and environmental policy.

\section*{B. Assumptions}

Several assumptions must be made at this point. First, oil or gas produced in a federal OCS lease area that is pumped through a state OCS area is transported in interstate commerce. From a practical business standpoint and from case analyses, this appears to be a safe assumption. Second, the recent nature of several major statutes and their state counterparts leaves the total impact of such statutes rather uncertain. For exam-

\begin{footnote}
\item Id. at 7.
\end{footnote}
ple, the Coastal Zone Management Act (CZMA)\(^3\) has specific provisions allowing states to develop and implement their own local land use plans in coastal areas. Only now are cases emerging that afford solid precedent. Third, this type of regulatory system, affording much public input, can engender litigation. The effects of possible litigation, while not the major focus of this paper, must always be considered. Fourth, much variation exists in state statutes affecting the OCS. Issues of high visibility or importance in one state, reflected in that state’s statutes, are often times not addressed in another state’s statutes. For example, air quality issues may be hotly debated in California, but of little importance in Alaska.

Finally, overland pipeline routes for oil and gas and the associated regulatory problems are not discussed here. One cannot assume that the same issues are present nor that locating such pipelines is without regulatory difficulty.

II. Statutes

A. Outer Continental Shelf Lands Act/Submerged Lands Act

1. Jurisdiction

The Submerged Lands Act (SLA)\(^4\) and the Outer Continental Shelf Lands Act (OCSLA)\(^5\) effectively divide the OCS area between the federal and state governments. From the low water mark of a coastal state to a distance of three miles, that state has exclusive jurisdiction, control and ownership of the submerged lands.\(^6\) The OCS areas past the three mile limit are under the exclusive control of the federal government’s ownership, control and regulatory process over that area.\(^7\) Boundary disputes still occur between the state and federal governments,\(^8\) making location and subsequent regulation of pipelines an unclear task. Finally, where a boundary dispute occurs or an oil field crosses the federal/state boundary, provisions exist for cooperative agreements and joint sales between the federal and state governments,\(^9\) which allows lease sales, exploration and development to go forward.

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2. **LEASE PROGRAMS, STRUCTURE AND PUBLIC INPUT**

The OCSLA provides the framework for five year OCS lease sales programs under the Department of Interior. The statute sets out principles that govern the five year program, and no lease may be issued unless it is included in the approved leasing program. Public notice and participation are provided for, and the states have an opportunity to review the proposed five year program. Finally, Congress has an opportunity for review, but no congressional approval of the program is needed.

3. **EXPLORATION**

Pre-sale exploration can occur in OCS areas, but the Secretary of the Interior can inspect or use any of the information gathered. Pre-sale exploratory wells can be drilled after the requisite permits are obtained. After specific OCS tracts are nominated, but before selections for sale have been made, tract information for nominated areas within the three mile limit of any state must be provided to that affected state.

4. **ENVIRONMENTAL STUDIES**

An environmental analysis is prepared pursuant to the National Environmental Policy Act (NEPA) and a separate environmental evaluation by the Director of the Bureau of Land Management (BLM) then occurs. The final nomination of tracts is made by the Secretary of the Interior after recommendations from the Director of the BLM.

5. **THE SALE**

A proposed notice of sale and a final notice are given that contain information to the bidders, including bidding procedures. The lease sale

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22. 43 C.F.R. § 3314.1(b) (1981).
then occurs25 where the lease is awarded to the highest bidder.26 Bids may be disqualified or rejected,27 and the Attorney General reviews each sale for anti-trust violations.28

6. TERMS

The lease term is usually for 10 years,29 but lease activities can be suspended for indefinite periods.30 Once a lease is issued an exploration plan must be submitted to the United States Geological Survey (USGS).31 This plan must detail the activities undertaken, describe the installations and equipment to be used, locate each well and provide current structure maps.32 Each plan is reviewed by the Director of the USGS for severe environmental impacts33 and, again, an Environmental Impact Statement (EIS) might be prepared.34

7. DISCOVERY

Once a discovery has been made, a development/production plan must be submitted to the USGS35 which is reviewed for environmental impacts36 to determine if another EIS has to be prepared.37 Each plan must specify the activities to be undertaken, the equipment to be used, the location of all facilities and schedules for development.38

8. OTHER CONTROLS

A. MINERALS MANAGEMENT SERVICE

The Director or the Deputy Director of the Minerals Management Service (MMS)39 has the authority to promulgate operating orders for OCS re-
regions. These orders regulate the operation of activities in the OCS areas.

B. **CORPS OF ENGINEERS**

The power to prevent obstructions to navigable waters is vested with the Army Corps of Engineers (COE). Pipelines, pumping stations and storage facilities located in navigable waters will need COE permits before construction. However, the status of a certain structure as a hazard or obstruction to navigation is uncertain.

C. **FEDERAL WATER POLLUTION CONTROL ACT**

Finally, under the Federal Water Pollution Control Act, any discharge of pollution, without compliance with the Act, is illegal. Compliance entails permits when the discharge is intentional and controlled. If oil were to spill accidentally, this would be an illegal discharge under the Act.

**B. COASTAL ZONE MANAGEMENT ACT**

The Coastal Zone Management Act (CZMA) provides for the transfer of authority to the states for land use decisions that will affect their coastal areas. The federal government provides grants to the states so each may develop its own coastal management plan. The Secretary of Commerce approves the plan after certain criteria are met.

1. **AMENDMENTS**

The purpose of the CZMA was to encourage comprehensive state and local planning when managing coastal resources, in cooperation with the federal government. Prior to 1980, the main focus of the CZMA was to afford the states the authority and flexibility to regulate their unique coastlines, with federal assistance and cooperation. With the passage of amendments in 1980, the goals of the CZMA changed from an environmentally protectionistic to a developmental point of view. Most likely in response to the 1973-1974 Arab Oil Embargo and the corresponding high prices of oil and gas, Congress recognized the "national objective of attain-

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ing a greater degree of energy self-sufficiency." Therefore, Congress responded to the changing times and amended the CZMA in 1980. However, these amendments left an inherent conflict of goals in the CZMA.

2. Certification

Separate from the coastal state’s own plan are the activities carried out in the federal OCS areas. Four types of activities in the OCS are required to be certified by the state to ensure the activity will be consistent with the state’s coastal zone management plan. First, activities supported or conducted by federal agencies that directly affect the coastal area need certification.50 Second, any federal agency undertaking any development project in the coastal zone of a state must be certified.51 Third, private activities which affect the land or water uses in the coastal zone and require a federal license or permit mandate consistency certification.52 Fourth, federally assisted activities of a state or local government which affect a coastal zone are required to be certified.53 The OCSLA makes this consistency certification a prerequisite to gaining the federal license or permit necessary for development activities,54 as does the CZMA.55

3. Diversity

Each coastal state has the option to develop its own Coastal Zone Plan (CZP). The result is that a wide variety of regulatory structures are emerging. Implementation and enforcement are left to state mechanisms as well as the determination of local standards. Each state also allows for local participation in varying degrees. For example, the Alaska Coastal Management Plan creates an Alaskan Coastal Policy Council56 that affords local boroughs and municipalities a fair amount of control over standards and enforcement.57 The Washington state program, called the Shoreline Management Act of 1971, sets up timetables for local governments to complete their shoreline inventories and master programs,58 but notes:

This chapter establishes a cooperative program of shoreline management between local government and the state. Local government shall have the pri-

56. ALASKA STAT. § 44.19.155 (1980).
57. ALASKA STAT. § 46.40.030 (1982).
58. WASH. REV. CODE ANN. § 90.58.080 (1982).
mary responsibility for initiating and administering the regulatory program of this chapter. The (state) department shall act primarily in a supportive and review capacity with primary emphasis on insuring compliance with the policy and provisions of this chapter.\(^{59}\)

C. **DEPARTMENT OF ENERGY ORGANIZATION ACT\(^{60}\)**

Public Law 95-91 on August 4, 1977, established the Department of Energy (DOE)\(^{61}\) but reserved to the states the authority of any matters exclusively within state jurisdiction.\(^{62}\) Interstate Commerce Commission jurisdiction over the transportation of oil was transferred to the DOE\(^{63}\) and, subsequently, within DOE, the ICC regulatory functions concerning rates or charges for the transportation of oil by pipeline were transferred to the new Federal Energy Regulatory Commission (FERC).\(^{64}\)

1. **FEDERAL POWER COMMISSION AUTHORITY**

The Federal Power Commission’s authority over gas pipelines was transferred to the DOE and the FERC,\(^{65}\) including the power to issue certificates of public convenience and necessity.\(^{66}\) FERC is also vested with the responsibility to regulate the transportation of gas as an industry affected with public interest, pursuant to the Natural Gas Act,\(^{67}\) under the DOE Organization Act.\(^{68}\)

This power to regulate has been interpreted to be very broad by the United States Supreme Court.\(^{69}\) More specifically, recent regulations provide that any holder of an OCS lease:

contemporaneously with the submission of a development and production plan to the USGS, must submit to FERC that portion of any development and production plan which relates to production of natural gas and the facilities for transportation of natural gas.\(^{70}\)

2. **TRANSFERS OF AUTHORITY**

The federal government’s transfer of authority concerning natural gas to DOE and FERC appears complete. However DOE’s and FERC’s regula-

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59. WASH. REV. CODE ANN. § 90.58.050 (1982).
64. 42 U.S.C. § 7172(b) (Supp. IV 1980).
70. 30 C.F.R. § 250.34-2(q) (1982).
tion of the transportation of oil only extends to "the regulatory function establish[ing] rates or charges for the transportation of oil by pipeline or establish[ing] the valuation of such pipelines." 71 FERC does not appear to have complete authority over the regulation of oil pipelines. For example, FERC does not appear to have veto power over the location of an oil pipeline through the certification of public convenience and necessity process. FERC does have licensing and permitting authority for the construction of works for the development and utilization of power across, along, from, or in navigable waters pursuant to the DOE Organic Act. 72

III. CONFLICTS

A. PIPELINE RIGHTS-OF-WAY

The federal agencies have control over pipelines in the federal OCS area by virtue of the federal statute (OCSLA) and the federal lease granted to the explorer/developer. In terms of authority over location, the Director of the USGS must approve the design, construction and the plan of installation of OCS pipelines that are contained in a lease area, utilized lease area or contiguous leases of the same owner or operator. 73

The OCSLA provides for the procurement of rights-of-way through submerged lands for the transportation of oil or natural gas by pipeline. 74 These rights-of-way can extend through either lease areas under the OCSLA or nonlease areas. 75 Environmental protection must be maximized through the use of the best available and safest technologies, including the safest practices of pipeline burial. 76 Any established pipeline must provide transportation service to oil or natural gas produced from the OCS leases in the vicinity, without discrimination, based upon proportionate amounts established by the FERC. FERC may hold public hearings and must consult with the Secretary of Energy in determining the proportionate amounts. 77 Any failure to comply with these provisions could lead to the forfeiture of the grant of the rights-of-way. 78 The OCSLA also provides that pipelines in the OCS region must be operated in an open and non-discriminatory manner. 79

For pipeline authority granted after September 18, 1978, FERC can, upon request by shippers that are able to provide a guaranteed level of throughput and on the condition that the shipper bears its proportionate

71. 42 U.S.C. § 7172(b) (Supp. IV 1980).
73. 30 C.F.R. § 250.20 (1982).
75. Id.
76. Id.
77. Id.
78. Id.
share of the costs and risks, order the expansion of throughput capacity, after notice to all interested parties and a full hearing.\textsuperscript{80} Finally, the Attorney General must be consulted by the Secretary of State and FERC concerning specific conditions to be added to any grant of rights-of-way for pipelines.\textsuperscript{81}

1. **MEDIATION**

The CZMA provides for a limited mediation mechanism if a federal agency and a coastal state disagree over the development or implementation of a management program or the administration of such a program.\textsuperscript{82} If any such differences should develop, the Secretary of Commerce, with the cooperation of the Executive Office of the President, must seek to mediate such differences.\textsuperscript{83} This process must include public hearings in the affected local area.\textsuperscript{84}

2. **COASTAL ENERGY IMPACT PROGRAM**

A second, more practical effort to help the states impacted by coastal or OCS energy development is the Coastal Energy Impact Program (CEIP) established in amendments to the CZMA.\textsuperscript{85} CEIP consists of a system of grants to states having federally approved coastal zone management programs impacted by coastal or OCS energy development activity.\textsuperscript{86} The program does not provide any new mechanisms for avoiding possible adverse impacts, but funds efforts to mitigate such impacts once they occur. CEIP finances state programs for the study and planning of new or expanded coastal or OCS energy facilities.\textsuperscript{87}

The conflict between state and federal authority over pipelines becomes critical when a pipeline is to cross both federal and state lands to reach the shore. The states have ownership and regulatory control of the lands from their coastline to a three mile limit by virtue of the SLA.\textsuperscript{88} The federal government retains ownership and control over all other OCS submerged lands.\textsuperscript{89} Theoretically, the conflict is handled in one of two ways: cooperative agreements and consistency certification.

\textsuperscript{82} 16 U.S.C. § 1456(h) (1976).
\textsuperscript{83} Id.
\textsuperscript{84} Id.
\textsuperscript{89} 43 U.S.C. § 1334 (Supp. IV 1980).
3. **COOPERATIVE AGREEMENTS**

First, the location of any pipeline right-of-way could be included in the cooperative agreement between the affected state and the federal government. However, these agreements usually only cover the lease sale area and the sale itself, to allow exploration and development of common areas. Because pipeline rights-of-way generally are located after a discovery of oil and gas, they are rarely included in such cooperative agreements.

4. **CONSISTENCY CERTIFICATION**

The second method available to control the location of pipelines through federal and state areas is the state’s CZPs. Because each federally licensed or permitted activity must obtain a certificate of consistency if its proposed activity, as found in the development and production plan, will affect the land or water use in the affected state’s coastal zone, a further look at the state’s CZP is mandated. The California CZP is a complex one that has delayed coastal development projects and increased the cost of the same. The Alaska and Washington state plans are contrasted because the programs have different levels of local interaction and state control.

**A. ALASKA’S COASTAL ZONE PLAN**

Alaska’s CZP encourages the development of district coastal management programs based upon a municipality’s existing or new comprehensive plan or a comprehensive statement of needs, policies, objectives and standards. The local programs, in existing municipalities, then control what land and water uses will take place in that municipality’s area. In an unorganized borough (not an uncommon entity in Alaska) coastal resource service areas may be organized to draft district coastal management programs. If the local program seizes upon strictly non-development or non-industrialized uses of the coastal area, the required consistency certificate may be difficult, if not impossible, to obtain.

**B. WASHINGTON’S COASTAL ZONE PLAN**

The Washington State Shoreline Management Act of 1971 provides that the local government will have “the primary responsibility for initiating and administering the regulatory program.” The same difficulties in obtaining consistency certification exist here, as they do in Alaska.

However, the Washington program further requires a permit from the

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92. ALASKA STAT. § 46.40.030 (1982).
93. ALASKA STAT. §§ 46.40.110, 46.40.180 (1982).
94. WASH. REV. CODE ANN. § 90.58.50 (1982).
governmental entity having administrative jurisdiction for any substantial development undertaken on the shoreline. The applicant must also bear the burden of proof that a proposed substantial development is consistent with the criteria established by that governmental entity.

C. Federal Energy Regulatory Commission's Authority

Contrasted with the Alaska and Washington state CZPs is FERC's wide reaching power over construction, extension, and abandonment of natural gas pipeline facilities, the granting of certificates of public convenience and necessity and the right of public domain. These broad powers could come into conflict with a state or local government's power under the CZP, drawn up and approved by the federal government.

D. Projection of Pipeline Routes

A third alternative method to locate pipeline routes was tried by Suffolk County prior to a lease sale under the OCSLA. The county contended that the EIS should project the pipeline routes to predict the possible onshore zoning and coastal environmental problems. The United States Court of Appeals for the Second Circuit found that such speculation would not aid in the EIS process. The court reasoned that projected routes would be of no avail because:

no oil had as yet been discovered within the half-million acres of ocean bottom, some 50 miles by 50 miles in size, which was under consideration for lease, and . . . one could not specify the location or locations where it could be discovered, much less the quantity and quality of oil that might be discovered. Any projected routes would of necessity, therefore, have to be arbitrary, and might bear no similarity to the routes that would actually be proposed upon discovery of oil.

The EIS in this case did contain numerous references to state and local regulatory powers and procedural requirements that could be invoked to restrict coastal pipeline location and advised that the state and local authorities would control pipeline sites, routes and use their land use controls. The court concluded that this was sufficient to meet the requirement that the environmental aspects of transportation of oil and gas be considered in the EIS.

98. Suffolk County v. Secretary of the Interior, 562 F.2d 1368 (2d Cir. 1977).
99. Id. at 1376.
100. Id. at 1376.
101. Id. at 1377.
IV. CONCLUSION

Historically the federal government dominated OCS lease sales, and development under the OCSLA, especially prior to the SLA. This is contrasted by the present state and local government authority to control the local coastal land use decisions in their area. The OCSLA has created a complex layered system of laws and regulations, basically following the exploration, development and production phases of the OCS lease. Compliance with the planning for the system is difficult and time consuming. The end result of this system, combined with the state CZPs and boundary disputes, is that the cost of development, and especially transportation, of OCS leases will continue to rise. Secondly, the development and consumption of OCS resources will be delayed. 102

A regulatory system affording input, reflection, study, cooperation and compromise usually produces better, more dynamic results. The OCS coastal regulation of oil and gas pipelines is such a system with certain qualifications. First, the Department of Energy must eliminate confusion surrounding jurisdiction and regulation of OCS pipelines. Identification of regulatory authority and specific regulations will lend stability to the regulatory structure and induce timely compliance.

Second, local political entities need to define their coastal zone policies more completely and in further detail. By setting out objectives, criteria and procedures, companies are better able to respond to local needs and comply with reasonable requirements which will finally speed resource development.

Third, too many studies are done on the same project. Data must be collected and consolidated to lend efficiency to resource management questions. Because OCS pipelines pose a unique set of study problems, all levels of government should have timetables established for projection of possible routes, before discovery, and pipeline project environmental studies after discovery occurs.

Oil and gas, like other minerals, are of localized occurrence and must be developed. They must be transported as efficiently as possible to market or the refinery. Because the state and local governments control coastal land use decisions, oil and gas producers must be willing to meet both the federal conditions under the lease and the local coastal use and permit requirements. By so doing, a tension is created between our present energy policy promoting self-sufficiency and the existing environmental statutes affording states, and localities, control over coastal resources in their jurisdictions. On balance, this writer believes healthy tension in a federal

102. See Bright, supra note 91, at 243.
system is much preferred to a one-sided policy dictated by one of the parties to that system.

Thomas E. Hames
Common Carriers—Continuity and Disintegration in United States Transportation Law

Part II*

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C. **DEREGULATION AND THE COMMON CORE OF TRANSPORTATION LAW**

1. **THE PROCEDURAL FRAMEWORK OF RATEMAKING**  
2. **SUBSTANTIVE CRITERIA OF RATEMAKING**  
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III. **CONCLUSION**

I. **INTRODUCTION**

A. **THE DISINTEGRATION OF THE LAW AND THE NEED FOR HARMONIZATION**

Part One of this article was essentially concerned with rate regulation and the maintenance of the appropriate level of competition by entry, merger and antitrust rules. In evaluating such regulations a primary standard is furnished by what may be called the presumption of uniformity. An appropriate solution as between a railroad and a shipper cannot be deviated from in the law governing other transport modes without a plausible explanation. Different interest groups and administrative bodies involved in legislative and regulatory actions have too often prevented sufficient consideration of the basic need for uniform solutions. Today this need is felt more strongly than ever.\(^1\) The harmonization of divergent rules would restore the coherence to transportation law which has been missing since the common law days. It would also save administrative costs for legal research and, above all, benefit combined transport, which is presently hampered by overlapping agency jurisdictions and contradictory substantive rules and policies.

In light of the foregoing remarks, this article will compare the various solutions adopted by different modal laws to common or similar problems. In analyzing arbitrary deviations from an otherwise common rule, it is important to bear in mind that the presumption of uniformity is only a formal standard. It does not indicate whether the majority or deviating minority rule should be approved as the better one. Although such a substantive appraisal requires further consideration, tentative answers will be suggested which may indicate a direction for future research and reflection.

1. **TARIFFS**

Legislation has created a structure of tariff regulations which is surpri-

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\(^1\) See the statements of a former U.S. Secretary of Transportation and his aides: “There is a need to develop... a true transportation law, a law whose principles are applicable to all modes of transportation.” Boyd, Ross & Teberg, *New Dimensions in Transportation Law*, 1 Transp. L.J. 1, 17 (1969).
ingly common to all modes of transportation. This commonality seems to provide for a minimum degree of equality among shippers and passengers without overly restricting the carriers' flexibility. There are four essential elements of tariff regulation:

(1) Publication. Carriers are required to publish tariffs and make them available for public inspection. While the Shipping Act requires only the latter, publication does not seem any more difficult for shipowners than for other carriers. Publication by ocean shippers, especially if centralized and standardized, would make the information more accessible to inland shippers. As to the contents of tariffs, comprehensive information about all price components as well as classifications, rules, practices and regulations is prescribed by statute for ocean shipping, inland navigation and railroads. Motor and air carriers are required to include non-price elements only after further regulation of the ICC or CAB. The expense of compliance with the publication requirements could be minimized by using approved standardized contracts drafted by trade associations.

(2) Filing. All carriers are required to file their tariffs with their respective regulating agency. Where the agency, like the Federal Maritime Commission (FMC) in domestic ocean shipping, lacks the power to prescribe minimum rates, the filing requirement consequently concerns only maximum rates. However, this nexus with rate regulation is only one function of tariff filing. Filing also provides reliable and accessible information about the carrier's business behavior. Such information becomes the more important when an agency lacks direct regulatory powers. In this regard, the limited filing duty of domestic ocean shipping lines, especially in light of their limited publication duty, is subject to criticism. In general, however, the filing requirement would not be necessary if a standardized form of publication provided for easily accessible and comprehensive tariff information.

(3) Observance. Although statutes use different language which may solicit divergent interpretations, carriers of all modes are unambiguously required to observe their tariffs. This obligation, combined with the duty to publish tariffs, is the key to tariff regulation. It guarantees the application of rates which have been found reasonable and non-discriminatory by an agency under the present system of rate regulation. Even if the agencies and their regulatory powers were abolished, the observance of tariffs would substantially limit the industry's price discriminating power. If carriers charge a different rate under similar conditions, it must be established by

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public tariff. A carrier will therefore always take into account the effects that a tariff change might produce if generally applied. In some cases, by a special agency authorization, carriers are excused from complying with their published tariffs. In surface transportation, this exemption applies only to contract carriers who operate on a more individual basis.\(^7\) In domestic ocean shipping, the FMC may allow common carriers to charge more than their established tariff rates after ten days public notice.\(^8\)

(4) Notice of tariff changes. The inherent virtue of tariff regulation is supported by provisions which require carriers of all modes to give public notice of proposed tariff changes. Changes become effective thirty days after notice, unless the supervising agency exercises its discretion and shortens this period.\(^9\) Thus, carriers are not at liberty to grant special rates for single occasions and withdraw them afterwards. Here again, the legislation regarding domestic ocean shipping does not contain any rule about tariff changes; thus, it does not fit the general pattern. Rather, it provides for exceptional deviation from established tariffs and thereby fosters carrier flexibility. There is no obvious reason for this difference; accordingly it should be replaced by the general approach.

As a whole, tariff regulation reduces the carrier's ability to adjust his price and service standards to whatever the market will bear under the given circumstances, and thereby furthers the equality of shippers and passengers vis-a-vis the same carrier. However, there remains one very effective device for the carrier to achieve price discrimination. Nothing prevents carriers from writing classifications into tariffs which are so precise that they concern only one shipment or only one shipper.\(^10\) Agencies or courts willing to suppress these practices will face great procedural difficulties, but they possess and should exercise a wide discretion to rebut such classifications as arbitrary, artificial and unreasonable.

2. **The Duty to Serve**

The ancient common law duty of common carriers to serve every applicant has been codified in all modal laws.\(^11\) However, the various statutes differ in language and they provide little information about the scope of the obligation. The Shipping Act is particularly unclear. It prohibits the refusal to carry only in the context of retaliatory actions; however, there can hardly be any doubt that the refusal to carry is unlawful regardless of the carrier's

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motives in the absence of a legitimate excuse. Also, it is difficult to understand why air carriers should be subject to the duty to serve only in domestic and not in foreign transportation. These legislative gaps are undoubtedly filled by the more comprehensive common law rule.

In this area, the problem is not the individual rejections of shippers or passengers, but the shortages of capacity in rail and air transportation. The lack of capacity has always been regarded as a sufficient excuse for the refusal to carry. If it were not for the duty to carry and the basic policy objective of making transportation generally available, the shortage of transport capacity would not differ from supply shortage in any industry and no agency would be obligated to intercede. Both the ICC and the CAB, however, have felt constrained to remedy existing scarcities, though they approach the issue differently. While the ICC may try to overcome the deficiencies by requiring rail carriers to enlarge their capacity at least temporarily, the CAB administers shortages by allowing embargoes and overbooking. In this comparison we may disregard overbooking because it is a counterpart of the special form of airline reservations which do not bind the passenger. But the different handling of capacity shortages by the agencies must be noted and deserves further study.

3. The Carrier’s Liability

The key elements in every liability system are the basis of liability, the amount of recovery and the possibility to change the respective rules of law by agreement of shippers and carriers. Other important facets are the time span of liability under the various modal laws and specific exceptions. Short time limits and the venue for litigation often discourage potentially successful claims.

In the absence of tariffs, the liability for cargo loss and damage of railroads, trucks and domestic air carriers is strict, save for the classical common law exceptions. In domestic ocean shipping, this principle is upheld, but the Harter Act excludes errors of master and crew in the management and navigation of the vessel, thus creating a peculiar blend of non-liability (even for negligence) and strict liability. The international conventions governing foreign shipping and aviation have adopted the non-liability exception and changed the basic rule from strict liability to fault liability with a reversed burden of proof.

Restrictions on tariffs provide that no limitations of the carrier’s liability

15. See generally id. at 24-27, 33-34, 39-41.
are allowed in surface transportation. Through their tariffs, both domestic water and air carriers usually confine their liability to negligence, which is allowed under the Harter Act and at common law. Therefore, there remain two major differences among the modal laws:

(1) The management and navigation or piloting exceptions under the Hague Rules and the Warsaw Convention. These are outdated and have been deleted in later conventions which the U.S. has not ratified.

(2) The strict liability of railroads and trucks as opposed to fault liability with a reversed burden of proof for water and air carriers. In practice, this difference concerns those causes of damage like fire and theft which the carrier may be able to prove without difficulty, but which do not fall within one of the exceptions of strict liability. For example, if a warehouse fire destroys goods, some of which were shipped by railroad, others by barge, the railroad is liable to the shipper for damages while the barge owner may discharge himself from liability.

This result can hardly be explained in terms of intelligible policies. Rather, it appears that a solution can most easily be found by approaching the types of damages individually instead of doctrinally. In cases of uncertainty one might envision a rule under which parties can choose between different liability standards at different freight rates.

As to the amount of recovery granted, the modal laws vary in a similar way. While the trucking, railroad, domestic shipping and domestic aviation legislation affirms or at least does not impair the common law principle of full damages, the international conventions severely limit the recoverable amount in foreign air transportation. Under the Warsaw Convention, full recovery may be obtained only if carrier or crew has acted with willful misconduct.

If the analysis includes contractual or tariff limitations, the cases of full recovery further diminish. Domestic air carriers of property limit their liability to 50¢ per pound. Similar stipulations by surface and domestic water carriers have been upheld only if the shipper was offered full recovery at a higher freight rate. Surface carriers also need ICC approval. On the other hand, carriers in foreign transportation by air and water may extend their liability up to the actual value under agreements with the shipper. While the Warsaw Convention seems to require the carrier to accept a shipper’s declaration of value and to negotiate a potential extra charge with him, the

Hague Rules leave the carrier entirely free to make such an agreement. The apparent lack of uniformity of liability would be less troublesome if a higher amount of recovery could always be obtained for a higher rate. This is not always the case. In many sections of foreign shipping or surface transportation there is no such choice. Moreover, where the shipper is faced with this choice, his starting-point varies according to whether the law provides for full or limited recovery in the absence of an agreement between the parties. None of the differences in the carrier's liability has been explained on intelligible grounds. Rather, the differences seem to be the product of a political balance in the respective organizations which sponsor the various rules.

Until more is known about how many carriers and shippers actually view liability as a competitive practice, a common solution for all transport modes can hardly be devised. Also, the average value of cargo or shipments in the various modes should be known before one can consider any numerical liability limitations. Under the present uncertainty, the least detrimental system would be one which enables shippers to choose between different liability and rate combinations. Carriers should be required to offer such different combinations. Such an obligation can probably be imposed more easily under a law which makes the carriers liable for the full amount of damage in the absence of an agreement restricting liability. Carriers will be interested in discharging themselves of liability which causes unnecessary administrative costs for large claim departments and increases their overhead. Under a basic rule of limited liability, there is no incentive to offer higher rates for increased recovery. It should also be noted that under a system of expanded liability there will be a need for provisions which protect carriers against ruinous claims and protect consumers against a choice of rate and liability combinations based upon gross misperception.

4. **The Scope of Application of Regulations: Common Carriers**

Almost no regulation is applicable to all carriers of one mode because of the pervasive distinction between common and private carriers. The borderline between common and private has been drawn in very different ways. Almost all railroad and aircraft concerns are operated as common carriers. Major portions of the trucking and shipping markets, however, consist of private carriers. Different modes performing the same function may be subject to different characterizations. For example, under a voyage charter, the owner of a vessel is a private carrier whereas the owner of an airplane is regarded as a common carrier. A truck owner working under the same conditions may be a contract carrier. Even within the same mode of transportation, the characterization may differ. Tramp ships may function

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as private carriers for one purpose while remaining common carriers with respect to liability.

Against this background, the term "'common carrier'" is little more than a political catchphrase for transport regulation. It is frequently used in statutes and rarely defined. Future legislation should define what the term means in the context of a specific statute or replace the term "'common carrier'" with "'regulated carrier'" or another term less burdened with historical connotations.

Apart from these suggestions, it is doubtful whether regulatory statutes should generally focus upon the status of the carrier. For some commercial purposes, the better solution seems to center upon the performed activity. Businesses can more easily recognize the type of commercial operation at hand than the general status of the carrier. The status approach will still be necessary in setting requirements for other purposes such as entry control, financial responsibility and safety regulations. What is retained is the general idea that the scope of a regulation has to be defined in accordance with its purpose and subject matter. Therefore, the statute must use appropriate criteria which may change from rule to rule.

The recent history of transport regulation has given much support to a fundamental reappraisal of rate regulation. Restoring competition is not equivalent to an overall deregulation. There are areas of transportation law which obey different policies than those governing rate deregulation. The last section of this article will investigate whether the present deregulatory movement respects those independent areas of transportation law and whether it has contributed to its needed unification or to further disintegration.

II. THE COMMON CARRIER IN THE ERA OF DEREGULATION

Since the 1970's, regulation in general and transport regulation in particular, has faced increasing criticism. Pursuing lines of economic thought developed in the 1960's, first the CAB and then the ICC tried to implement more competitive policies within old statutory frameworks. The deregulatory movement was encouraged during the administration of President Ford, but received its present vigor from the joint efforts of the Carter Administration and Senator Edward Kennedy. These efforts brought about the deregulation of the airline industry in 1978, which was followed by a less drastic decontrol of railroads and trucking in 1980.

Before presenting an overview of the major deregulatory steps in the above mentioned industries, the arguments in favor of and against dereg-

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lation will be set out. There will follow an assessment of the remaining common carrier duties and obligations.

A. The Arguments For and Against Deregulation

In evaluating the following discussion one must bear in mind that the choice open to the legislature is seldom complete deregulation. Often only a less restrictive alternative to the present regulatory scheme is politically feasible or socially desirable. Therefore, the arguments on both sides have relative weight.23

1. The Arguments in Favor of Deregulation

There are essentially four major arguments in favor of deregulation.24 The first and perhaps the most important in a free enterprise economy is that management rather than government should control a carrier's economic behavior. Under regulatory statutes, however, the price and service decisions of a regulated carrier require more legal analysis than market inquiry. There is the risk that firms will no longer receive their information from the marketplace but primarily from an agency which possesses second-hand knowledge.

The second argument condemns the agencies for their overly protective and paternalistic policy. Indeed, the equal-price-for-equal-distance rule promulgated by the CAB during the Domestic Passenger Fare Investigation reduced price competition between different carriers to zero.25 In surface transportation, the value-of-service ratemaking policy of the ICC has been extensively used to prevent intermodal competition.26

The third argument is a variation on the theme that regulation fosters inefficiencies. For example, the exclusion of air fare competition fostered service competition beyond demand, especially an unnecessary frequency of flights, which drove load factors down. The argument is that deregulation would result in lower rates on the one hand, and in an increase of

25. The Domestic Passenger Fare Investigation proceedings are contained in CAB Docket 21866. Other protective measures of the CAB are the route moratorium of 1969 and the toleration of the capacity-limitation agreements among carriers in 1971. See Behrman, supra note 22, at 97-98.
26. See generally Basedow, supra note 13, at 22-23.
demand for transportation services on the other. Both would combine to increase carrier profits. The experience of the non-regulated intrastate air carriers in California and Texas supports this argument.27 It seems, however, that this line of thought is rooted in the transportation of passengers and does not apply to transportation of cargo. In the carriage of goods, regulation undoubtedly imposed some inefficiencies upon trucking. This was not caused by rate regulation, but rather by the prescription of routes which often engendered empty returns instead of allowing the carrier to pick up cargo at a point for which he was not licensed.28 What happened in the airline industry was an expansion of demand in response to lower prices. This was possible because of the high price elasticity of demand for the transportation of passengers. As to the carriage of goods, however, transportation costs in most situations are so low as compared with the value of the cargo that changes in freight rates are very unlikely to influence the demand for traffic.29 Thus, rate decreases are not expected to result from the deregulation of the railroads. The main objective with regard to railroad deregulation is to increase railroad revenue.30 This can be achieved by higher rates in those parts of a system where alternative transportation is not easily available.31 In trucking, lower rates are more likely to follow deregulation, which would result from increased competition, not higher transport efficiency.32

The fourth argument contends that the expansion of activity just described increases overall employment in the transportation industry. While this is plausible with regard to the airlines, such expansion is much less likely in freight transportation.

2. THE ARGUMENTS AGAINST DEREGULATION

The major argument against deregulation is protectionist. Organized labor has opposed deregulation because it fears lower wages and a potential decrease of overall employment from growing competition. Wage levels in the transportation industries, however, have risen higher under the regu-

27. See Breyer, supra note 23, at 588; Mansfield, supra note 10, at 91-92.
29. Mansfield, supra note 10, at 68, refers to a study which calculated the price elasticity of demand for shipping services at −0.13; with respect to surface transportation, a similar argument is made by Dempsey, supra note 22, at 313. Contra, Rakowski & Johnson, supra note 24, at 69 (reporting the case of Texas International Airlines, which reduced its fares about 50% on certain flights in five test markets; the result was a 600% increase in passenger traffic in those test areas).
32. Johnson, Ready Or Not!—Here Comes Transportation Deregulation!, 46 ICC PRAC. J. 352, 353 (1979) (reports a return percentage on invested capital of 19.66% in 1977 in the trucking industry as compared with a 14% average in U.S. industry).
latory umbrella than in unregulated markets. This is so because higher labor costs were accepted as valid reasons for higher tariff filings by the ICC and the CAB.33

Opponents of deregulation contend that it will be ruinous for some carriers and drive others into mergers. This prediction has been verified by some post-deregulation mergers in the airline industry.34 This prediction seems plausible in trucking but would be unverifiable for railroads, with years of government supported mergers behind them.

Other arguments foresee abandonment of small community service in favor of the lucrative markets between major cities and a cutback on safety expenses due to increased competition.35 Smaller carriers entering the markets abandoned by large carriers will have poorer safety records and will be more difficult to supervise.36

B. THE STEPS TOWARD DEREGULATION

The deregulatory movement, though most clearly expressed in the several statutes promulgated since the mid 1970's, is not confined to the acts of Congress. Economists had, with an unusual unanimity, favored partial or total deregulation since the 1960's, and an impressive body of literature had broken the terrain.37 After 1970, inflation due to soaring fuel prices became a major concern, especially for the airline industry. Deregulation promised a partial remedy in the form of lower transportation rates.38 When deregulation was implemented in the late 1970's, the economy experienced a revival with growing transportation markets. Thus, the risks of detrimental effects, especially bankruptcies due to increased competition, were diminished, and the political opposition declined.39

Deregulation started in the airline industry, which is an inherently competitive market because of low entry barriers. The structure of the trucking market, the next object of decontrol, was even more favorable to competi-

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34. Dempsey, supra note 22, at 306.
35. Though Caves, Performance, Structure and the Goals of the Civil Aeronautic Board Regulation, in THE CRISIS OF THE REGULATORY COMMISSIONS 131, 132 (P. MacAvoy ed. 1970), lays stress on the separation of economic and safety regulation in the CAB and in the Federal Aviation Agency, he concludes, "it is not possible to refute the assertion that regulating turnover is a safety measure."
36. The inadequate safety records of the new commuter lines is well documented. The probability of a fatal accident involving a commuter aircraft was five times that of its regional and national counterparts in 1979. Fasten Your Seat Belts, Time, Aug. 4, 1980, at 47.
38. In September 1974, President Ford convened a "summit conference on inflation" which unanimously recommended deregulation as a means of lowering prices. See Behrman, supra note 22, at 102-03.
39. Id. at 113-14.
tion. In justifying the withdrawal of government interference, even in the monopolistic railroad industry, Congress found that "today, most transportation within the United States is competitive," and that "nearly two-thirds of the nation's intercity freight is transported by modes of transportation other than railroads." Though it might have been expected that the deregulatory movement would spread to ocean shipping, this has not yet occurred. While there are tendencies to reinforce competition in the ocean liner markets, the toleration or encouragement of the liner conference system by most countries makes unilateral action by the United States a delicate problem. Moreover, it is not clear whether competition or cartelization provides for the more efficient structure. Small amendments focusing on specific conference and carrier practices are therefore more appropriate and likely than an overall attempt at systematic deregulation.

The only common pattern in deregulatory legislation is a relaxation of rate control by the creation of zones of reasonableness. As long as the carriers' charges remain within the respective zones, the power of the agency is minimal. The lowering of legal entry barriers was an essential part of trucking and airline deregulation. Because of the length of rail networks, legislators focused on abandonment of unprofitable routes in deregulating railroads. The thrust of the Staggers Act is the broad permission to contract rates with single shippers which meet specific shipper demands and thereby provide for more efficient use of rail facilities. Though the antidiscriminatory provisions remain almost unaltered, the favor accorded to contract carriage and to discount fares implies that Congress today sees more virtue than harm in discrimination.

1. **Airlines**

Airline deregulation became a serious political issue in early 1975 when the Economic Report of President Ford deplored the inefficiencies brought about by regulation and Senator Edward Kennedy opened hearings on CAB practices. Concurrently, the CAB started to loosen its control. The route moratorium under which the CAB had refused almost all new applications since 1969 was terminated, as were the capacity limitation agreements among carriers competing on a given route which the CAB had authorized since 1971. CAB also withdrew certain operating restrictions on charter carriers. It encouraged rate experiments on various routes which

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43. Rakowski & Johnson, supra note 24, at 71.

44. See Behrman, supra note 22, at 97-99, 110-11.
generated a surprising increase in demand, but also induced passengers to reroute their journeys so as to profit from the low fare routes. Consequently, the airlines applied for low fare approval on other routes.

The most radical withdrawal from precedent was the policy of "multiple permissive entry," formulated in 1978. Previously, route awards for particular markets resulted from two inquiries: (a) an investigation of the demand for additional service in that particular market and (b) the selection of the carrier who would be best able to meet that demand. The innovation of "multiple permissive entry" left the second inquiry to market forces. If the CAB acknowledged a need for additional service, it would grant route awards to all applicants without requiring them to actually operate on the route. Whether this new policy is authorized by statute remains an open question since deregulatory legislation has totally reshaped entry regulation.

The first legislative step toward decontrol was the deregulation of carriage of goods by air in 1977.45 Almost hidden in a statute about the war risk insurance of aircraft, the deregulatory provisions initiated in the Senate brought about two major changes:

(1) Creation of a special certificate for all-cargo air service in domestic transportation which can be obtained regardless of "public convenience and necessity" by any applicant who is fit, willing, and able to provide such service. Conditions and limitations which the CAB may impose on the certificate must not concern rates or routes.46

(2) Restriction of CAB's authority to regulate rates for both the domestic and international transportation of property, whether by all-cargo aircraft or combination aircraft. The CAB can still alter rates and practices which it finds predatory or discriminatory and order a carrier to discontinue such practices. However, the CAB may no longer prescribe rates or suspend proposed tariffs pending a hearing.47

The most spectacular event in deregulation was the Airline Deregulation Act of 1978.48 This Act restricts government supervision and, for the first time, tries to phase out a regulatory agency entirely. The paramount feature of the statute is the relaxation of several entry provisions. New certificates were previously issued on a "public convenience and necessity" basis; now they merely need be "consistent" with these targets. The burden of proving the inconsistency lies upon the opponent of an application, such as an incumbent carrier.49 Moreover, no inquiry into the demand for

additional service is allowed on so-called dormant routes. Dormancy occurs when a certified carrier holding a route fails to provide service five times a week for at least thirteen weeks of any twenty-six week period. If there is only one carrier on a route, entry is permitted to any carrier who is able to provide service on a first-come-first-serve basis. 50 Under the automatic entry rule, any certified interstate carrier could acquire, without opposition, one new city-pair market a year until 1981. Each existing interstate carrier can protect one city-pair route each year by designating it ineligible for automatic entry. 51 The spirit of the new entry regulation is perhaps most clearly expressed by the provision authorizing experimental certificates of limited duration. 52

In the area of rate regulation, the major innovation is the concept of a zone of reasonableness. Rates may be increased by up to five percent above the standard industry fare level, except in monopolistic markets, and decreased by up to fifty percent. Within these limits, fares are presumed to be just and reasonable. A further element of liberalization is the containment of the power of the CAB to approve mergers, interlocking relationships and inter-carrier agreements and to confer antitrust immunity.

In order to protect small communities from deregulation, Congress provided that all cities previously served by certified carriers were guaranteed "essential" service for the next ten years. The CAB must either find a carrier willing to serve such cities or subsidize the carrier formerly operating the unprofitable line so that it can continue service. 53

The International Air Transportation Competition Act of 1979 extended the deregulatory program to foreign air transportation. 54 Like the Airline Deregulation Act, this statute eases entry into foreign air transportation by making it dependent upon mere "consistency" with the public interest. 55 Similarly, the Act provides for zones of upward rate flexibility of five percent and downward rate flexibility of fifty percent, centering upon a "standard foreign fare level" which the CAB periodically adjusts for all city-pair markets. 56 The effect of these and other provisions will largely depend upon

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whether the United States can persuade foreign governments to adopt its competitive aviation policy. There has been some success in this regard in recent bilateral agreements with foreign nations.57

2. TRUCKS

Historically, there has been less regulation in the trucking industry than in the airline industry. Agricultural transport, as well as local carriage within defined commercial zones, has been exempt from regulation, and control over contract carriers has been restricted.58 The administrative deregulation by the ICC proceeded from these exempt areas, trying to widen them where possible.

One of the important ICC decisions considerably enlarged the commercial zones of cities and the equally exempt terminal areas of motor carriers.59 Other decisions abolished the restriction imposed on motor contract carrier certificates to serve not more than eight shippers, and allowed private carriers to carry for hire incidentally to the transportation of their own merchandise. Also, the Commission drastically lowered entry barriers. While previous entry regulation tried to avoid any financial harm to incumbent carriers, the ICC recently made it clear that the benefits of heightened competition may outweigh the potential harm to the incumbent certificate holder.60

The deregulation of motor carriers of goods was sanctioned and furthered by the Motor Carrier Act of 1980.61 Without wholly abandoning the industry to market forces, it limited the power of the ICC. Applicants for entry need not now show that service is “required” by public convenience and necessity. As in CAB proceedings, it is up to potential opponents to demonstrate that the new entry is “inconsistent” with public convenience and necessity. The diversion of revenue or traffic from an existing carrier does not in itself prove this inconsistency.62 Moreover, carriers are entitled to the extension of existing certificates to intermediate points and round trip authorizations which will put an end to the empty back-hauls often required under the former regulations.63

In the field of rate regulation, the main innovation is the carrier’s right to choose, within certain limits, between ICC and antitrust regulation. If the

57. See Bailey, supra note 50, at 49-50 for more details.
58. See generally Basedow, supra note 13, at 28-29.
60. See generally Dempsey, supra note 22, at 316-17.
carrier notifies the ICC accordingly, prices which do not deviate by more than ten percent from those of the preceding year may not be attacked by the Commission as unreasonable. If the ICC finds sufficient competition in the particular market, it may increase this flexibility percentage by up to five percent in either direction. But if the carrier chooses to withdraw these prices from rate control by his notification, they are subject to antitrust scrutiny.64

Finally, the deregulation of rates has also modified the liability rules.65 While the basis of liability under the Carmack Amendment remains unchanged, the requirement of ICC approval for released rates on the basis of limited recovery is maintained only for carriers of used household goods. Other carriers may contract at limited liability rates if the value limitation is reasonable and rely either on a written value declaration of the shipper or on a written agreement of the parties. The ICC may require carriers to offer alternative full coverage rates.66

3. RAILROADS

Since the Kennedy Administration, the ailing financial condition of the railroads has kept politicians busy. However, the first major legislative remedy did not come until the Railroad Revitalization and Regulatory Reform Act of 1976 (4R Act).67 Under the 4R Act, railroads could lower their rates to the level of variable costs without the interference of the ICC.68 For an experimental period of two years, Congress enacted a zone of reasonableness for certain tariff classes. Rate modifications of up to seven percent a year could not be suspended by the ICC if the carrier notified the Commission accordingly.69 Also, a 4R Act amendment cautiously opened the door to rail contract rates by giving a five year validity guarantee to rates for transportation requiring an investment of more than $1 million.70 This provision was intended to cover situations requiring specialized freight cars, installation of side track and other unusual expenditures.

Deregulation of railroads was accelerated by the Staggers Rail Act of 1980.71 In the field of rate regulation, it affirms the variable cost level as the lower limit of reasonableness, but maintains a maximum limit only for

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65. See generally Basedow, supra note 13, at 24-27.
those railroads which the ICC finds to have market dominance.\textsuperscript{72} For these railroads, a zone of upward rate flexibility is installed, in the limits of which the ICC must not interfere by the prescription or determination of reasonable rates. Every railroad in a position of market dominance may increase its rates up to a base rate which is defined in the Act and periodically adjusted to cost developments by the ICC. In addition, carriers are entitled to rate increases of six percent per year of the adjusted rate base until 1984 and four percent thereafter.\textsuperscript{73} As a compensation for purely inflationary cost increases, the ICC may prescribe a percentage rate increase which must be deducted from the increases mentioned earlier.\textsuperscript{74}

The most fundamental change in railroad regulation seems to be the broad allowance of contract rates. Contrary to the law governing other modes of transportation, railroad legislation only allowed special rates to be given to particular shippers with specific needs on the basis that these shippers commit themselves to deliver either a certain volume or a certain percentage of traffic over time to a railroad. Initially, this individualistic and contractual approach to railroad transportation was thought to be a destructive competitive practice\textsuperscript{75} and incompatible with the classical principle of shipper equality. But recent experiments under the 4R Act have indicated a strong demand from shippers and potential gains for carriers to be had from such contracts.\textsuperscript{76} The Staggers Rail Act of 1980 now requires such contracts to be filed with the ICC, which shall approve them in principle. In the carriage of non-agricultural goods, the Commission may base its disapproval only on discrimination against a port or on the fact that a railroad is no longer able to meet its common carrier duty to serve other shippers because of the special contractual commitment. Once a contract is approved, the ICC may interfere with its performance only in times of war.\textsuperscript{77} The result is that contract rates are permitted to take priority over the carrier's legal duty to serve every applicant, and the carrier is exempted from the prohibition against discrimination.\textsuperscript{78}

The Staggers Rail Act of 1980 has also relaxed liability requirements. ICC approval for released rates based upon limited liability is no longer required. The statute further offers the alternative of liability agreements in which the shippers agree to deduct certain amounts from liability claims


\textsuperscript{76} The cases reported in Upward Track—Rail-Rate Increases Due for Early Arrival Thanks to New Law, Wall St. J., Oct. 14, 1980, at 1, col. 6, stress the shipper demand for punctuality which could not be satisfied under general regulation, but can be met under bilateral contracts.


C. DEREGULATION AND THE COMMON CORE OF TRANSPORTATION LAW

The motivation behind deregulation in the various areas of transportation law was the desire to increase competition. The question is whether deregulation has enhanced or diminished the degree of uniformity in the various problem areas of transportation law.

1. THE PROCEDURAL FRAMEWORK OF RATEMAKING

(a) Zones of rate freedom. Except for the phasing out of the CAB, deregulation of rates has complicated rather than simplified the legal framework of rate regulation. In the airline, railroad and trucking industries there are now zones of rate freedom. As long as rates move within the limits of these zones, they are presumed to be reasonable and may be attacked only on the basis of discrimination or predation. The zones of rate freedom vary considerably from mode to mode with regard to limits, points of reference and the role of the market structure.

The zones of rate freedom use different rate standards as points of reference. The standard industry fare level and the standard foreign fare level introduced by the aviation statutes are essentially the fares for each city-pair and each class of service on two key days in 1977 for domestic flights, and in 1979 for foreign flights. These fares are periodically adjusted to variations in cost per seat-mile for the whole industry. Costs actually incurred by the individual carrier are not considered. The base rate used in the railroad industry is the rate in effect for a given commodity on the first day of a two-year period beginning on October 1, 1980. Periodically, the ICC will publish rail cost adjustment factors by which the base rate may be adjusted. For motor carriers, the point of reference is simply the rate in effect one year prior to the effective date of the proposed rate; in the case of rate cuts, the lesser of this and the rate in effect on July 1, 1980 governs. Two factors determine the reference rate and the scope of rate freedom for the future: (1) costs to the industry, and (2) the carrier’s own previous rate modifications. The standard fare levels of the aviation statutes are only adjusted to cost changes. If an airline cuts a rate equal to the standard industry fare level by fifty percent, it does not create a new zone of rate freedom centering on the decreased fare. Rather, the fare has reached the bottom limit of the carrier’s zone of rate freedom. Railroads have a new rate every two or five years which is based on the rate they charged on the

first day of the relevant period. Consequently, if they use the zone of their upward rate flexibility to the maximum, their permissible future rates will be higher than they would have been had the railroads been content with lesser rate increases. This dependency on previous ratemaking is even more conspicuous in the case of trucking. Surface carriers will make rate changes not only with regard to imminent competitive effects, but also with regard to a zone of rate freedom appropriate to their own business expectations in the long run. Cost variations have a much more attenuated and indirect impact on railroad and trucking rates than on air fares.

Rate freedom has been extended because of the underlying confidence in competition. Market powers are to prevent carriers from reaping monopoly profits. Consequently, the five percent upward rate flexibility for domestic air carriers is confined when the carrier has a market share of more than seventy percent.83 There is also a limit to the rates railroads may charge when they are in possession of market dominance.84 The upward extension of the motor carrier's zone of rate freedom beyond ten percent depends upon an ICC finding that there is sufficient competition. This same finding is also required when a motor carrier wants to lower his rates by more than ten percent.85 The criterion of market power as a prerequisite for larger rate increases seems appropriate because the ability of carriers to set monopoly prices differs from market to market. However, it is highly questionable whether the market share used in aviation law or the size of profits on which the Staggers Act of 1980 bases its inquiry are sufficient indicia of market power. The better solution seems to be that of the Motor Carrier Act of 1980, which entrusts the determination of the competitive environment to the regulatory agency which can consider all aspects of the single case at hand.

(b) Agency powers. Outside the zones of rate freedom, the agencies have the power to reject, cancel or disapprove proposed rates. They can suspend rates pending a hearing, prescribe minimum rates, or fix maximum rates. Used in combination, the latter two powers may result in the prescription of precise rates. This deprives a carrier of any freedom to determine his own rates. In addition to the powers with direct impact on a carrier's charges, agencies have investigatory powers which affect ratemaking more indirectly. The strongest blend of agency powers is the suspension of proposed rates combined with a prescription of minimum and maximum rates. This combination was a classical pattern for the regulation of all surface carriers and for the transportation by air and inland wa-

The deregulatory statutes have brought about the demise of such plenary agency power.\textsuperscript{86} Even after deregulation, the ICC may still intervene if a proposed railroad rate is unreasonably low. In such a case, the ICC may reject the proposed rate or prescribe a rate not higher than variable costs.\textsuperscript{87} The Commission may only set maximum rates for railroads which have market dominance. All others are free to raise their rates\textsuperscript{88} without review. The regulatory powers of the CAB over air fares in domestic transportation terminated on January 1, 1983.

These facts are evidence of an increasing disintegration of a basic pattern of economic regulation of carriers. In foreign air transportation, the CAB has and will retain the power to reject and cancel rates which it finds unreasonable. It also has the power to suspend rates for one year.\textsuperscript{89} In foreign shipping, the Federal Maritime Commission (FMC) may not prescribe rates or suspend proposed rates, but may disapprove rates found "so unreasonably high or low as to be detrimental to the commerce of the United States."\textsuperscript{90} The FMC has a tighter grasp on foreign government controlled carriers. It may disapprove their non-compensatory rates as unreasonably low and suspend them for up to 180 days.\textsuperscript{91} Different powers are vested in the FMC over ocean carriers in the domestic shipping markets. In this case, the FMC lacks authority to suspend or reject proposed rates and to prescribe minimum rates; it may only prescribe maximum rates.\textsuperscript{92} The differences discussed here frustrate all attempts at unification. "Deregulation from within" has demonstrated that the substantive agency policies are more important than the legal garment of powers through which they are expressed, and that they may fundamentally change without a change in the legal framework.

(c) Rate agreements. In the past, all transportation markets have been cartelized under a regulatory umbrella to a greater or lesser extent. While price fixing agreements have been considered to be illegal in other areas, filing requirements and approval by regulatory commissions has afforded antitrust immunity to cartels and their price fixing agreements in the transportation industry.\textsuperscript{93}

Rate agreements allow the regulatory agencies to predict the market impact of rate rulings and guarantee the carriers profit levels which are deemed necessary to maintain scheduled services with low load factors.

\textsuperscript{92} 46 U.S.C. § 817(a) (1976).
The deregulatory movement has stressed the harm rather than the inherent virtues of transportation price cartels. Congress and the ICC are convinced that such agreements set rates high enough to protect even the least efficient carrier and thereby deprive consumers of the benefits of price competition.94

Under the new statutes, one would hope that a common pattern of price fixing regulation would emerge. Price fixing agreements, discussions among carriers or votes on rates charged for transportation on single line routes on which a particular carrier performs without assistance of other carriers, should be prohibited. As to joint routes, rate agreements should only be permitted among carriers which actually operate on the route. Carriers who operate on a competing joint route should be excluded from price fixing agreements.95 Unfortunately, the new modal statutes do not adopt a common approach to these issues. In trucking, the prohibition of single line rate agreements has been postponed until 1984 and may be revoked after further study. The Motor Carrier Act of 1980 does prohibit agreement on rates within the zone of rate freedom or based upon limited liability.96 But the scope of this provision may very well be restricted to single line rates because there must be a means of agreeing on joint rates. While single line rate agreements are illegal in domestic aviation, exceptions are made for agreements relating to foreign flights on the basis of transportation need, public benefit, comity or foreign policy requirements.97 With the transfer of CAB powers to the Department of Justice in 1985,98 the exceptions for foreign air transportation may well become less significant because the Department of Justice has a history of deploiring the anticompetitive actions of regulatory agencies. In contrast to the airline industry, the price fixing authority of the ocean shipping conferences remain entirely intact.99

While the lack of uniformity may be justified on the basis of comity or the relative impotence of unilateral regulation of international activities, Congress should refrain from hammering out specific antitrust rules for each mode of domestic transportation. If the purpose of deregulation is to conform the law of transportation to general business law, the carrier antitrust legislation should not stress the particularities of each mode lest excuses for future restraints on competition be provided.

2. **Substantive Criteria of Ratemaking**

The preceding discussion focused on the extent carriers are free to determine their rates either alone or through price fixing agreements, and by what powers an agency may implement its policies. Now considered are the two criteria by which the actions of the carrier are tested. These are the common law concepts of "reasonableness" and "non-discrimination."

(a) Reasonableness. Regulatory statutes have traditionally required carriers of all modes to charge reasonable rates without defining "reasonableness." When codifying the common law principle, Congress took the position that reasonableness was a function of the particular circumstances of each case or group of cases and not subject to generalization. Specification was, therefore, left to the regulatory agencies. In the modern deregulation statutes, reasonableness is no longer prescribed, or it is specified to mean a certain cost-rate relationship.

These statutes notwithstanding, rates must be reasonable with regard to ocean and inland water carriers, trucks, freight forwarders, pipelines and foreign air transportation. In domestic air transportation this requirement was phased out on January 1, 1983. With regard to rail carriers, only roads with market dominance are required to keep their rates below a reasonable maximum. Other roads may demand "any rate."

This makes it clear that the Staggers Rail Act removes both statutory and common law barriers to unreasonably high rail rates. Shippers will no longer be able to attack such rates either in ICC or court proceedings. A similar conclusion is much more difficult to draw with regard to domestic air carriers. The Airline Deregulation Act declares that the section of the Federal Aviation Act which contains the reasonable rates requirement shall cease to be in effect on January 1, 1983. There is no indication whether any corresponding common law obligation is abrogated. Although the general policy of the Airline Deregulation Act may favor a construction in favor of complete decontrol, the statute has an experimental character which should prevent an overly broad interpretation. In light of such uncertainty,

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104. This experimental character is evidenced by the motivation for the CAB Sunset provisions articulated in H.R. Rep. No. 1211, 95th Cong., 2d Sess. 22, reprinted in 1978 U.S. Code Cong. & Ad. News 3737, 3758: "This provision will require the Congress to undertake a thorough review
the common law requirement of reasonable rates should be maintained as a safeguard which the courts may employ in cases of apparent abuses of rate freedom. Of course, such use must not intrude into the zone of rate freedom now acknowledged by statute. However this question is finally resolved, future deregulatory legislation should take a clearer stand on the common law rules.

Some statutes have defined the lower limit of what is reasonable in terms of a cost-rate relationship. The rail rates above variable costs are "conclusively presumed not to be below a reasonable minimum." If they fall short of covering variable costs, they are "presumed to be not reasonable." In order to profit from a similar presumption of reasonableness, motor carriers have to "cover total operating expenses" plus a reasonable profit. Finally, an analogous formulation requires foreign state "controlled" ocean carriers to charge rates which are "fully compensatory" of the carrier's costs.

None of these provisions allow the economic ideal of pricing at marginal costs. This may be because the calculation of marginal transportation costs poses insurmountable difficulties in most instances. While such difficulties can be overcome, a carrier may rebut the statutory presumptions and set his rates at marginal costs. Usually, a carrier will be allowed to lower his rates only to the variable or total cost level. Here, it is difficult to understand why rail rates are related to variable costs while truck rates have to cover total costs. Of course, the difference between variable and total costs is much larger for railroads than for trucks because of the comparatively low overhead for trucks. This observation merely explains the difference without justifying it.

One may ask whether the presumption of reasonableness in favor of rates covering variable costs could be adopted as a general rule applicable to all modes of transportation or at least to the remaining regulated carriers. Once the railroads are free to shift from value-of-service to cost-of-service ratemaking there is no need to prevent other surface carriers from doing the same. The necessity of protecting inefficient rail rates against intermodal competition is no longer present. Cost-of-service ratemaking could also be applied to shipping and to foreign aviation in accordance with the fifty percent downward rate flexibility zone and an air fare level covering variable costs.

of the CAB and the functions it performs, and to determine whether the agency should be continued in the same or modified form.

108. See supra note 56.
(b) Discrimination. Discrimination appears in different forms such as rates, tariff classifications and volume rebates. It may be directed against shippers or groups of shippers and against regions and industries as well as transit points, ports and connecting carriers. Whenever there are different rates for services generating equal costs there is discrimination.

This discussion focuses on rate discrimination against shippers. Its main negative effect is subsidization of shippers or passengers paying lower rates by those paying higher rates for equal service. This discourages high rate paying shippers, while stimulating shipping from low rate customers. It should be noted, however, that price discrimination provides for a more efficient use of transportation equipment to the extent that discount rates generate new traffic, thereby increasing load factors.

Common law traditionally has been sensitive to the inequalities created by price discrimination.\textsuperscript{109} Moreover, all regulatory statutes contained provisions prohibiting rate discrimination against persons, places, ports and descriptions of traffic.\textsuperscript{110} Most of these provisions did not specify any particular rate practices as discriminatory per se. The long-and-short-haul clause of the Interstate Commerce Act is an exception which requires railroads to charge rates higher for longer than shorter distances on the same route.\textsuperscript{111} The CAB required an even more rigid proportionality of rate and distance in the Domestic Passenger Fare Investigation. This requirement became obsolete after the deregulation of air fares. Because distance is not a reliable indicator of transportation costs, rate-distance ratios cannot provide a basis for ratemaking in all modes of transportation. It is basically the rate-cost relationship which tells us something about discrimination. When cost calculation is possible, discrimination is ascertained by the comparison of cost-rate. Distance-rate relations should only be employed when cost cannot be calculated due to high fixed and joint costs. This argument furnishes some justification for the isolated existence of the long-and-short-haul provision in railroad law. Unlike other modes, the railroads own their whole infrastructure and they must have a means of apportioning these costs. Since there is no unambiguous way of allocating the overhead, the costs of individual transport operations can be calculated only approximately. A distance-rate relationship may, therefore, be appropriate as an indicator of rate discrimination in this context.

Deregulatory statutes have modified the prohibition of rate discrimination in two respects. On January 1, 1983, the Federal Aviation Act lost effect with regard to domestic aviation.\textsuperscript{112} This again poses the problem whether the common law principle is meant to be affected by the abroga-

\textsuperscript{109} See generally Basedow, supra note 13, at 13-14.


tion. Contrary to the case of reasonable rates, the answer should be affirmative. Congress clearly favors the use of discriminatory rates, such as discount fares, which are viewed almost unanimously as a step toward transport efficiency. The Staggers Rail Act has declared the prohibition of discrimination to be inapplicable to contract rates. The enlarged possibilities for contract carriage, which can also be observed in trucking legislation, reflect Congress’ altered view of price discrimination. High load factors and individual service are valued more than the equality of shippers.

3. **Tariffs**

The four essential elements of tariff regulation are publication, filing, observance and notice of change. Prior to deregulation, tariff regulation was the most common feature in transportation law. Deregulation has challenged the validity of the theory that tariff regulation has an independent importance in transportation law even in the absence of direct rate regulation.

The creation of zones of rate freedom has barely affected tariff regulation. One might have expected that all regulations regarding tariffs within the zones of reasonableness would have been eliminated. Presumably, customers would be sufficiently protected if tariffs were filed with the ICC so that the Commission could determine their consistency with remaining rate regulation. Customers could also be protected by requiring the carrier to publish the legal limits of his rate freedom. Neither of these amendments has been enacted. The only impact of rate freedom on tariff regulation is the new rule in air law which provides that tariff changes which exceed the minimum or maximum of the zone of rate freedom become effective only after sixty days’ notice; changes within the zone of freedom require only thirty days’ notice, as they did prior to airline deregulation.

With regard to railroads, notice periods have been shortened to twenty days for increases and ten days for cuts. Because this provision is entitled “Efficient Marketing” it suggests that the former thirty day period did not allow carriers to react to market demand as quickly as necessary. If this is true, the solution could be extended to other regulated carriers. However, recent legislation has increased rather than decreased the number of notice periods which a shipper employing different transportation modes must contemplate when he evaluates the reliability of tariffs. The former standard 30 day period has been replaced by: (a) 10 and 20 days for railroads, (b)

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114. See supra text accompanying notes 2-10.
60 days for air carriers beyond the limits of their rate freedom, and (c) 30
days for other carriers.

Deregulation of the airlines challenges our theory of the independent
virtues of tariff regulation. The Airline Deregulation Act simply terminates all
tariff regulations in domestic aviation as of January 1, 1983. It can be
argued that this provision is both inappropriate and logically incoherent with
other provisions of the same statute. It is difficult to see why the total abro-
gation of rate regulation should entail an equally total abrogation of tariff
regulation. Rather, the increased rate freedom of carriers enhances the
need for protection of the patrons against the carriers’ notably high price
discriminating power. Unlike demand for most goods and services, the de-
mand for transportation is tied to a specific time and place. This gives car-
riers a temporary monopoly power, even in an otherwise highly competitive
market. Therefore, tariff publication cannot be attacked by the assertion of
the competitive structure of the airline industry. It helps to protect the ship-
ner and passenger precisely in those inevitable moments when competition
proves ineffective. The counter-argument that the publication of tariffs fa-
vors interdependent pricing is not convincing. If carriers benefit from inter-
dependent pricing they will voluntarily publish their rates.

4. The Duty to Serve

Only two changes have affected the duty to serve since the start of
deregulation. The Staggers Rail Act permits special contracts between a
railroad company and individual shippers to take priority over service to the
general public. If the carrier’s capacity is exhausted by such contracts,
there is still no violation of a duty to serve every applicant. The ICC is to
consider the railroad’s capacity before approving a special contract. Ap-
proval is to be based on the carrier’s ability to fulfill his duty to serve the
general public. Priority for contract shippers is necessary because, if the
contract shippers ranked below general shippers, the investment which
special contracts usually engender would be wasted. In some cases, how-
ever, the economic losses imposed upon the general shippers by the un-
availability of railroad transportation could outweigh the waste of resources
provoked by a breach of the carrier’s special contracts. Moreover, the effi-
ciencies of contract performance may be too small to justify the foreclos-
ure of transportation to the general public by a few contract shippers. It is im-
portant to note that only the Staggers Act gives a clear priority to special
contracts. The Motor Carrier Act of 1980 allows common and contract

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118. See supra text accompanying notes 11-14.
carriage on the same vehicle but remains silent as to the appropriate priority.

The second change is the repeal of the requirement that domestic air carriers provide air transportation authorized by their certificates.\(^{121}\) It is unclear whether this applies only to the statutory duty to serve within the limits of the certificate or also to the common law duty within the limits of the carrier’s holding out. Prior to deregulation, a carrier could only hold out his services within the limits of his certificate. With the abolition of route certificates, the common law standard of the carrier’s holding out will regain importance. It can be argued that both the language and the position of the sunset provision in the context of the abolition of entry regulation\(^{122}\) show the intention of Congress to abrogate only the statutory duty to serve. This solution is a counterbalance to the remaining monopoly power of air carriers, particularly in small markets.

5. **The Carrier’s Liability**

The modal laws have varied considerably with regard to both the basis of liability and the amount of recovery for cargo loss and damage.\(^{123}\) Deregulation has ended the brief period of strict liability by divesting the CAB of its power to prescribe tariff regulations. Decontrol has also impacted on the amount of recovery by modifying the liability provisions of the Interstate Commerce Act through the Motor Carrier and Staggers Rail Acts of 1980.

Before deregulation, carriers could limit their liability in exchange for lower rates on approval of the ICC. This was inefficient because it imposed the risk and the insurance costs on the carrier even where the shipper was the cheaper risk bearer and willing to accept the risk for a rate release.\(^{124}\) The requirement of ICC approval has, therefore, been cancelled for rail and motor carriers. Motor carriers of household goods and the non-motor and non-rail ICC carriers are still subject to approval as are pipeline carriers, express carriers, sleeping-car carriers and freight forwarders.\(^{125}\) The question then arises as to why the members of this group require ICC approval for released rates and why rail and motor carriers do not. With regard to motor carriers of household goods, the legislative materials simply reserve the question for later consideration.\(^{126}\) This apparent inattentiveness on the part of the legislature has affected previous uniformity.

\(^{123}\) See supra text accompanying notes 15-21.
While both motor and rail carriers are now free to offer lower rates for limited recovery regardless of ICC approval, the respective rules differ in some points. The declared or agreed value has to be reasonable in trucking, whereas this requirement was explicitly abandoned in the Staggers Act in order to "assure greater flexibility" for the parties.\textsuperscript{127} If the bargain of the parties was not influenced by unequal power, no value can be called unreasonable. The requirement of a reasonable value only makes sense in cases of unequal bargaining power where it may help the shipper reject rate-liability combinations which provide for a minor rate reduction and a major reduction in liability coverage. The total freedom of the Staggers Act comes down to the permissibility of such practices.

The pro-rail bias could perhaps be tolerated if rail carriers still offered full coverage rates. Under the new legislation, the ICC may require motor carriers to offer full coverage rates as an alternative to released rates. However, the Staggers Act does not contain a similar provision.\textsuperscript{128} The Staggers Act notwithstanding, it is suggested that railroads are required to offer full coverage rates as a matter of law and not of ICC discretion. The statute provides that all ICC carriers "shall" establish rates for the transportation and service they provide.\textsuperscript{129} This is a requirement of full coverage because carriers are required to pay the actual loss damages. The permissibility of released rates at limited liability does not impair this principle.\textsuperscript{130} Against the background of this construction of the Interstate Commerce Act, it is the Motor Carrier Act which departs from the common terrain and makes the obligation to offer full coverage rates a matter of ICC discretion.

6. The Scope of Transportation Regulations

An interesting innovation is the use of market power as a new criterion for the application of certain rules. We have observed that the scope of the various new zones of rate freedom depend upon the market power of the carrier.\textsuperscript{131} This reflects a recognition of the fact that many transportation markets are intrinsically monopolistic while others can sustain intense competition.\textsuperscript{132} Therefore, the degree of rate regulation concerning the duty to serve and the prohibition of discriminatory and predatory practices could be tied to the market power of the respective carrier. In monopolistic and oligopolistic markets such regulations are necessary, though they may be

\textsuperscript{130} 49 U.S.C. § 11707 (Supp. V 1981) (released rates flow from subsection (c)).
\textsuperscript{131} See supra text accompanying notes 80-85.
\textsuperscript{132} In a comment on the Airline Deregulation of 1978 in H.R. Rep. No. 1211, 95th Cong., 2d Sess. 9, reprinted in 1978 U.S. Code Cong. & Ad. News 3737, 3745, drafters explain that upward rate flexibility is foreclosed to carriers with a high market share "because actual and potential new entry is needed as a check on abuses of upward rate flexibility."
dispensed with in more competitive markets without detrimental consequences. The determination of market power would have to be left to administrative discretion; but the heavier administrative burden in some areas may be outweighed by the liberalization in the competitive markets.

III. CONCLUSION

The law of common carriers developed three basic doctrines which distinguished it from general business law: (1) the carrier's duty to serve every applicant, (2) the prohibition against unreasonable and discriminatory rates and practices, and (3) strict liability. The crisis befall these rules when transportation became a mass enterprise in the course of industrialization. Courts had more and more difficulty determining the reasonableness of rates and the permissible level of discrimination. Passengers and shippers were unprotected because they could not avoid monopolistic railroads and cartelized shipping companies. This explains why the three decades after enactment of the Interstate Commerce Act in 1887 saw an uncurbed regulatory fever affecting all traditional and many new aspects of transportation law with regard to the railroads. This era of repressive regulation discouraged railroad investment to the point where equipment decayed. About 1920, general policy shifted from the oppression of carrier power to the weighing of shipper and carrier interests. This protective or even promotional regulation rose to its peak in the 1930's when motor carriers, water carriers and air carriers were all regulated, partially to protect the railroads from intermodal competition, but partially to contain intramodal competition.

During the last two decades the theory that an ever more refined network of administrative rulings can shape an industry has yielded to deregulation. Recent statutes express a fundamental shift in policy towards competition in the transportation markets. Unfortunately, policy makers have recognized only part of the regulatory burden which they purport to take off the shoulders of the transportation industry. They fail to recognize the unwarranted burden of a lack of uniformity among the modal laws. Lack of uniformity jeopardizes agreements between carriers of different modes, distorts the information about the various available transportation alternatives and complicates administrative and court proceedings. Where regulation is as meticulous as in the fields of transportation law, uniformity becomes a primary need. While deregulatory statutes have reduced agency powers, they have also contributed to a further increase in disparity of modal rules affecting the common problems.

Future legislation should avoid the errors of the past in two ways. First, legislative proposals should constantly be compared with existing regulations in other modes affecting the common problems. If one of the existing formulations serves the same purpose as the proposal, the latter should be
redrafted in terms of the existing law. Legislators should ask whether a specific modal bill may be extended to other modes. Some provisions of the deregulatory statutes contain generally recognized principles and could easily be adopted by other modal laws. This would help prevent future unwarranted disparities and would preserve uniformity where it still persists. Second, positive reunification of existing modal rules should be undertaken. Apart from defining common concepts on which future modal laws could turn, a model transportation act should be drafted which would provide a basis for a future unification of the modal statutes. This second step would put into effect the legal prerequisites for the pledge of former administrations to create an integrated transportation system. A pledge such as this gave rise to the Department of Transportation fifteen years ago.¹³³ In many respects, this pledge is still unfulfilled.

¹³³. See supra note 1.
 ENTRY AND EXIT
An Economic Analysis of Statutory Changes in Rail Carrier Entry and Exit

RODNEY D. PETERSON*

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Rail Carrier Entry and Exit

1. INTRODUCTION

Rail carriage provides an interesting example of how changes in technology and government policy toward entry and exit affect competitiveness in the transportation industry. In 1830, only 23 miles of rail trackage were operational in the United States.¹ By 1916, the American rail net had reached an all-time high of 254,037 miles.² Today, less than 200,000 miles of track are left in this country,³ a reduction of twenty percent in the 67-year period of 1916 to 1983. This diminution occurred as America’s gross national product (GNP) increased nearly tenfold in real terms⁴ and its population more than doubled.⁵ The period of decline in rail trackage, spanning two-thirds of a century, featured changing technology during which increasing competition from air, motor and water carriers led rail companies to consolidate lines, discontinue service, abandon trackage and lose large amounts of business and revenue.⁶ Whereas railroads carried nearly three-fourths of all domestic U.S. intercity freight traffic in 1930, they hauled less than two-thirds of such shipments in 1979.⁷ Moreover, in the forty years between 1939 and 1979, total commercial carriage by rail dropped from 23 billion to 11 billion passenger miles.⁸ Competition from air, motor and water carriers has been responsible for this decline of rail business.⁹

After seventy-five years of increasing entry between 1830 and 1916, subsequent years marked an exit out of the rail industry. What effect has government policy had on entry and exit? The era of overexpansion and of destructive intramodal competition, fostered by speculative entry into the industry, has been replaced by a period of decline and debilitating intermodal competition, culminating in exit from the industry.

Most railroads have been organized by private interest, although government subsidies, franchises and protectionism were provided at local, state and federal levels. The continuous concern over competition in our economy led government policy makers to foster minimized competition at one point in time and enforced competition at another. The key to competi-

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² Id. at 728.
⁴ Id. at 418-22.
⁵ Id. at 6.
⁶ Detailed data in HISTORICAL STATISTICS, supra note 1, at 728-34 bear out these contentions.
⁷ ASS’N OF AMERICAN RAILROADS, YEARBOOK OF RAILROAD FACTS 36 (1980).
⁸ Id. at 32.
⁹ W. TALLEY, INTRODUCTION TO TRANSPORTATION 171-74 (1983).
tion is ease of industry entry and exit. The railroad industry, tightly regulated, has seen overexpansion (too much entry) and financial difficulties (prevention of exit). Today, a new approach to competition, air and motor transportation deregulation, is being promulgated. The immediate purpose of this approach is to foster additional entry into the marketplace. However, such deregulation may detrimentally affect railroads.

The primary purpose of this paper is to trace changes in transport law with respect to entry and exit experiences of railroads during nearly a century of government regulation. Specific objectives are: (1) to review major economic provisions in important pieces of transportation legislation affecting rail carriers; (2) to review how entry and exit are analyzed in economic terms; (3) to consider selected legislative acts affecting rail carrier entry and exit provisions; and (4) to provide an economic evaluation of entry and exit in rail transportation.

The following question is considered at each statutory juncture: What economic interpretation can be given to various changes occurring in major rail carrier entry and exit legislation during the past century? Criteria for evaluating these changes will be based on entry and exit analysis from industry economics. Legal aspects of rail carrier entry and exit regulation are described by selected statutory provisions.

II. ENTRY AND EXIT IN TRANSPORT LAW AND IN ECONOMICS

Entry and exit are parallel concepts in law and economics. However, the terms used in each discipline vary significantly.

A. ENTRY AND EXIT IN TRANSPORT LAW

In the United States, various segments of transportation have been regulated for nearly a century.\textsuperscript{10} As a result, free-market forces are not a primary determinant of entry into and exit out of a particular mode of transport. Statutes govern entry and exit. They establish procedures to follow, applications to file, criteria to meet, justifications to make, reviews to hold, and decisions to render by administrative agencies and by the courts. Free-market forces operate only on buyer demand and production economies, which, in turn, induce carriers to come into or go out of the industry. These reactions, however, only constitute an initial step. Once the inducement motivates action on the part of a carrier, the determining step is a petition to the appropriate regulatory agency for permission to enter or to exit via certification, consolidation, discontinuance or abandonment.

\textsuperscript{10} Act of Feb. 4, 1887, ch. 104, 24 Stat. 379 was the first real comprehensive attempt at the national level.
1. Certification as Entry

In the regulation of rail carriers, entry into the industry may be closely monitored by requiring potential entrants to apply for a certificate of public convenience and necessity (PC&N). Generally, criteria used to secure the PC&N certificate stress the need for additional transport services, adequacy of existing service, and the impact of the new entry on competition among existing carriers, on interstate commerce, and on the public interest. In order to qualify for and obtain such a certificate, a carrier must meet certain conditions promulgated by the regulatory agency. Criteria tend to vary over time because economic, social and political conditions change and because policy views as to what constitutes the public interest and the general welfare are not static.

2. Consolidation as Entry

Consolidation refers to bringing together existing productive units into an industry which is serving a market. Consolidation ordinarily occurs through the mechanisms of merger and acquisition. Whenever two or more firms join together, not only is the number of separate, independent competitive forces in a market reduced, but the level of concentration is also increased in the industry.

A market can be entered on either a small or a large scale. Since entry affects the nature of competition in a market, the scale of operation characterizing entry is an important consideration. If new firms enter a market, additional competitive units are brought into play and the market tends to become increasingly competitive in the technical sense. If entry by already established firms occurs, however, the market moves away from competition and toward an oligopolistic form of market organization. But if mergers occur between existing market participants in a line of commerce, there is at the same time an exit of one of the competitive forces in the market as well as entry of an oligopolistic force in that market.

14. It is common usage in economics and law to refer to merger, acquisition, combination and consolidation as being synonymous. See E. Kintner, Primer On The Law Of Mergers 110, 133-35 (1973); E. Singer, Antitrust Economics 242-54 (1968).
15. That is, an entrant firm can attempt entry with a small-size plant or a large-size one. See J. Bain, Barriers to New Competition 9-15 (1956).
3. **Discontinuance as Exit**

    If a rail carrier desires to cease operating a particular train along a given route, it is contemplating discontinuance. This particular cessation of service along a route is not a total exit from the market, but only a partial exit in a market sub-group. The Interstate Commerce Commission (ICC) presently considers applications for discontinuance of service and requires that the following criteria be met: (1) public convenience and necessity not be harmed; (2) financial conditions of the carrier not be impaired; (3) adequacy of service not be disrupted; (4) existing carriers not be burdened; and (5) public interest not be hurt.\(^\text{18}\) However, discontinuance is based on the old section 13a of the Interstate Commerce Act (ICA) and has a very limited application because it now applies primarily to non-Amtrak passenger trains.\(^\text{19}\)

4. **Abandonment as Exit**

    Abandonment is a complete exit from a market area rather than a mere withdrawal from one or more market sub-groups.\(^\text{20}\) Abandonment criteria usually are more rigid and detailed than discontinuance criteria. The former include: (1) giving public notice; (2) providing opportunity for purchase; (3) identifying applicant’s other lines and financial conditions; (4) calculating costs and revenues emanating from abandonment; and (5) determining whose interest will be protected by allowing or not allowing abandonment.\(^\text{21}\) In addition, standards for PC&N, competitive effects and the public interest are also applied when evaluating abandonment proposals.\(^\text{22}\)

B. **Entry and Exit in Industry Economics**\(^\text{23}\)

    A key factor affecting the extent of competition in any line of commerce is the number and size distribution of firms. In a free enterprise and market economy, easy entry and exit, coupled with the profit motive and the price mechanism, interact to sustain a sufficient number of firms so that prices are lowered by competitive forces toward the average cost of production. As a result, remaining profits are sufficient to retain the most efficient firms in that particular line. In some cases, where entry is too easy or exit too difficult, destructive competition may develop over time as the in-

\(^{18}\) See Dempsey, supra note 12, at 732-34.


\(^{20}\) R. Sampson & M. Farris, Domestic Transportation 113 (1979) [hereinafter cited as Sampson & Farris].

\(^{21}\) Dempsey, supra note 12, at 732-34.

\(^{22}\) Id.

\(^{23}\) A good example of how entry and exit are evaluated from the standpoint of industry economics can be found in R. Peterson & C. MacPhee, Economic Organization in Medical Equipment and Supply 45-49 (1973).
industry becomes clogged with excessive supply relative to demand at competitive prices.

Industrial organization economics examines the structure, conduct and performance of firms in an area of commerce to determine the extent of competition therein. The structure of the market refers to the economic environment in which rival firms produce and distribute, challenging each other for sales revenue. This environmental setting—structural conditions—embodies the nature of the product, buyer characteristics, extent of concentration and conditions of entry and exit into and out of the industry and its market. Whereas market conduct refers to sellers' behavior for pricing, production and distribution practices, market performance refers to the economic end results of structure and conduct (such as profit rates, selling costs, progressiveness and efficiency). The structure of a market affects the forms of conduct in which firms can engage. Structure and conduct, both interacting, result in a unique set of market performance characteristics for each industry. In this milieu, the extent of entry and exit shape the prospects for competitiveness in the market served by that industry.

The ease with which new firms can enter an industry is a vital element of market structure and is important to competitiveness. Easy entry into an industry helps to create a large number of sellers in a market. Difficult entry into an industry helps to limit the numbers of firms and to reduce competitiveness. Several conditions tend to limit the numbers of firms in an industry: (1) technical requirements for production which necessitate large size or scale; (2) differences in costs of production which exclude potential producers; and (3) opportunities for product differentiation which limit the number of customers a firm might serve. The extent to which these conditions limit entry is dependent on the overall size of the market. A large and growing market provides opportunities for new firms.

1. **Economies of Scale**

A plant which produces an output of some good or service can ordinarily be built with a relatively large or small capacity. Generally, the greater the amount of equipment, the larger the plant size and the greater its capability for output. If costs per unit of output, i.e., average costs, become smaller as plant size is increased, economies of scale probably exist in that line of commerce. The extent of economies of scale is measured by the shape of the firm's long-run average cost (LRAC), which traces the behavior of unit cost of production as plant capacity is increased. If the LRAC is U-shaped, it means that the average cost of production decreases as plant size is expanded, then reaches some low-cost point of relatively constant costs, and rises as diseconomies of scale take over. If LRAC is L-shaped, it

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suggests that economies of scale occur but no diseconomies cause average production costs to rise as plant size increases.

Scale economies probably occur in railroading. Suppose a rail company was established, complete with track, stations, and rolling stock, between two points ten miles apart. The cost per ton-mile of shipment would undoubtedly be higher for that company than for a rail firm which constructed track, stations and rolling stock between two points 500 miles apart. The ability of the latter entity to carry freight the longer distance would allow the company to spread its costs allocated to fixed facilities over a larger number of miles.

If the LRAC for a firm is so U-shaped or L-shaped that costs per unit of output, such as cost per ton-mile, do not reach their trough until plant size is extremely large, then economies of scale become a barrier to entry into that industry. If these barriers exist, it means that it is difficult for a prospective competitor to enter the industry at a relatively small size. Significant economies of scale may even trap existing companies in an industry. Indeed, the cost of going out of business may be so high that firms consider tactics to prevent additional entry or even try to drive existing rivals from the market.

2. Absolute Costs

Often, regardless of the size of a plant of an already established enterprise—whether large or small—a company may be able to purchase necessary inputs at lower costs than prospective firms. If this situation occurs, then a certain plant size not only provides a cost advantage, but there are also benefits of being established in business. Existing firms, compared with new firms, are usually able to buy raw materials at cheaper prices, pay lower interest rates on borrowed funds and hire more productive labor than striving, entrant firms. Established companies, compared with entrants, may already be profitable, face lower risks and enjoy keen business relations with suppliers. These situations are known as absolute-cost advantages for established firms.

Consider railroading as an illustration of absolute costs. An existing rail carrier company may have the best pass through a mountain range; other carriers are at a disadvantage because to tunnel through the mountains elsewhere can only be done at a much higher cost than the carrier with the preferred route. In this respect, the cost of investing in capital may be greater for the new than for the established firm, although both may be of the same plant size and capacity along the LRAC path.

Absolute cost differences operate as a barrier to entry in certain industries. Established firms may set prices above their own costs yet below the costs of potential competitors. As with scale economies, the difference be-

tween price and cost, as it affects profitability (or unprofitability), is a primary determinant of entry conditions (and ultimately of the number of firms in an industry and resulting prospects for competitiveness).

3. PRODUCT DIFFERENTIATION\textsuperscript{26}

In a perfectly competitive market there are few strong buyer preferences for the output of any one of many firms because the product is standardized. Substitution of one product for another would normally occur in this situation. One important result of competition is that a common price is established by the market forces of supply and demand rather than being under the control of individual firms. Whenever one company, however, is able to distinguish its output from that of rival firms the prospects for non-competitive behavior arise. In such a context, a seller may possess the ability to establish a price for its output which is based on product differences. Product differentiation not only causes a market to be imperfectly rather than perfectly competitive, but it often operates to the benefit of established firms and to the detriment of entrants.

Product differentiation becomes a barrier to entry whenever buyer preferences for the output of existing companies are so strong that a potential competitor is unable to charge as high a price for a similar good or service as established firms. Suppose that a hopeful businessman decides to set up a motor launch service between Oakland and San Francisco to transport workers to their jobs. If there are stronger passenger preferences for the Bay Area Rapid Transit (BART) trains than for the water carriage, then the launch operator may not have very many fares and will be destined to an unprofitable business venture.

If consumers prefer one mode of transport, although its price is higher, a product differentiation barrier to entry may occur in an industry. A form of price-cost squeeze can develop for entrants if these barriers are significant. Either the new enterprise must spend vast sums for promotion to try to overcome buyer preferences or it must lower prices significantly below that of existing firms in order to entice customers to its counters. Both tactics result in prices being close to (or even below) cost. In turn, profits will be low (or possibly even nonexistent).

Product differentiation is probably more feasible in the market for passenger service than in the market for freight. Passengers are ultimate consumers, obtaining satisfaction directly and personally from their rides. The general subjective nature of personal human behavior ordinarily makes the ultimate consumer somewhat susceptible to design, style, feature, comfort and other aspects of non-price conduct. Freight, however, is generally a

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\textsuperscript{26} See generally F. SCHERER, INDUSTRIAL MARKET STRUCTURE AND ECONOMIC PERFORMANCE 99, 320 (1970).
business service purchased by managers of firms who largely evaluate alternatives according to objective factors such as price, delivery time and condition, and reliability. A carrier may be able to differentiate its freight service from another rail carrier, but the opportunity to do so, and thereby impress business buyers, is probably less than for consumer passenger services.

4. A Digression on Exit

A necessary factor for a functioning competitive market is relative mobility of resources. This means that few impediments restrict productive capital from going into or out of a line of commerce. For a market to be price competitive, resources allocated to the creation of productive capacity must bring forth additional competitive units. If there are barriers to entry or exit in a line of commerce, competitiveness is hampered whenever additional capital infusions do not increase the number of sellers.

Although industry economists have frequently analyzed entry, exit has received scant attention. Entry is of vital concern because of the desire to foster competitiveness by increasing the number of separate economic units in a market. Exit attracts attention whenever large firms drive out smaller ones through a variety of predatory tactics, such as below-cost pricing. In regulated industries, however, the situation is different because freedom of entry is not generally allowed. Once permitted, entry becomes fixed because exit can only be accomplished by applying and meeting certain rigid criteria.

III. An Act to Regulate Commerce, 1887

The great era of industrialization in America occurred during the period of reconstruction following the Civil War. While industry and commerce were being revitalized in the East and South, the development of the West began in earnest during the 1860's. The construction of our now vast rail network continued from its meager start in 1830, especially beyond the Mississippi River, to augment the settlement of the Western Frontier. In fact, between 1860 and 1890, the amount of railway in the United States

27. A. MARSHALL, PRINCIPLES OF ECONOMICS 540-41 (1920).
increased from 30,626 miles to 163,597 miles, or by more than fivefold.32

A. BACKGROUND TO THE ACT

A compatibility of interests supported the iron horse as it pushed across our land in the mid-1800's: "The public wanted railroads [and] the companies wanted to build them."33 However, by 1870, a conflict of interests appeared: "The public wanted the lowest possible rates; the railroads wanted to earn as large profits as possible."34 Farmers in the Midwest and the Great Plains were angered by high railroad rates and rate discriminations among types of commodities, shippers and routes. The Granger Movement of the early 1870's sparked some state control over the railroads, but such attempts were generally ineffective.35

In less than ten years, three significant events finally induced Congress to do something about the perceived problems in rail transportation: the Windom36 and Cullom37 Senate reports, and the U.S. Supreme Court decision in Wabash.38 The report of the Senate-appointed Windom Committee identified "insufficient facilities, unfair discrimination, and extortionate charges"39 as national transportation problems. The Committee recommended government ownership of one or more railroads. "The Cullom report differed from the Windom report... in that more emphasis was placed upon the evils of discrimination than upon the level of rates... [and]... favored a system of mild regulation."40 In Wabash, the U.S. Supreme Court held that a state (Illinois) could not impose its regulation upon the intrastate part of an interstate shipment.41 This ruling made federal legislation necessary if rail rates were to be controlled. Rail transport was thereby declared to be an interstate phenomenon. High and discriminatory rail rates could not be corrected by separate state legislation because coordination among states is impractical, if not virtually impossible. The result was An Act to Regulate Commerce, passed in 1887.42

B. PURPOSE AND MAJOR PROVISIONS

The 1887 Act was a clear attempt to solve some of the problems addressed in the Windom and Cullom reports, and to respond to the Wabash

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33. D. Locklin, Economics of Transportation 211 (1972).
34. Id.
40. D. Locklin, supra note 33, at 224.
41. Id.
decision. Rail rates were believed to be excessively high and unevenly applied to shippers in the same class. Before 1887, rail rates were established within a framework involving subjective, on-the-spot determinations, overt collusion and special agreements from negotiations based on status. The Act was designed to control high and discriminatory rates, selective ratemaking, pooling and combinations. Collectively, by its provisions, the Act had the purpose of begetting fair and just rail shipment rates in interstate commerce. The following sections appeared in the original Act:

Sec. 1. All charges for any service rendered . . . shall be reasonable and just.

Sec. 2. [A]ny common carrier imposing any special rate, rebate, drawback, or other device . . . shall be deemed guilty of unjust discrimination . . .

Sec. 3. [I]t shall be unlawful . . . to give . . . unreasonable preference or advantage to any particular person . . . or any particular . . . traffic, to any undue or unreasonable prejudice . . .

Sec. 4. [I]t shall be unlawful . . . to charge or receive any greater compensation in the aggregate for the transportation of passengers or of like kind of property, under substantially similar circumstances and conditions, for a shorter than for a longer distance over the same line, in the same direction . . .

Sec. 5. [I]t shall be unlawful . . . [to contract] for the pooling of freight of different and competing railroads, or to divide between them . . . the net proceeds of the[ir] earnings . . .

Sec. 6. No advance shall be made in rates, fares, and charges which have been established and published . . . except after ten days' public notice . . .

Sec. 7. [I]t shall be unlawful . . . to enter into any combination, contract, or agreement . . . to prevent . . . the carriage of freights from being continuous . . .

C. ENTRY/EXIT PROVISIONS

The 1887 Act failed to address adequately the problem of entry and exit. Indeed, there were no entry/exit provisions in the Act. It was no secret at the time that entry was rampant, that duplication of trackage and routes existed, and that predatory pricing was being used to force exit from the industry.44 These problems can be traced to free and speculative entry and to a lack of reasonable efficiency standards for effecting exit. But in that era, private enterprise, competition and assumption of risk were characteristics of an economic system dedicated to freedom and democracy, not to the rigors of government controls.45

43. Id. at §§ 1-7, 24 Stat. 379-82.
D. ECONOMIC EVALUATION

It is surprising that Congress failed to make a vital economic connection when the 1887 Act was drafted, debated and passed. The document itself addresses primarily the matter of rates: high rates, discriminatory rates, and subjective ratemaking.\(^{46}\) The vital economic connection missed was that of excessive entry and its consequences: too much supply in relation to then-present demand so that profitable prices could be charged. Whenever this occurs in an industry where capital equipment is long-lived and immobile it inevitably leads profit seeking firms to capture the limited market. Unprofitable prices inevitably lead some firms to failure and exit. Accordingly, it was reasonably foreseeable that pooling, collusion conspiracies, discrimination, predation and other unfair practices would develop to destroy competitiveness and to waste society's resources. Unfair and unjust rates, to the extent that they existed, were only behavioral manifestations of a deeper underlying structural condition—that of excessive entry and contrived exit via the non-technical economic factor of pricing below cost.

IV. TRANSPORTATION ACT, 1920

Within ten years after passage of the Act to Regulate Commerce in 1887, a series of events had emasculated that statute. In some cases witnesses refused to testify; in others, court delays handicapped the activities of the ICC.\(^{47}\) Moreover, Court decisions in 1896\(^{48}\) and 1897\(^{49}\) reduced the authority and importance of the ICC. These cases challenged the rate-making power of the ICC and rendered ineffective the long-haul/short-haul clause in section 4 of the 1887 Act, which allowed railroads to practice rate discrimination. In the first decade of the twentieth century, however, three statutes were passed to strengthen the rate-making powers of the ICC: the Elkins Act (1903);\(^{50}\) the Hepburn Act (1906);\(^{51}\) and the Mann-Elkins Act (1910).\(^{52}\) Respectively, these acts made both carriers and shippers guilty for illegally granted preferential rates, gave the ICC power to fix maximum rates and restored the provision prohibiting higher charges for short versus long hauls to deal with discriminatory rates.

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47. R. Westmeyer, supra note 39, at 113-14.
A. BACKGROUND TO THE ACT

The United States entered World War I in April of 1917 and the federal government took over the railroads in December of that year.\textsuperscript{53} The take-over was accomplished because the railroads were unable to acquire the necessary equipment to handle the increased volume of wartime traffic.\textsuperscript{54} The U.S. Railroad Administration was created for this purpose and operated the railroads until March 1920.\textsuperscript{55} During the nearly two years and four months of federal operation of the rail system, each railroad was guaranteed a yearly rental payment no greater than a company’s average annual operating income for three years (1914 to 1917). Also, railroad facilities were to be maintained in order to return them in similar shape as the time of take-over.\textsuperscript{56} Efforts were also applied to utilize equipment efficiently, to coordinate rail and ocean shipping facilities, to avert a breakdown in railroad service and to increase wages and rates.

The immediate impetus for passing the Transportation Act of 1920, also known as the Esch-Cummins Act,\textsuperscript{57} was to remove the railroads from direct government operation. Congress also seized the opportunity to review the entire transport regulatory policy and to modify it where necessary and possible.\textsuperscript{58}

B. PURPOSE AND MAJOR PROVISIONS

The main purpose of the 1920 Act was to overcome several inadequacies in railroad regulation. Among these shortcomings were a lack of control over railroad capitalization and service, and labor troubles.\textsuperscript{59} Other problems were also recognized in the rail transport system: "First, the policy of enforced competition . . . was a mistake; and second, the system of regulation was too restrictive."\textsuperscript{60} For one thing, too much entry had occurred; for another, rail rate regulation was beginning to cause the rails to be less profitable.\textsuperscript{61} Moreover, the motor car had been introduced, highways were being built, and additional intermodal competition was threatening.

Broadly, the Act contained five key provisions: (1) a new rule of rate making; (2) encouragement of railroad consolidations; (3) rules for issuing

\footnotesize{53. See Ratner, supra note 31, at 442.}
\footnotesize{54. Scheiber, supra note 44, at 322.}
\footnotesize{55. Id. at 323.}
\footnotesize{56. R. Westmeyer, supra note 39, at 128.}
\footnotesize{57. Transportation Act of 1920, ch. 91, 41 Stat. 456 (codified as amended in scattered sections of 49 U.S.C.).}
\footnotesize{58. D. Locklin, supra note 33, at 240.}
\footnotesize{59. Id. at 240-41.}
\footnotesize{60. Id. at 241.}
\footnotesize{61. Id. at 240-42.
railroad corporate securities; (4) orderly resolution of rail labor disputes; and (5) control of rail service. The first provision provided for rates of return on rail investment of five to six percent, a recapture of earnings clause for excessive profits to be turned over to the ICC, Commission power to prescribe minimum shipping rates via rail, and some ICC control over intrastate rail rates. The second provision was aimed at alleviating a weak-strong road problem by having the ICC prepare tentative consolidation and routing plans to preserve rail resources, to reduce costs and to create operating efficiencies. The third provision "brought issuance of securities by railroad companies under the control of the Commission" and gave the ICC additional power over railroad affairs. The fourth provision established a Railroad Labor Board of nine members to decide controversies involving wages. The Board was an arbitration group which could not render binding decisions. It was superseded by the Railway Labor Act of 1926. The fifth provision pertained to car supply and to extensions of or abandonments of a carrier's rail line. It gave the ICC control over new construction (entry) and over abandonment of line (exit).

C. ENTRY/EXIT PROVISIONS

The Transportation Act of 1920 was the first statute to deal specifically with entry and exit affairs in the rail industry. Senator Cummins, a major sponsor of the original bill which culminated in the 1920 Act, defended its entry/exit provisions by stating that the "transportation system... is now suffering... from the unguided, uncontrollable right of owners to build railroads wherever they may see fit." He argued essentially that speculative entry had created a competitive problem which needed to be corrected.

The ICC needed power to remedy this destructive situation. Section 402 of the Act added twelve paragraphs to section 1 of the 1887 Act to Regulate Commerce (Interstate Commerce Act by virtue of title 1, section 1 of the 1920 Act). Of special importance are the following paragraphs:

(18) [N]o carrier... shall undertake the extension of its line of railroad, or the construction of a new line of railroad... until... first have been obtained from the Commission a certificate that the present or future public convenience and necessity require or will require the construction... and no carrier... shall abandon all or any portion of a line of railroad... until there shall first have been obtained from the Commission a certificate [of public convenience and necessity].

63. D. Locklin, supra note 33, at 249.
65. M. Fair & E. Williams, Economics of Transportation and Logistics 389 (1975).
(21) The Commission may . . . authorize or require . . . any carrier . . . to provide itself with safe and adequate facilities . . . and to extend its line or lines . . . [if] . . . it is reasonably required in the interest of public convenience and necessity . . . .

(22) The authority of the Commission . . . shall not extend to the construction or abandonment of spur, industrial, team, switching or side tracks, located to or to be located wholly within one State . . . .

Section 407 of the Transportation Act of 1920 further amended section 5 of the ICA, as follows:

(4) The Commission shall as soon as practicable prepare and adopt a plan for the consolidation of the railway properties of the continental United States into a limited number of systems.

(6) It shall be lawful for two or more carriers by railroad . . . to consolidate their properties . . . into one corporation . . . .

D. ECONOMIC EVALUATION

Congress ostensibly recognized economies of large-scale operations in railroading when it included a provision in the 1920 Act for consolidation. Failure among the rails had already begun to occur. Direct encouragement and aid from the ICC, coupled with rules for issuing securities, were attempts to allow carriers to achieve efficient size, thereby enabling them to become going concerns. The relation between easy entry, overexpansion and destructive competition was apparently known, for Congress gave the ICC specific power to evaluate applications for permits to construct new rail lines. In addition, one view is that exit was already in its infancy because public policy makers were becoming increasingly interested in preventing society’s scarce resources from leaving the industry. The mechanism of an exit barrier was contained in ICC control over discontinuance and abandonment.

Technological forces were already at work in the economy, culminating in the Great Depression (i.e., the slowdown in the rate of investment) and affecting the field of transportation (i.e., the development of air and motor carriage), which would eventually obviate certain goals of the 1920 Act. New modes of transport injected an element of product differentiation into a sector which lacked a variety of services. Rather than operating as a barrier to entry, however, shipper and passenger preferences for different forms of intermodal transport facilities intensified competition.

68. Id. at § 407(4),(6), 41 Stat. 481 (current version of § 407(6) at 49 U.S.C. § 11343(a) (Supp. V 1981)).
70. T. VAN METRE, TRANSPORTATION IN THE UNITED STATES 335 (1939).
V. EMERGENCY RAILROAD TRANSPORTATION ACT, 1933

During the 1920’s and early 1930’s, at least thirty-eight specific pieces of federal transport legislation were passed.71 Most of these statutes made minor changes in the 1887 Act and the 1920 Act. Several provisions focused on water transport, safety, and special conditions of carriage. One in particular provided for temporary financial assistance to railroads during the early part of the depression.72

A. BACKGROUND TO THE ACT

When a downturn in the business cycle occurred between 1929 and 1933, GNP fell from $316 billion to $222 billion in real terms (i.e., in constant 1972 dollars), labor unemployment rose from eight percent to twenty-five percent, and the Federal Reserve Board’s Index of Industrial Production fell by fifty percent.73 In 1930, approximately seventy-five percent of all commercial domestic freight and passengers was carried by rail.74 When business activity slowed down, so did the need for and use of rail transport facilities. As a result, many railroads declared bankruptcy and were placed into receiverships for corporate reorganization.75 Franklin Delano Roosevelt assumed the Presidency on March 4, 1933, and subsequently persuaded Congress to pass emergency and relief programs to aid ailing businesses, financial institutions and consumers. The Emergency Railroad Transportation Act of 193376 was one of these pieces of legislation.

B. PURPOSE AND MAJOR PROVISIONS

The explanatory headnote to the 1933 Act states that it is: “An act to relieve the existing national [transportation] emergency in relation to interstate railroad transportation, and to amend . . . the Interstate Commerce Act.”77 The Act created an office within the ICC called the Federal Coordinator of Transportation. The Coordinator himself was not to be a member of the ICC.78 The Coordinator had two main responsibilities: (1) to help railroads cooperate among themselves to achieve cost-economies; and

71. These are listed and contained in G. UDEL, LAWS RELATING TO INTERSTATE COMMERCE AND TRANSPORTATION iii-iv (1971).
73. C. McCONNELL, ECONOMICS i-ii (1978).
75. R. WESTMEYER, supra note 39, at 149.
77. Id.
78. Commissioner Joseph B. Eastman headed this office until it was abolished in 1936. D. LOCKLIN, supra note 33, at 261.
(2) to determine various means of improving national transportation conditions given their poor financial shape.\textsuperscript{79} The 1933 Act amended the 1887 Act by establishing a different rule of ratemaking and by repealing the re-capture clause of the 1920 Act. The effect of the first was to give the ICC power to control, and hence to prevent, the use of holding companies for creating combinations and consolidations. The effect of the second was to increase the flexibility by which the ICC regulates rates—to allow consideration of the public interest, adequate and efficient service and the movement of traffic. The intended effect of both was to provide railroads suffering from inadequate earnings with some financial relief.

C. \textit{ENTRY/EXIT PROVISIONS}

The main posture of the 1933 Act was to prevent or forestall exit (via failure and bankruptcy) and to promote, or preserve entry (via mergers among existing carriers). Both title 1 and title 2 of the 1933 Act contained provisions supporting combinations and consolidations. Title 1 pertains to the Federal Coordinator's role; title 2 amended the 1887 Act to include specific provisions authorizing the ICC to control rail mergers.

The policy of promoting and assisting combinations and consolidations among the beleaguered railroads was designed to prevent impending exit and to preserve existing entry. One mechanism to achieve this goal enabled the rails to elect representatives who worked with the Federal Coordinator to develop merger plans. The provision is expressed as follows:

Sec. 3. The Coordinator shall divide the lines of the carriers into three groups . . . eastern . . . southern . . . western . . . and may . . . make such changes . . . as he may deem to be necessary . . .

Sec. 4 [T]o encourage and promote or require action . . . of the carriers . . . which will (a) avoid unnecessary duplication of services and facilities . . . and permit the joint use of terminals and trackage . . . [but] . . . no routes . . . shall be eliminated except with the consent of all participating lines or the Coordinator . . . .\textsuperscript{80}

Another key part of title 2 addressed the question of a mechanism by which rail combinations and consolidations were to be made:

It shall be lawful, with the approval and authorization of the Commission . . . for two or more carriers to consolidate or merge their properties . . . into one corporation for the ownership, management, and operation of the properties theretofore in separate ownership . . . .\textsuperscript{81}

In addition, the title contained precise but complicated language to ensure that the type and form of combinations and consolidations used by merging railroads were subjected to administrative and judicial review for

\textsuperscript{79} Id.

\textsuperscript{80} Emergency Railroad Transportation Act, 1933, ch. 91, §§ 3-4, 48 Stat. 211, 212-13.

\textsuperscript{81} Id. § 202, 48 Stat. 217.
both approvals or disapprovals. These sections required that the merger of one railroad with another must be with actual, existing rail carriers and not with bogus holding companies. 82

D. ECONOMIC EVALUATION

By 1933, the notion of the public interest was firmly established as a goal of overall national policy. With the depression and railroad failures, both Congress and the Administration wanted to protect the rail network. At the time, national concern focused on preserving private enterprise and its competitive market system. Actual and potential exit from the industry was a problem handled by encouraging rails to combine and consolidate—to merge. But any merger or acquisition was expected to result in larger, more efficient size carriers, not speculative entry by those unfamiliar with the railroading business. The Coordinator was in a key position to reach these ends. His duty was to assist in organizing combinations and consolidations which would enable the railroads to achieve the necessary size to be cost-efficient and thereby remain in the industry rather than falter and fail. It was believed that larger carrier size would beget cost efficiencies while preserving competition, but it actually promoted the creation of an oligopolistic structure. 83 Fostering entry via combination was essentially a prevention-of-exit policy which would have the ultimate effect of raising the level of seller concentration in the industry. The frantic effort to cope with the depression apparently caused public policy makers to try to save capitalism at the expense of competitiveness.

IV. TRANSPORTATION ACT, 1940

The Great Depression lasted the entire decade of the 1930’s. 84 By 1939, President Roosevelt’s administration was facing the possibility of entering another world war. 85 Rising military expenditures expanded business activity. Due to the impending armed conflict in Europe and the Pacific, 86 Congress recognized that an adequate transportation system had become a national priority.

83. The number of separate decision making units is reduced when companies merge. See D. NEEDHAM, ECONOMIC ANALYSIS AND INDUSTRIAL STRUCTURE 157-60 (1969).
84. Although income, output and employment fell four straight years beginning in 1929, an economic recovery began in 1933. However, another contraction occurred in 1937-38. L. VALENTINE & C. DAUTEN, BUSINESS CYCLES AND FORECASTING 36 (1983).
85. War with both Germany and Japan was contemplated in 1938 and 1939. See R. BARNET, ROOTS OF WAR 26-28 (1972).
86. Id.
A. BACKGROUND TO THE ACT

Both the depression and technological advances in motor and air carriage created financial difficulties for the railroads. In particular, intermodal competition diminished the prospects for future profitable rail operations. During the 1930's, the number of operating railroads decreased from 775 to 574 and the railroad industry as a whole showed a deficit of nearly a hundred-million dollars. 87 In 1938 and 1939, several ICC reports called for additional transportation laws: (1) to regulate water carriers, (2) to change the policy encouraging consolidations and combinations, (3) to recognize the suitability of specific transport modes for certain purposes, and (4) to eliminate the provision for land-grant rail rate reductions. 88

In response to the intermodal competition problem, Congress passed the Motor Carrier Act in 1935 89 to place highway transport under ICC control, and the Civil Aeronautics Act of 1938 90 to place air transport under control separate from the ICC. Passage of both acts was designed to equalize the regulatory constraint under which the rails were operating. Highway and air transportation, as well as rail transport, became controlled. But the railroad industry needed more help than merely relegating its main competitors to government control.

B. PURPOSE AND MAJOR PROVISIONS

Air, motor, water and even pipelines were alternative modes of transportation used by an increasing number of shippers in the 1930's. Public policy makers expected that these modes would be further developed and perfected during the 1940's and 1950's. 91 A primary focus of the Transportation Act of 1940 92 was to establish a basis for coordination among the forms of transport within a total regulatory context. The major provisions of the 1940 Act reflected this concern by containing features: (1) to subject a limited segment of water transportation to ICC jurisdiction; (2) to promulgate a National Transportation Policy; (3) to eliminate the old predetermined ICC plan of railroad consolidation; (4) to tighten rate-making procedures; (5) to release land-grant railroads from the obligation to haul government mail at reduced rates; and (6) to establish a temporary board of rail transport investigation and research. 93

The initial three provisions merit special attention. The first set up a

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87. Historical Statistics, supra note 1, at 728.
88. R. Westmeyer, supra note 39, at 158.
91. R. Westmeyer, supra note 39, at 160-61.
93. R. Westmeyer, supra note 39, at 156-65.
regulatory procedure for water transport patterned after rail and motor carrier controls. A result of this maneuver was to protect and benefit the railroads by placing water carriers under conditions similar to the rails. The second feature created a general overall policy to be followed by the ICC as it regulated various modes of transportation. Congress, through a National Transportation Policy, recognized that rail, motor and water carriage all had inherent advantages to be preserved. Henceforth, ICC regulation of each mode of carriage had to consider its effect on the other modes. The third provision made significant changes in ICC provisions for rail consolidation and unification. Mergers were to be consistent with the public interest; the specific concerns of labor, and other rail carriers, as well as financial requirements had to be considered in an ICC merger evaluation.94

C. ENTRY/EXIT PROVISIONS

The 1940 Act did not treat the matter of entry and exit according to traditional mechanisms for certification and abandonment. The Act did, however, make a significant contribution to rail policy for entry and exit of already established firms by addressing combination and consolidation plans.95 Basically, the fixed-plan idea for consolidations from the 1933 Act was eliminated and the following new procedures were promulgated: (1) rail carriers would be allowed to combine via their own plans, subject to ICC approval; (2) the ICC could require one or more willing railroads to become part of a proposed merger plan in the same geographical area; and (3) the ICC was given power to prevent holding companies from being used as a form of corporate organization in rail consolidations and combinations.96 The 1940 Act also raised the possibility of rail and motor carriers combining their transport operations.97

D. ECONOMIC EVALUATION

Congress and the ICC did not fully understand the tendency of competitive problems in the railroad industry to exist largely because of entry and exit factors. The Transportation Act of 1940 confronted some basic competitive problems in the railroad industry with indirect and incomplete considerations of entry and exit.

By 1940, Congress and the ICC had learned one lesson regarding the nature of entry and exit: it is not practical for government to design overt plans for private enterprise or to expect designated firms to follow those

94. D. PEGRUM, supra note 74, at 328-29.
96. Id. at 905-06.
97. Id. (amending § 5 of the Interstate Commerce Act).
plans. By allowing some freedom for rail companies to propose their own plans, from the bottom up rather than from the top down, Congress and the ICC moved toward increasing freedom of entry. However, the ICC could require, as a condition for merger of two or more lines, the inclusion of other lines in the same section of the country. Moreover, provisions for labor protection may have been a significant economic disincentive to merge.

The statement in the 1940 Act which contemplated rail and motor mergers is interesting because it considers using service differentiation and diversification to protect a carrier from changes in consumer preferences for alternate modes of transport. It also opened the door for cross-coordination of governmental control of various modes of transportation. The ICC could use its authority to control certification and abandonment of separate economic units within one mode subject to their competitive effects on entry and exit in other modes.

VII. TRANSPORTATION ACT, 1958

After World War II, two pieces of important legislation were passed which affected the ability of railroads to survive and to compete: the Railroad Modification Act of 1948 and the Reed-Bulwinkle Act. The former created a procedure for allowing the financially troubled railroads to alter the terms of their outstanding corporate securities as a means of avoiding receivership and trusteeship. The latter legalized railroad rate bureaus by exempting them from the antitrust laws. These two statutes, however, were not a panacea for the nation’s troubled rail transport system and the continuing problems of previous excessive rail entry as well as subsequent entry by intermodal competitors.

A. BACKGROUND TO THE ACT

During the fifteen years after the 1940 Act was passed, the railroads prospered because of increased freight traffic generated by World War II and the Korean War. By 1956-57, the railroads began to fare poorly as intermodal competition mushroomed from highway and air carriage. During the 1940’s and 1950’s, rail problems were discussed frequently by government agencies and by Congress. In 1954, President Eisenhower appointed the Secretary of Commerce, Sinclair Weeks, to chair a special committee on transport policy. The committee’s 1955 report suggested changes in the ICA but Congress failed to carry out those recommenda-

98. Sampson & Farris, supra note 20, at 403-20.
100. Ch. 491, 62 Stat. 472 (1948).
Next, the Senate Committee on Interstate and Foreign Commerce created a Sub-Committee on Surface Transportation in 1958 to study the rail situation. Several months of hearings were held and several thousands of pages of testimony were published. Persons from government, the rail industry, other transport modes and the academic world all testified about serious problems in railroading. Two U.S. Supreme Court decisions in 1958 raised the prospect of restricting ICC control over rail rates. Congress moved quickly to enact the Transportation Act of 1958 to provide aid to financially distressed railroads.

B. PURPOSE AND MAJOR PROVISIONS

The Transportation Act of 1958 was passed to assist the railroads with difficulties they experienced in adjusting their rates and services to the changing conditions caused by the growth of other modes of competitive transport. The 1958 Act provided for: (1) temporary loan guarantees to railroads; (2) liberalized rules for controlling intrastate rail rates; (3) possible discontinuance of rail service; and (4) a change in rate-setting procedures for rails. Two additional provisions pertained to motor carriers.

Nearly all of the provisions of the 1958 Act focused on promoting or clarifying ICC control over intermodal transportation. The railroad loan program did not involve direct federal aid but created a mechanism by which the government guaranteed payment of interest and principal to private lenders to railroads. Section 13 of the ICA was amended to provide that rates and fares could be declared too low without a rail company having to show their relation to the costs and revenues of its intrastate line operations. In addition, the Act streamlined the timing for ICC investigations and decisions concerning proposals to increase rail rates. For additional relief from destructively low rates and fares, the rule of rate making was amended to provide that the ICC should not hold carrier rates up to a certain level to protect the rates of other modes. A provision was also added to the ICA relating to a rail carrier’s notice of discontinuance of spe-

102. D. Locklin, supra note 33, at 270.
104. Id.
105. In essence, the entire business activity of a rail company, costs and revenues from interstate as well as intrastate operations, had to be considered by the ICC whenever approving rail rates. Chicago, M., St. P. & Pac. Ry. v. Illinois, 335 U.S. 300 (1948); Public Serv. Comm’n of Utah v. United States, 356 U.S. 721 (1958).
107. D. Locklin, supra note 33, at 270.
108. Sampson & Farris, supra note 20, at 359.
110. Id.
cific service and ICC investigation of that carrier's application: "The Commission may by order require the continuance or restoration of operation of service of such train . . . for a period not to exceed one year . . . ."

C. ENTRY/EXIT PROVISIONS

Before 1958, the ICC had no authority over passenger train service. Most states controlled passenger routes but were usually reluctant to allow unprofitable passenger trains to discontinue their service. The 1958 Act gave the ICC jurisdiction over discontinuance or change of the operations or service of passenger trains and railroad ferries.

The new ICA section dealt separately with trains that operated across state lines as compared to those that operated entirely within a state. The Act contained these provisions:

[C]arriers . . . with respect to the discontinuance or change . . . from a point in one State to a point in any other State . . . may . . . file with the Commission . . . notice at least thirty days in advance . . . Upon the filing . . . the Commission shall have authority . . . to enter upon an investigation . . . .

[T]his paragraph shall not supersede the laws of any State . . . .

Where the discontinuance or change . . . of the operation or service of any train or ferry operated wholly within the boundaries of a single State is prohibited by the constitution or statutes of any State . . . the Commission [may] effect such discontinuance or change.\textsuperscript{112}

The 1958 Act was essentially emergency legislation.\textsuperscript{113} Section 13a of the ICA was amended to give the ICC power to prevent discontinuance or change of service for no more than one year if public convenience and necessity existed or if interstate commerce was not unduly burdened. The ICC was also given power to conduct investigations for discontinuance or change of service.\textsuperscript{114}

D. ECONOMIC EVALUATION

In economic analysis, exit usually involves the removal of a competitive force from the market. If the firm makes a marginal adjustment downward to reduce its output because the extent of market demand cannot justify a larger level of production, it is a rational economic decision to reduce output, but not necessarily to cease operating altogether.\textsuperscript{115} Prior to 1958, railway exit by abandonment was allowed for freight operations. The 1958 Act included a provision for discontinuance of passenger service. As such,

\textsuperscript{111} Transportation Act of 1958, § 5, 72 Stat. 568, 572 (current version at 49 U.S.C. § 10908(c) (Supp. V 1981)).

\textsuperscript{112} Id., 72 Stat. 571-72 (current version at 49 U.S.C. §§ 10908-10909 (Supp. V 1981)).

\textsuperscript{113} D. PEGRUM, supra note 74, at 306.

\textsuperscript{114} D. LOCKLIN, supra note 33, at 272.

\textsuperscript{115} C. McCONNELL, ECONOMICS 513-14 (1981).
it did not deal with entry policy but only with a form of partial exit policy. The nature and extent of that exit is not akin to withdrawal from the industry.

Conspicuously absent from the 1958 Act was a refinement of previously amended merger policy. In prior years, notably in the 1933 and 1940 acts, consolidations and combinations were considered as a possible means of salvaging failing railroads. Congress and the ICC apparently believed in 1958 that merger and acquisition were no longer as desirable as other policy alternatives. Instead, the merger approach toward adjusting entry and exit, which tended to result in an oligopolistic structure, was rejected. Congress may have believed that direct financial aid from private loans, guaranteed by the federal government, would improve the financial conditions of rail companies already operating under ICC-approved mergers.

VIII. 4R ACT, 1976

After the 1958 Act was passed, the rail situation still did not improve. Although the 1960's were a period of increasing prosperity, due primarily to government spending on the war on poverty and the war in Southeast Asia, as well as to government monetary and fiscal policies,\textsuperscript{116} the venerable twin problems of intermodal competition and excessive trackage could not be overcome. Transportation continued to be a vital national concern as evidenced by the creation of a cabinet-level agency. The Department of Transportation (DOT) Act\textsuperscript{117} of 1966 was passed in order to develop, improve, and coordinate national transportation policy. Its goals included stimulating technological advances in transport facilities and, of course, fostering the public interest and the national defense. The 1966 Act created, among its various agencies within DOT, the Federal Railroad Administration and a National Transportation Safety Board. DOT received no regulatory powers over rail, except for safety. The ICC maintained nearly all of its previous regulatory authority over rates, entry, exit, mergers and service.

A. BACKGROUND TO THE ACT

Between 1958 and 1969, many passenger trains discontinued their service under the new provisions of the 1958 Act.\textsuperscript{118} Indeed, during that twelve-year period the number of operating railroad companies decreased from 412 to 351.\textsuperscript{119} Passenger services deteriorated badly and Congress sought to upgrade their quality.

\textsuperscript{118} Sampson & Farris, supra note 22, at 113, 359. See supra text accompanying notes 112-14.
\textsuperscript{119} Historical Statistics, supra note 1, at 727.
In the latter part of the 1960's, several rail companies filed for protection under the bankruptcy laws. In mid-1970, the well-known Penn Central went into receivership. In fact, six railroads, making up most of the rail system for seventeen northeastern states, and carrying about twenty percent of the nation's freight, were in receivership at that time. Unfortunately, previous merger policies had not prevented these rail failures.

In the early 1970's, two more acts were passed to try to solve the country's rail problems: the Rail Passenger Service Act of 1970 and the Regional Rail Reorganization Act of 1973 (3R Act). The former created what is now called AMTRAK (for AMerican TRavel trAcK) to deal with rail passenger service problems. The latter created CONRAIL (for CONsolidated RAIL Corporation) to deal primarily with freight traffic. In both cases track was abandoned, trains were discontinued and rail services were combined. Congress allocated hundreds of millions of dollars toward these efforts.

There were some successes resulting from the 1970 Act and the 1973 Act. Once again however, chronic rail problems persisted. Regulation is a continuous process and additional aid and arrangements were needed for rails to be able to serve those shippers and passengers who preferred that mode of transportation. In response to these continuing problems, Congress passed the Railroad Revitalization and Regulatory Reform Act of 1976—the 4R Act.

B. PURPOSE AND MAJOR PROVISIONS

The 4R Act is approximately 150 pages in length and contains nine titles. In addition to the usual declaration of policy, there are provisions involving rail rates, ICC reform, mergers, financial assistance for improvements, an overall rail system plan, a northeast corridor project, continuation of local rail service, and studies of various rail matters. The 4R Act has been referred to as a deregulation statute for railroads. Although only a small part of this legislation addressed regulatory reform, it did authorize conducting deregulation studies.

A primary purpose of the 1976 Act was to augment previous legislation of the early 1970's, notably through specific and detailed provisions for.

120. D. Locklin, supra note 33, at 276.
121. Sampson & Farris, supra note 20, at 377.
124. Sampson & Farris, supra note 20, at 374, 376.
126. Id.
timings of rate changes, mergers, and abandonments, and with specified
dollar and percentage allocations of aid to the troubled rails. The Act dis-
tributed vast amounts of federal funds to the rails. For example, govern-
ment aid was to amount to $360 million during the first five years (1977-
1982).\footnote{Sampson & Farris, supra note 20, at 374-75.} The federal share started at 100\% and was to be decreased to
70\% in the last year.\footnote{Id.} Via this act, Congress allocated $1.75 billion to
AMTRAK to buy and improve track in the northeastern corridor of the
United States, $2 billion to CONRAIL so it could purchase facilities from
northeastern rail owners, and a fund of $1 billion in loan guarantees and
$600 million in redeemable shares to assist national rail revitalization.

The 4R Act attempted to improve certain aspects of rail rate making.
Railroads were given increased freedom to raise or lower their rates, particu-
larly with respect to variations in seasonal and regional demands of ship-
ners. In addition, the Act tried to encourage separate pricing methods for
different rail services.

C. ENTRY/EXIT PROVISIONS

The 4R Act gives the Secretary of Transportation a key role in approv-
ing rail merger applications, including negotiation and ICC testimony. An
alternative set of merger procedures is also established by section 403.
The section states that the Secretary should consider several factors when-
ever studying a rail merger proposal: (1) geographic rail needs; (2) effect
on rail and intermodal competition; (3) environmental impact; (4) effect on
employment; (5) cost of modernizing rail facilities; (6) rationalization of the
rail system; (7) impact on shippers, consumers and rail employees; (8) ef-
effect on communities; and (9) prospects for improving service.\footnote{4 R Act, \S 403, 90 Stat. 65 (current version at 49 U.S.C. \S 11350 (Supp. V 1981)).}

The 4R Act provided that a railway must submit a diagram of its sys-
tem to the ICC to identify those lines which are potentially subject to aban-
donment. No line is allowed to be abandoned until it is included on the list
for a duration of four months. The ICC must postpone abandonment if any
financially responsible entity, including a state government, offers sufficient
monetary aid to continue the service which will contribute to a line’s revenue
less its avoidable costs, including a reasonable profit on the line’s value.\footnote{Id. \S 802, 90 Stat. 129 (current version at 49 U.S.C. \S\S 10904-10905 (Supp. V 1981)).}

The 4R Act required the ICC to expedite its processing of merger and
abandonment applications to determine if they are in the public interest. In
the case of abandonments, the ICC must first find that the PC\&N will permit
the abandonment or discontinuance before any offer of subsidy may even
be considered. In abandonment applications the burden of proof as to PC&N is on the applicant. The procedure and times are shown in Table 1.

<table>
<thead>
<tr>
<th></th>
<th>TIME LIMITS FOR ENTIRE ABANDONMENT PROCESS, 4R ACT</th>
</tr>
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<tbody>
<tr>
<td>1</td>
<td>Notice of Intent to Abandon .......................... Published and posted at least 30 days prior to filing of application. Served at least 15 days prior to filing of application.</td>
</tr>
<tr>
<td>2</td>
<td>Application filed ................................. 60 days prior to proposed effective date.</td>
</tr>
<tr>
<td>3</td>
<td>Commission’s order to investigate .................... During the 55-day period subsequent to filing.</td>
</tr>
<tr>
<td>4</td>
<td>Issuance of certificate in unopposed case ............ By 60th day of filing.</td>
</tr>
<tr>
<td>5</td>
<td>Effective date of certificate in unopposed case ..... Possibly 90 days after filing of applications if no offer of subsidy received or longer if certificate is so conditioned.</td>
</tr>
<tr>
<td>6</td>
<td>Evidentiary proceedings in opposed case .............. 180 days from time evidentiary proceeding is designated</td>
</tr>
<tr>
<td>7</td>
<td>Initial Decision...................................... 120 days after completion of evidentiary proceeding.</td>
</tr>
<tr>
<td>8</td>
<td>Publication in Federal Register of findings of PC&amp;N ......................................................... When initial decision is administratively final.</td>
</tr>
<tr>
<td>9</td>
<td>Offer of subsidy ...................................... Within 15 days of publication in Federal Register of findings, if not made earlier.</td>
</tr>
<tr>
<td>10</td>
<td>Commission’s determination whether offer meets statutory criteria .................. Within 30 days of publication of findings in Federal Register.</td>
</tr>
<tr>
<td>11</td>
<td>If offer meets statutory criteria .......................... Issuance of certificate postponed for up to six months for negotiation of offer.</td>
</tr>
</tbody>
</table>


D. ECONOMIC EVALUATION

The 4R Act of 1976 is a continuation of previous policy toward entry and exit, although its provisions are more specific than prior, looser legislation. A sense of frustration and urgency can be noted from the various sections, such as the three distinct sections designed to expedite ICC decision making regarding rate changes, mergers and abandonments. A dual
policy is pursued by Congress, one which preserves entry of established firms while permitting the exit of only sufficient trackage to allow for the public interest to be served. It is a policy of careful calculation, albeit by non-mathematical means, to prevent absolute monopoly power from developing and to maintain the appearance of competition. The design of Congress in passing the 4R act, with respect to entry and exit, was apparently an attempt to solve the age-old dilemma for the rails: how can the nation have a viable competitive rail system in the face of excessive rail facilities at a time when economies of scale, the level of absolute costs, and shipper-passenger preferences for rival transport modes dictate that a tight oligopolistic structure is inevitable as opposed to a partial oligopoly of a few large carriers with a competitive fringe of smaller carriers? Congress chose to spend massive amounts of taxpayer dollars to encourage some marginal private funding and to allow additional concentration, via merger and abandonment, as a hoped-for solution to the rail transport dilemma.

IX. STAGGERS RAIL ACT, 1980

Unfortunately, the three rail acts of the 1970’s did little to solve the financial problems of the railroads. Of the three traditional modes of moving people and freight—air, motor and rail—the latter is the cheapest on a direct-cost basis. As a result of the actions of the OPEC oil cartel in 1973, the United States began an era of serious energy conservation. Efficiencies in heating, producing, distributing and transporting were promoted as national goals in order to control the consumption of petroleum. Transportation is a major user of fossil-fuel energy, so reducing petroleum consumption for carriage became extremely important in the late 1970’s.

A. BACKGROUND TO THE ACT

After nearly a century of government control of transportation, serious talk began to surface in the mid-1970’s about deregulating various modes of carriage. The Airline Deregulation Act of 1978 was enacted. Its alleged successes led to passage of the Motor Carrier Act of 1980, which reduced ICC controls over the trucking industry. Results of both statutes caused further difficulties for railroads. Congress, by its partial deregulation of air and motor carriers, fostered additional entry, lower rates and fares, and increased usage of these two not-so-relatively fuel efficient modes at a time when rational energy policy dictated a reduction in their use.

Several urgent problems arose in the late 1970’s. Railroads were still considered an essential mode of transportation, but intermodal competition

was strong and increasing. Congress undoubtedly realized that many regulations promulgated by government had become costly and burdensome. At a time when rail transport was needed to help combat energy shortages and inflation, the rail system continued to deteriorate and rail companies earned low rates of return on their investments in equipment. Congress predicted that the railroads would need increased earnings to modernize their facilities in light of an expected $20 billion capital shortfall. Given this situation, a dilemma arose: in a time of energy shortage, transport by rail is desirable because of its relatively low fuel cost per ton mile; however, with low earnings and deteriorating trackage and rolling stock, how can a viable rail system be restored and maintained? The Staggers Rail Act of 1980\textsuperscript{135} attempted to answer this question with a rational rail policy.

B. PURPOSE AND MAJOR PROVISIONS

The headnote to the Staggers Rail Act states that it is "[t]o reform the economic regulation of railroads."\textsuperscript{136} Broadly, the Act had two main purposes: to provide financial assistance to the railroads, and to eliminate unnecessary regulation. Congress hoped that rail corporations would earn revenues sufficient to allow them to refurbish their operating facilities and to provide continued service to the shipping and traveling public.

The Act has seven titles.\textsuperscript{137} The first title announces a rail transportation policy to promote competition and deregulation, safety and efficiency, sound economic conditions for carriers, reasonable rates and fair wages, energy conservation, and accurate cost accounting. The second title calls for vast changes in the way individual rail carriers establish their rates, chiefly by allowing, within bounds, some rate-setting freedom by carriers. Certain entry/exit provisions are also contained in title II. The third title constitutes an attempt to set up a uniform cost accounting system for railroads by establishing a Rail Road Accounting Principles Board, with a life of three years, to develop, implement and certify rail carrier accounting procedures. The fourth title addresses the matter of railroad modernization assistance by speeding up the abandonment procedure and by providing financial assistance for restoration, maintenance and upgrading of track and facilities. The fifth title amends the 3R Act of 1973 to provide for labor protection within the CONRAIL system, especially for fair treatment of displaced workers and their transfer and training. The sixth title also amends the 3R Act to allow a transfer of CONRAIL properties in Connecticut and


\textsuperscript{136} Id.

\textsuperscript{137} Id. § 1, 94 Stat. 1895-96.
Rhode Island. The seventh title contains provisions dealing with properties and employees of the now defunct Rock Island and Milwaukee railroads.

C. ENTRY/EXIT PROVISIONS

Although the 1980 Act treats rail regulatory reform mainly through the mechanism of changes in rate-making procedures, it contains several important entry and exit provisions. First, section 221 deals with railroad entry by increasing the difficulty for a competing railroad to deny track crossover permission whenever the ICC issues a certificate of PC&N for new rail line construction.\textsuperscript{138} Second, a provision in section 228 offers merger language to the ICC consistent with existing antitrust rules for evaluating mergers. Another provision allows the ICC to approve the application of a railroad to provide motor carriage prior to or subsequent to transport by rail in order to provide service to small communities. The main thrust of section 228 is its provisions for accelerating the time requirements for notice, evaluation, hearings and actions on rail carrier applications for consolidation, merger and acquisition. For example, the ICC must now evaluate and act on a merger proposal no later than 270 days after the initial notice is filed and published.\textsuperscript{139} Third, section 402 is aimed at streamlining the rail abandonment process. Procedures are established for accommodating outside financial assistance, though subsidy or sale, of prospective lines to be abandoned.\textsuperscript{140} The time period for filing, investigating and deciding a proposed abandonment proceeding is also shortened. Fourth, section 405 amends the 1976 4R Act by substantially increasing the amount of federal funding, possibly in excess of $3 billion, to be allocated to restoring and upgrading specific portions of the country’s rail system.\textsuperscript{141}

D. ECONOMIC EVALUATION

The 1980 Act is a rather comprehensive approach toward saving America’s rail network, at least those parts which might serve a significant share of shipping needs. The two primary features, infusing financial aid and streamlining abandonment procedures, interact to allow for entry of additional capital and for exit of redundant facilities. The net effect will undoubtedly be to create an even tighter oligopolistic rail industry structure than currently exists. Congress apparently believes that the benefits from technical efficiency, continued rail service to the public and energy conservation outweigh the disadvantages of decreased competition and increased concentration.

\textsuperscript{139} Id. § 11345.
\textsuperscript{140} Id. § 10905.
Entry and exit involve much more than the mere coming in and going out of a line of commerce. Among rails, not only is previous entry of existing firms preserved when exit is prevented, but some exit is facilitated when the entry of larger, more efficient units is allowed by merger, consolidation and acquisition. The 1980 Act allocates approximately $3 billion to the rail system, and invites additional funding from both private and public (state/local) sources where exit is imminent. These financial efforts, if successful, may prevent some exit but that in itself does not preserve present competitiveness because through merger any exit prevented could possibly be channeled into "entry" to create larger, more potentially powerful market participants.

The 1980 Act may have opened the door to a new sort of merger policy for carriers, namely, intermodal entry. Specifically, section 228 addresses the matter of motor transport prior or subsequent to rail carriage. Ostensibly, the purpose of this section is to serve shippers and the public interest in cases where merger and abandonment eliminate transportation services to small communities. In the face of continuing deregulation efforts, however, multi-modal carriage diversification may be the next step in the never-ending saga of the concentration of the nation's transport industries.

X. CONCLUSIONS

The nation's railroads have been in trouble for more than a century. Public sentiment against them began in the 1870's for exercising monopoly power over rates. By the 1970's, the shipping and traveling public had already been rejecting their services for many decades in favor of cheaper, faster or more convenient modes of transport. Part of the problems can be traced to entry and exit conditions in the industry itself.

A. SUMMARY

Federal regulation over the railroads did not begin until 1887 when "An Act to Regulate Commerce" was passed. The chronic financial conditions in the rail industry over the last fifty years is due to the excessive entry which occurred during the fifty year period prior, which in turn may be traced back to the misdirected regulatory effort begun in 1887. Congress created the ICC by the 1887 Act but gave it no specific powers over entry and exit. Although nearly two-thirds of the all-time high in rail track mileage that existed in 1916 had already been built in 1887, an entry-monitoring provision was not enacted. The only statement in the 1887 Act close to an entry or exit provision is a brief reference giving the ICC power to serve the

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142. Title changed to "Interstate Commerce Act" by the Transportation Act of 1920. See supra text accompanying notes 29-46.
public interest. Although this ostensible license to control rail carrier entry and exit existed, it was not until thirty-three years later that Congress gave specific attention to these two matters.

Entry into railroading was not regulated by the federal government until the Transportation Act of 1920 was enacted. That legislation required a certificate of PC&N to be obtained from the ICC before new interstate rail lines or extensions could be constructed. This provision was ineffective because most of the track had been laid in this country by 1916. Since 1920, approximately 69,000 miles of track have been abandoned while less than 10,000 miles have been constructed. This new construction has usually been for very short distances and mainly to serve the establishment of new businesses. Entry control has not been a prominent feature of rail carrier legislation in this country since 1920.

An interesting twist to entry is given by the consummation of mergers, acquisitions, consolidations and combinations. The uniting of two already established rail companies is a unique aspect of entry insofar as it creates a newer but larger enterprise. The 1920 Act encouraged the polygamous marriage of smaller carriers into large companies, albeit at the behest of ICC design and coordination, but this feature was later discarded. Congressional action and ICC concern over mergers have continued throughout the years. Every major piece of rail legislation since 1920 has contained either a corrective or a creative provision concerning mergers. Each time Congress has passed a statute dealing with rail mergers, additional provisions have been included in order to encourage, subsidize, regionalize and reorganize mergers so that efficient, viable and adequate rail transport companies would be created. The result, however, has been to systematically create over time an oligopolistic structure through the allocation of billions of taxpayer dollars, rather than achieve the competitive ends sought.

The 1920 Act gave the ICC control over abandonment of tracks; thus, the entire provision of service by an existing railroad line was placed under ICC control. This power applied to interstate as well as intrastate abandonment. The ICC has permitted abandonment when its balancing test indicates that losses to carriers would be greater than benefits to the public if the lines were kept in operation. This test has been used through the years, although the specific factors considered for losses and benefits have varied. The abandonment process has suffered because of lengthy delays, but it has been accelerated by ICC practices, a court ruling, and the 4R Act of 1976.

143. See supra text accompanying notes 47-70.
144. HISTORICAL STATISTICS, supra note 1, at 728-29.
The Great Depression spawned additional legislation to avert rail failures by amending rate-making procedures and by encouraging mergers. The emergency 1933 Act\(^ {147} \) was another step in the creation of an oligopolistic tendency in railroading. In fact, that legislation created a structure which brought rail companies together with government to create mergers and to divide markets. The scheme was confined to rails, however, and non-rail holding companies were discouraged from participating in such combinations. Fortunately, these features did not work as planned. The coordination provision expired in 1936 and the Transportation Act of 1940\(^ {148} \) provided additional merger freedoms for rail carriers and gave the ICC additional powers to ascertain that mergers occurred among legitimate railroad companies.

With the Transportation Act of 1958,\(^ {149} \) Congress and the ICC began to focus on another form of exit—discontinuance of rail passenger service. Mergers apparently were not considered to be an important policy alternative at the time because the 1958 Act said little about them. What was important, however, was the strengthening of ICC powers over rates and intermodal competition. In this regard, Congress continued to perpetuate its earlier policy from the 1940 Act of trying to achieve competitiveness via large numbers of intramodal carriers in separate industries, rather than looking at all modes of transportation as a sector of interdependent industries. Nevertheless, the new policy allowing rails to discontinue already approved passenger service ushered in an era of concern and action.

Three key legislative acts in the 1970's\(^ {150} \) dealt firmly, but incompletely, with entry and exit. By combining ratemaking, mergers, abandonment, governmental coordination and financial assistance provisions in these three acts, Congress was able to increase rail carrier size, provide funding for rail renovation, reduce inefficient rail operations and create a centrally monitored (but segmented) regional rail system. AMTRAK and CONRAIL may be harbingers of the path to follow: entry of oligopolistic firms by government-sponsored merger; exit of duplicative, inefficient lines by abandonment and discontinuance; and entry of additional rail capital with taxpayer dollars to augment the oligopolistic structure.

Finally, via the Staggers Rail Act of 1980,\(^ {151} \) by relaxing rail carrier rate-making procedures, and by accelerating time requirements for rail carrier requests to ICC concerning mergers and abandonments, Congress is

\(^{147}\) See supra text accompanying notes 72-83.
\(^{148}\) See supra text accompanying notes 84-98.
\(^{149}\) See supra text accompanying notes 99-115.
\(^{151}\) See supra text accompanying notes 132-41.
proceeding toward the end suggested above. It is not a competitive and private-enterprise market solution, but it is also not true socialism. Whenever a federal government sponsors, subsidizes and coordinates largely private operations, government ownership and operation are not involved. Mercantilism and fascism characterize these kinds of relations.  

B. INDUSTRY ECONOMICS APPRAISAL

Entry and exit concepts from industry economics can be used to explain their counterparts in transport regulation. Economies of scale, absolute costs and product differentiation relate indirectly to the use of certificates of PC&N, mergers, abandonment and discontinuance for rail transportation.

1. ECONOMIES OF SCALE

Scale economies exist in rail transportation. Apparently, the LRAC is L-shaped in railroading. The limitation of certificates of PC&N to only very short distances fosters scale rather than inhibits it by allowing a given carrier to add to its existing line, rather than by creating separate carriers for short routes. Mergers, including combinations, consolidations and acquisitions, also foster economies of scale by creating larger companies. Abandonments and discontinuance aid scale economies only to the extent that marginal adjustments downward in plant size tend to lower overall costs of operation, but do not create larger, more efficient units per se. Probably the most scale-inducing policy has been that of allowing mergers. Not until recently, however, have previously restricted merger policies been relaxed so that economies of scale could be experienced more fully. This hesitancy by Congress and the ICC has been costly to both the railroads, causing them to operate at high costs, and to society by causing higher rates to cover costs, lost usage of facilities and wasted resources. Economies of scale may even have been a barrier to exit in the railroad industry because the high fixed costs of a railroad, compared to its variable costs, cause a company to remain in the industry as long as out-of-pocket expenditures can be recovered.

2. ABSOLUTE COSTS

Absolute costs do not refer to the extremely high costs of entry. Absolute costs refer to whether an entrant's costs are significantly higher than those of existing firms even when both entrant and established firm are of the same capacity. Except for selected commuter lines, no important entry

of a completely new extensive interstate railroad has occurred for more than fifty years. Most of the new entry of capital has been by established firms in the form of extensions or construction of track for short distances. As a result, it is difficult to compare the absolute cost advantages of existing rail companies with the absolute cost disadvantages, if any, for potential competitors.

During the period of rapid entry into railroading in the 1880-to-1916 period, few absolute cost disadvantages for entrants apparently existed. Absolute costs are analyzed as an entry barrier if their presence operates to deter prospective firms from coming into an industry. Wherever entry is rapid, and few barriers exist, economists ordinarily conclude that entry conditions are not encumbered by technical economic factors. In some lines of commerce, absolute costs for entrants might be higher than for established firms if patents and permits are needed to become viable in the market. The certificate of PC&N may be evaluated as an absolute cost entry barrier to the extent that the costs of applying and paying for the permit would place the entrant at a significant cost disadvantage compared with existing firms. This cannot be evaluated, however, in the rail industry because there are no long, or even short, lines of investors eagerly applying to get into the business. This same reasoning can apply to exit in terms of the costs of applying for and obtaining permission to abandon or discontinue service. For acquisitions, there is no doubt that legal, accounting and other fees make merging costly, and therefore burdensome, for the combining parties. Whereas the cost-lowering efficiencies of a merger probably more than offset any special costs of merging, many factors other than cost reduction may motivate mergers.

3. **PRODUCT DIFFERENTIATION**

Product differentiation as a barrier to entry implies that consumer preferences for the output of established firms are so strong compared to what entrants have to offer that an entrant company finds it difficult to sell its output at profitable prices. A steady growth in shipper and passenger preference has occurred for air and motor carrier transport to the detriment of railroads for several decades. Even if there had not been excessive entry into railways prior to 1916, product differentiation barriers to entry most likely would deter investors from entering the railroad business today. The shift of shipper/passenger preferences away from rail carriage toward air and motor carriers helps to explain the fact that more track has been abandoned and more service discontinued than new lines constructed and new service offered by the rails in the past sixty years. Abandonment and discontinuance are a direct, but not the only result of product differentiation as an economic factor in the rail industry. Air and motor carriers are able to differentiate their services significantly from rail carriers on the basis of con-
venience, speed, comfort and special services. Even if the fares and rates per ton-mile were the same for all modes, rails would be at a product differentiation disadvantage compared to air and motor carriers. Because of a partial, relative product differentiation disadvantage for rail service, the business of those carriers has decreased, thereby leading to petitions to abandon, discontinue, and merge in order to combat the increasing consumer preferences for air and motor transport.

C. IMPLICATIONS

Controlling entry via permit or operating certificate is not new. Indeed, it is an old mercantilist practice used in the sixteenth and seventeenth centuries in England, France and Spain.\(^\text{153}\) It can be traced back in elemental form to the guilds of the feudalist era.\(^\text{154}\) Its avowed purpose has always been, usually under the guise of health, safety and well-being, to thwart free and open competition and to protect established firms from the erosion of their custom from upstart potential entrants. American public policy makers have retained this impediment to competition for more than a century. It is encountered every day by people in the ordinary walk of life, chiefly in the form of occupational licensure. Barbers, dentists, lawyers, physicians, real estate agents, stock brokers and public accountants are but a few examples of the dozens of licensed occupations operating in our economy.\(^\text{155}\) It was not until 1920 that Congress allowed the mercantilization of transport by passing special legislation. Since that time, additional statutes have been passed to correct the mistakes and abuses of previous laws and their administration. In the 1970's, the United States entered into an internal self-styled revolution, similar to its reaction against the mercantilist excesses of King George III, by deregulating some of what it has regulated for fifty to one hundred years.

Although air, motor and rail carriers have all been subjected to deregulating legislation, the future is unclear as to which ideological mold the railroad industry might be placed. Classical competition is probably unworkable because of economies of scale and product differentiation. Mercantilism has not worked because the industry continues to suffer after decades of governmental regulation, subsidy, franchise and protectionism. Perhaps socialism is the answer: allow for entry of a giant nationalized rail company with the exit of all duplicative and excessive trackage, equipment and rolling track. Alternatively, perhaps the trackage should be nationalized and private rail carriers bid on and pay rental fees for its use. The U.S. is ideologically committed to free enterprise and the competitive market.

\(^{153}\) W. Minchinton, Mercantilism vii-xii (1969).
\(^{155}\) C. Wilcox, Public Policies Toward Business 4-13 (1966).
This commitment will probably cause public policy makers to continue to provide piece-meal subsidization of private rail companies from the public largesse rather than radically restructuring the tired, worn-out railroads.
Entry Controls on Regulated Household Goods Carriers: The Question of Benefits

EDWARD A. MORASH*

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I. INTRODUCTION

Recent research on the theory of regulation has emphasized the economic-political nature of the regulatory process.¹ Similarly, the beneficiaries of regulation under varying conditions and assumptions have also been considered.² As two specific cases of this theoretical focus, the "consumer-protection" and "producer-protection" orientations identify two potential beneficiaries of regulation. At one extreme, the "public interest" or "consumer-protection hypothesis" purports that regulation benefits consumers by ensuring high levels of service to the public and lower prices resulting from firm efficiencies. In contrast, the "capture" or "producer-protection hypothesis" predicts that regulation, and in particular, entry control, restrains competition, raises the prices of services, and allows firms to achieve monopoly gains. However, even some proponents of the "producer-protection hypothesis" concede that service performance to the public may be enhanced. This recognition stems from the contention that when rate competition is restricted, firms may compete away excess profits by offering excessive services.³

This paper will examine the beneficiaries and benefits of regulation for one particular segment of the motor carrier field, the household goods (HHG) moving industry.⁴ Because of the importance of service performance in this market, the interstate HHG moving industry has been the most heavily regulated segment of the entire surface transportation arena.⁵ In turn, service performance is particularly important in the HHG market because of certain demand characteristics relating to the personal and non-repetitive nature of the service, the high emotional value attached to shippers' personal belongings, the relatively uninformed status of many individual consumers, and the dispersed locations of shipment origins and destinations. In a sense, the importance of service performance and the heavy regulation of this industry provide a crucial test of the "consumer protection hypothesis."

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4. The market for HHG moving services is basically a distinct industry. For a discussion of this point, see G. Wilson, Essays On Some Unsettled Questions In The Economics Of Transportation 24-29 (1962); and B. Chow, The Economics Of The Motor Freight Industries 43-46 (1978).

The specific focus of this study was to empirically investigate the effects of regulatory entry controls on HHG firm size, operating efficiency, and the quality of carrier service performance. While prior empirical studies have investigated the effects of regulatory entry controls on carrier rate levels (see, for example, studies listed in notes 2 and 3), this study builds on previous research by emphasizing the relationships between entry controls and the quality of firm service output. Unfortunately, the Household Goods Transportation Act of 1980\(^6\) did not deal with the basic structural issue of entry controls but rather focused on symptomatic concerns of consumers such as binding estimates and shipment weighing procedures.

Since entry barriers in the HHG moving industry generally take the form of restrictions on carrier certificates, a brief review of these HHG restrictions is warranted.

A. ENTRY CONTROLS — RESTRICTIONS ON CARRIER OPERATING AUTHORITIES

To provide services in a given transportation market, HHG carriers must obtain a "certificate of public convenience and necessity"\(^7\) from the Interstate Commerce Commission, and the contemplated service must not be restricted by the authority. Presently, only twenty-seven carriers hold nationwide authority from the Interstate Commerce Commission to serve most points in the United States.\(^8\) However, a number of these carriers can only provide "nationwide" service by tacking together numerous separate grants of authority.\(^9\)

In the interstate HHG moving industry, there are three major features of HHG carrier certificates which make the authorities more or less restrictive in nature and which may, therefore, create barriers to carrier entry and market expansion. First, the number of states specified in the certificate either restricts the carrier to a limited market area or permits a wider scope of geographical operations. Generally, a broad grant of authority means that a carrier can serve many different states. Since the origins and destinations of household goods shipments tend to be geographically dispersed, a broader authority makes it possible for the carrier to enjoy both enlarged market areas and increased lengths of haul.

Secondly, the distinction between radial and non-radial operating au-

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7. This paper treats the terms certificates, operating authorities, and operating rights as synonymous.
According to the text, the radial authority also relates to the restrictiveness of carrier certificates. A radial type authority, being more restrictive in nature, requires that a carrier conduct operations between the base area (or hub) and the prescribed destination area. Thus, a radial authority is similar to a "bicycle wheel," where the hub is the base or origin area and where the wheel spokes emanate out from the hub to the destination area. For example, with Washington D.C. as the base and Maryland, Delaware, and Virginia as destination points, only movements between Washington, D.C. and points in Maryland, Delaware, or Virginia would be authorized. No "cross-hauling" would be permitted between the three named states nor within the base area. As a result, a radial type authority makes it more difficult for a carrier to consolidate shipments in the same vehicle for increased load factors.

In contrast, a non-radial authority is less restrictive in nature since it authorizes a carrier to operate between any points named in the certificate. For example, "between points in Maryland, Delaware, Virginia, and the District of Columbia" would allow cross-hauling between any of the named points without requiring operations through a base area. As the least restrictive type of operating authority, a non-radial nationwide certificate would state simply, "between points in the United States."

A third type of limitation for radial authority relates to the size of the base area. The base area for a radial authority can be as small as one town, or in some cases, as large as several states. In essence, the smaller the base area, the more difficult it is to obtain return movements for increased average load factors, particularly since the destinations of HHG shipments tend to be dispersed. For example, a radial authority between Washington, D.C. and California would not authorize return movements from California to Maryland, Virginia, or any points in between (unless specifically mentioned in the certificate). Furthermore, if the authority specifies "from Washington, D.C. to California" instead of "between," no backhauls would be authorized in any event. This latter type of backhaul restriction is, however, gradually being removed as a result of both national concern over energy consumption and the Motor Carrier Act of 1980.

In some cases, carriers can partially compensate for some of the preceding certificate restrictions by "tacking" together separate grants of authority. If authorized, this joining of different authorities would allow for increased carrier market areas, through movements, and improved shipment consolidation and backhaul opportunities. However, "tacking" of

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10. In communications with I.C.C. legal staff, it was indicated that the early Commission intent was to refrain from issuing radial certificates with large base areas. However, some HHG carriers ended up with base areas of several states anyway. See also Breen, supra note 3, at 161.


12. The average number of separate grants of authority held by an individual HHG carrier is 1.5 (total number of authorities divided by total number of carriers). See Breen, supra note 3, at
authorities must be at common points in the certificates and the involved certificates must contain no prohibition against "tacking." Furthermore, no "cross-hauling" in the base or destination areas of radial authorities is permitted. It is also noteworthy that in the aftermath of the HHG Act and the Motor Carrier Act of 1980, the three major types of restrictions discussed in this section are also consistent with the increased possibility of new entrants. Thus, these particular restrictions are almost invariably placed on carrier applications for new HHG operating authority.

II. METHODOLOGY

The principal focus of this study is to identify the relationships between the restrictiveness of carrier certificates and firm size, operating efficiency, and service quality. The research approach involved three phases. First, an Interstate Commerce Commission listing was obtained of all 332 Class I and II carriers who were significant movers of HHG shipments.\textsuperscript{13} Similarly, the HHG industry's 109 agency systems were identified from a second ICC listing. Although the agency systems represent only about one-third of all Class I and II HHG carriers, they account for over eighty percent of all industry shipments.\textsuperscript{14} For the purposes of this study's analysis, these agency carriers were also broken down into small agency systems (less than seventy-five agents) and large agency systems (more than seventy-five agents). Thus, statistical comparisons could be made of the operating authority, size, operating efficiency, and service performance characteristics of carriers with no agents, small agency systems, and large agency systems.

The second research phase involved obtaining information on the restrictiveness of carriers' operating authorities. Since most interstate HHG carriers belong to one of two rate bureaus, this certificate information was obtained from the "Participating Carrier and Scope Tariffs" of the industry's two major rate bureaus — the Household Goods Carriers' bureau, and the Movers' and Warehousemen's Association of America. Of the complete universe of Class I and II HHG carriers (332), it was found that ninety-one percent (301) belonged to one or the other rate bureau. Thus, certificate information could be obtained for these carriers. The remaining in-

\textsuperscript{16} By way of comparison, a general commodities carrier holds an average of 14 separate authorities. C. TAFF, COMMERCIAL MOTOR TRANSPORTATION 439 (1980). It would therefore appear that the tacking option is less feasible for most interstate HHG carriers when compared to general commodities carriers.

\textsuperscript{13} As of 1980, the I.C.C. has redefined Class I motor carriers as those with annual operating revenues over 5 million dollars, Class II carriers as those with revenues between 1 and 5 million dollars, and Class III carriers as those with annual revenues less than 1 million.

\textsuperscript{14} Morash, supra note 7, at 38.
dependents (nine percent) were found to be small localized or short-haul carriers.

In the third phase, measures of carrier service performance, financial performance, and operating efficiency were obtained from carrier reports on file at the Interstate Commerce Commission. The service performance measures are reflected by the "Annual Carrier Service Performance Reports" while financial and operating statistics appear in the "Carrier Annual Financial Reports." For the service and financial performance measures, two years of data were utilized to better indicate the strength of statistical relationships.

III. FINDINGS: RESTRICTIVENESS OF OPERATING AUTHORITIES

A. FIRM SIZE AND CONCENTRATION TENDENCIES

A comparison was made of the operating authority characteristics of HHG carriers with no agents, carriers with less than seventy-five agents, and HHG agency systems with more than seventy-five agents. The major finding was that the less restrictive the operating authority, the larger the agency system. As Table 1 indicates, the larger agency systems with at least seventy-five agents have more states in their authority (an average of forty-five) and the authority tends to be non-radial (less-restricted). When their authority is radial, these same carriers have more average states (thirteen) in the hubs of all authorities held. However, only about one-fourth of these large agency systems hold predominantly radial authority (nine of the thirty-five in Table 1).

In contrast, for both carriers with no agents and smaller agency systems, almost eighty percent of the carriers hold primarily radial authority (157 of 201 and 50 of 65 respectively in Table 1). Furthermore, for carriers with no agents, the average size of the radial hubs is less than one state (.86, Table 1) while for small agency systems, the hubs average slightly less than two states (1.98).

The implications of these findings are several. First, the existence of an unrestricted grant of operating authority is a major impetus for carrier development of a large agency system. The reason for this impetus is simply that with the increased number of agents, carrier revenues are also increased. Thus, Table 1 shows that the average operating revenue of large agency systems with unrestricted operating authority is substantially above the average operating revenues of both carriers with no agents and small agency systems. Furthermore, the four largest agency systems in the U.S., all of which have nationwide, non-radial authority, account for approxi-
mately fifty percent of HHG industry revenues.¹⁵

A second implication of these results is that carriers with restricted or no interstate operating authority may have little alternative but to become agents for carriers with broad and less-restricted grants of authority. Simi-

| TABLE 1 |
| Certificate Restrictions and Carrier Size by Type of HHG Carrier |
| Carriers with No Agents | Small Agency Systems (Less than 75 agents) | Large Agency Systems (75 Agents or more) |
| Variables⁸ | Mean | Mean | Mean |
| A. Restrictiveness of Operating Authority |
| 1. Number of states in operating authority | 11 | 24 | 45 |
| 2. Tendency to non-radial authorityᵇ | 1.52 | 1.54 | 3.12 |
| 3. Number of states in all hubs if radial authority type carrierᶜ | .86 | 1.98 | 13 |
| (N=15.7) | (N=50) | (N=9) |
| B. Carrier Size |
| 1. Revenues — average carrier operating revenues in thousands | $1,570 | $2,163 | $29,609 |

Sources: Movers' and Warehousemen's Association of America and Household Goods Carriers' Bureau Participating Carrier and Scope Tariffs with updating supplements; Carrier Annual Financial Reports (on file at I.C.C.).

a. For all variables, the differences between means are statistically significant at the .01 level, which indicates that the odds are only one out of a 100 that the differences are due to chance.

b. This variable was coded: (1) radial with additional restrictions; (2) radial with no additional restrictions; (3) non-radial restricted; and (4) non-radial with no restrictions, for the predominant type of carrier authority.

c. A carrier may hold more than one radial authority.

incentive to become an agent. It is also noteworthy that many of the non-agency carriers and small agency systems in Table 1 also serve as agents for the largest agency systems when they operate beyond the scope of their own operating authorities. Thus, as both a carrier and agent, they are termed "carrier-agents." In this study, even a twenty-eight state carrier was found to serve as a carrier-agent for a fifty state carrier when the carrier-agent lacked the requisite operating rights.

While these industry conditions raise the revenue generating capabilities, and possibly the market shares of the larger agency systems, they also reduce the revenues and profits of both agents and carrier-agents. For example, for the privilege of using the principal carrier's certificate, the agent must pay a royalty of five-to-ten percent of the shipment revenues. Furthermore, most agency contracts require that the agent "exclusively" represent the parent company. For carrier-agents, some principal carriers also require that they surrender or place in escrow their own certificates; this tendency has increased after enactment of the Motor Carrier Act and the Household Goods Act of 1980. This latter requirement prevents the carrier-agent from using his or her own operating authority in those instances where it would be both legal and operationally feasible. In sum, these conditions are a major reason why at the time of enactment of the Household Goods Transportation Act of 1980, only about 1000 of the over 2500 certificated interstate HHG carriers were found to be conducting any operations at all with their own certificates.

Thus, the regulatory market barriers created by restrictive operating authorities may foster the development of large HHG agency systems along with concomitant industry concentration. In particular, these artificial entry barriers may encourage nonrestricted carriers to develop agency systems and restricted carriers to join them. Whether this regulatory effect is a desirable result will be subsequently discussed.

16. If a carrier's authority is not too restricted, interlining, or the transfer of shipments between carriers, provides a second, although less than ideal alternative. Interlining appears to be primarily a way to combine broad though somewhat restricted grants of authority. For example, in this study, 18 carriers who interlined significant amounts of tonnage (at least 1000 tons annually) were found to have an average of 31 states in their authority. However, their authority tended to be radial (1.67 or 14/18 carriers) with an average of five states in the hubs of all radial authorities held (compare with Table 1).


18. Id. at 640.


B. Efficiency of Firm Operations

A number of economists have provided evidence that what "apparent" economies of scale exist in motor carrier operations relate primarily to the average length of haul and to improved load factors. For HHG carriers in particular, Table 2 indicates that the large agency systems exhibit both significantly longer average lengths of haul and higher average load factors. Furthermore, the large agency systems achieve lower carrier operating ratios, a common measure of carrier financial health. A lower operating ratio reflects a lower percentage of operating expenses to operating revenues, and would also appear to reflect efficiencies in operations of the large agency systems.

Table 2 also superimposes the restrictiveness of operating authorities on these results. Viewed in this light, the apparent operating efficiencies of the large agency systems may be directly related to regulation and the restrictiveness of operating rights. First, large agency systems with more states in their certificates are able to achieve longer average lengths of haul. Second, given the geographically dispersed nature of HHG shipments, carriers with non-radial authority are better able to consolidate shipments in the same vehicle for improved load factors. Third, a non-radial authority, or a radial authority with a large base area, increases the likelihood of return movements. Return movements would serve to increase average carrier load factors. In total, the broad and generally non-radial certificates of large agency systems facilitate their ability to concentrate on the desired lengths of haul, to consolidate shipments, to obtain balanced movements, and to provide through movements without interlining (shipment interchange with other carriers). In contrast, the narrow radial authorities of carriers with no agents and small agency systems limit their opportunities for economical operations and create another incentive for agency participation.


22. These results are even more pronounced if either "return on equity" or "return on total assets" is used as the measure of financial performance. For example, the average return on equity for the largest agency systems was found to be 32% which was substantially above the returns for other carrier groups. This is because most of the fixed-assets of the large agency systems are provided by both agents and carrier-agents, which reduces the principal carriers' fixed investment costs. Thus, with a lower investment base, relative carrier returns would also increase.
### Table 2

**Efficiency of Carrier Operations by Type of HHG Carrier**

<table>
<thead>
<tr>
<th>Variablesa</th>
<th>Carriers with No Agents (N=201)</th>
<th>Small Agency Systems (N=65)</th>
<th>Large Agency Systems (N=35)</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>Mean</td>
<td>Mean</td>
<td>Mean</td>
</tr>
<tr>
<td>A. Restrictiveness of Operating Authorityb</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>1. Number of states in operating authority</td>
<td>11</td>
<td>24</td>
<td>45</td>
</tr>
<tr>
<td>2. Tendency to non-radial authority</td>
<td>1.52</td>
<td>1.54</td>
<td>3.12</td>
</tr>
<tr>
<td>3. Number of states in all hubs if radial authority type carrier</td>
<td>.86</td>
<td>1.98</td>
<td>13.0</td>
</tr>
<tr>
<td>B. Efficiency of Carrier Operations</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>1. Average haul in miles</td>
<td>500</td>
<td>680</td>
<td>960</td>
</tr>
<tr>
<td>2. Average load in tons</td>
<td>3.3</td>
<td>4.2</td>
<td>4.6</td>
</tr>
<tr>
<td>3. Carrier operating ratio(c)</td>
<td>103.12</td>
<td>100.21</td>
<td>98.51</td>
</tr>
</tbody>
</table>

**Sources:** Movers' and Warehousemen's Association of America and Household Goods Carriers' Bureau Participating Carrier and Scope Tariffs with updating supplements; Carrier Annual Financial Reports (on file at I.C.C.).

a. For all variables, the differences between means are statistically significant at the .01 level.

b. Higher numbers are less-restricted.

c. Carrier operating expenses as a percentage of gross revenues. Two-year carrier averages were utilized.

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The apparent operating efficiencies of the large agency systems appear to be at least partly regulation induced rather than inherent in increased carrier size. Since these operating efficiencies are not available to carriers with restricted authorities, another incentive exists for these restricted carriers to join large agency systems. Again, the artificial regulatory barriers created by certificate restrictions may be a major impetus for industry reliance on large agency systems for shipment movements. While in specific instances there may be operational advantages associated with agency participation (e.g., traffic corridors of low density), the point here is that regulatory entry controls encourage agency involvement. The desirability of these conditions will be considered in a subsequent section of this paper.
C. Firm Risk

Although the preceding revenue increasing capabilities and operating efficiencies of the large agency systems appear to be partly regulation-induced, the question might be raised as to why these large agency systems with unrestricted operating certificates do not perform the actual tasks themselves. For example, a number of the largest carriers own virtually no equipment or warehouses and directly employ no drivers. It would seem that by relying on agents and owner-operators to provide the equipment, local offices, and warehouses, principal carriers with broad grants of authority would be foregoing increased revenue and return (profitability) possibilities. For example, Table 3 shows that the large agency systems forego packing and warehousing revenue and pay out a large percentage of the revenue dollar for agency fees and purchased transportation.

The answer to this paradox relates to carrier risk. Essentially, an agency system allows the carrier to both enjoy higher returns while at the same time reducing carrier risk. In addition, this risk reduction takes several forms:

1. Investment risk — By providing the fixed assets, agents assume the investment risk.

2. Financial risk — Since these fixed assets are usually financed partly by debt instruments, agents also assume the financial risk associated with increased leverage. In fact, an agency system can possibly be viewed as a means for increasing system leverage without attendant carrier financial risk.

3. Operating risk — By reducing the proportion of carrier fixed costs to variable costs, an agency system transfers operating risk from the principal carriers to their agents. Consequently, carrier returns are less sensitive to changes in system revenue since most costs are variable.

4. Credit risk — Since agents usually extend credit directly to shippers, the principal carriers’ credit risk is also reduced. Thus, if a shipper defaults, the agent is often held responsible.

5. Market risk — Since principal carriers can legally adjust the revenue divisions for agents, owner-operators, and themselves, usually without regulatory interference, the principal carrier’s market risk can be reduced.

6. Risk diversification — An agency system is itself a form of risk diversification. Given a fixed market area, an increased number of agents makes it more likely that the poor sales performance or bankruptcy of some agents will be counterbalanced by the superior sales performance of other agents.

All of these conditions create a stability in both the revenues and returns of principal carriers, and may create another regulatory incentive for carrier development of a large agency system. As previously outlined, some restricted carriers may have little alternative but to become agents for large unrestricted carriers. Thus, risk considerations mitigate against principal carriers obtaining maximum return potentialities, since reliance on
agents reduces a principal carrier's risk. Similarly, a large agency system allows a carrier with broad and unrestricted authority to enjoy both higher returns and lower risk compared to carriers with narrow and restricted authorities.

IV. PRICE LEVELS AND SERVICE QUALITY

All of these industry conditions might not be of particular import if industry price levels and service quality were at efficient levels. As has been suggested, "the public might still benefit from the higher operating costs of restricted carriers as well as from the administrative costs of regulation itself if these costs are more than offset by the induced economies of utilization for the less-restricted carriers that become large firms." 23 However, regu-

lation must also ensure that these large carrier savings are passed on to the public in terms of lower transportation prices and/or improved services.

A. Price Levels

Unfortunately, recent research on the HHG moving industry has provided evidence that interstate HHG prices are higher than what they would be in a free entry environment. Thus, Breen estimates that interstate HHG rates are twenty-five to forty percent higher than HHG rates for comparable intrastate movements.24 Based on efficiency criteria, these elevated prices would be cause for concern.25 However, service performance to shippers might also be aggrandized. As Nelson observes:

Although supporters of current regulation do not emphasize that the process inevitably leads to lower unit costs and rates, they do strongly claim that it results in improved service, greater financial responsibility to shippers, and greater public safety on the highways.26 While heightened carrier service could be more than what shippers would be willing to pay for if afforded other options, at least shippers might receive some benefit from the improved service.

B. Service Quality

In this study, the service performance of HHG carrier groups with restricted and unrestricted authority was analyzed. A statistical comparison was made of the service performance of the non-agency carriers and small agency systems with restricted operating authority and the large agency systems with primarily unrestricted authority. The service performance measures related to timely pickup and delivery of shipments, correct estimation of charges, claim-free shipments, and expeditious handling of claims.27

Table 4 presents the results of the service performance comparisons for the carriers with restricted and unrestricted operating authority. Surprisingly, the largest agency systems with the unrestricted authority exhibit in-


25. Until the passage of the HHG Transportation Act of 1980, the rates for all HHG carriers were virtually identical. See Breen, supra note 3, at 156. This may have been due to the existence of only two major rate bureaus in the industry (the Household Goods Carriers’ Bureau and the Movers’ and Warehousemen’s Association of America) and the fact that almost all interstate Class I & II HHG carriers belong to one or the other of these rate bureaus. In the aftermath of the HHG Act, with its encouragement of innovative carrier pricing initiatives, a few carriers have begun to file independent rate applications. However, the HHG Act did not deal with regulatory entry controls or the rate bureau process.


27. Service quality can be viewed as a second output of the firm. See White, Quality Variation When Prices are Regulated, 3 Bell. J. Econ. & Mgmt. Sci. 426 (1972); A. LaMond, Competition in the General Freight Motor-Carrier Industry 77-78 (1980).
ferior service performance on all of the service performance measures. Furthermore, all of these relationships are statistically significant. Since the majority of industry shipments are also handled by these unrestricted carriers, it is therefore difficult to see how consumers benefit from entry controls. Similarly, it is difficult to rationalize the continued market protection of unrestricted HHG carriers from open competition.

<table>
<thead>
<tr>
<th>Variables^a</th>
<th>Service Performance (Two-Year Averages)^b</th>
<th>RESTRICTED AUTHORITY Carriers with No Agents (N=160) Mean</th>
<th>Small Agency Systems (N=63) Mean</th>
<th>UNRESTRICTED AUTHORITY Large Agency Systems (N=35) Mean</th>
</tr>
</thead>
<tbody>
<tr>
<td>1. % of shipments picked up on time</td>
<td>99.1</td>
<td>98.8</td>
<td>97.0</td>
<td></td>
</tr>
<tr>
<td>2. % of shipments delivered on time</td>
<td>97.6</td>
<td>93.5</td>
<td>84.3</td>
<td></td>
</tr>
<tr>
<td>3. % of shipment $ charges correctly estimated (not underestimated)</td>
<td>84.9</td>
<td>85.9</td>
<td>80.3</td>
<td></td>
</tr>
<tr>
<td>4. % of shipments without a claim</td>
<td>90.6</td>
<td>90.8</td>
<td>85.1</td>
<td></td>
</tr>
<tr>
<td>5. % of claims settled promptly (within 30 days)</td>
<td>66.0</td>
<td>66.6</td>
<td>58.9</td>
<td></td>
</tr>
</tbody>
</table>

Source: Computed from Interstate Commerce Commission, Annual Carrier Service Performance Reports (on file at I.C.C.).

a. The differences between means for all variables are statistically significant at either the .01 or .05 level.
b. All service performance measures are two-year averages.

In summary, entry controls as manifested by HHG carrier certificate restrictions do not benefit consumers. Thus, not only do most HHG shippers apparently pay higher interstate transport prices in a regulated entry

28. See also A. ROBINSON, HOUSEHOLD GOODS: AN ANALYSIS OF CARRIER PERFORMANCE, 10-14 (1981) (I.C.C Office of Policy and Analysis). In a replication of this study's approach, Robinson utilized a minimum annual shipment constraint of 500 shipments. In addition, the results were broken down by type of shipper: individual (C.O.D.) and corporate transfer (national account). Basically, the same conclusions were achieved. It is particularly interesting to note that the corporate shippers were not found to receive significantly better service performance than individual shippers. Robinson concluded that agency systems are incompatible with effective carrier service performance.
environment, but the service performance is also inferior. In a broader sense, the study results provide no support for a "consumer protection hypothesis."

V. DISCUSSION OF RESULTS

A. POLICY IMPLICATIONS

This study revealed that large agency systems with unrestricted operating authorities provide inferior service quality to that offered by restricted carriers. Although these unrestricted carriers receive the greatest market protection from the I.C.C. and handle the majority of industry movements, the induced economies of utilization (operating efficiencies engendered by regulatory protection) are not passed on to the public in terms of improved transportation services. Since only the large agency systems benefit from the regulatory entry controls, the study results would appear to justify either the complete deregulation of HHG moving services or the granting of unrestricted nationwide operating authorities to both carriers without agents and small agency systems. Thus, rather than I.C.C. "mandated" agency systems, these "carrier-agents" would then only serve as agents when they lacked operational supply capabilities. By promoting competition amongst carriers, it would be expected that such an open entry policy would benefit both consumers and restricted HHG carriers.

A policy question which remains, however, is whether the carrier-agents with new unrestricted authorities would then establish their own large network of selling agents without regard to service capabilities. As shown in this paper, the existence of a broad and unrestricted grant of authority has in the past been a major incentive for carrier development of a large agency system. Certainly, "carrier-agents" which no longer required their principal's authority would in most cases cease to be agents for that carrier. However, it is also possible that both carriers would then recruit less qualified agents to take full financial advantage of their operating authorities, to the detriment of industry service performance.

It would appear that only totally free entry would completely eliminate all regulatory incentives as opposed to operational incentives for agency participation and agent retention. In turn, by providing alternatives to small carriers, such an open entry policy would tend to reduce industry reliance on large agency systems for shipment movements. Preferably, an open entry policy would also be accompanied by relaxed entry controls for new

29. Labor unions and equipment manufacturers are not a major factor in this particular industry when compared to general commodities motor carriers and air carriers. Furthermore, of all regulated motor carrier groups, HHG carriers have the heaviest reliance on independent owner-operators for shipment movements. See Morash, Owner-Operators in the Household Goods Moving Industry, 19 TRANSP. J. 17 (1979).
in institutional possibilities, e.g., HHG brokers, shipment clearinghouses, etc. \(^{30}\) Basically, these institutional possibilities could provide smaller carriers with alternatives to current agency system involvements or could "channel" shipments to the more price and service effective carriers as dictated by shipper needs.

\section*{B. Motor Carrier Deregulation}

In the aftermath of the Household Goods Transportation Act of 1980 and the Motor Carrier Act of 1980, the Interstate Commerce Commission has refrained from removing "radial type" restrictions from HHG carrier certificates and has not adopted an open entry HHG policy. This regulatory posture appears to stem from the continued belief that HHG entry restrictions benefit consumers and shippers.\(^{31}\) However, a number of Commission initiatives will indirectly weaken the agency system concept and have also provoked widespread criticism from the large agency systems. First, the Commission has eliminated the requirement that carrier-agents and their principal carriers maintain the same level of rates.\(^{32}\) Thus, carrier agents will be able to directly compete price-wise with their principal carriers when the carrier-agents operate under their own certificates.\(^{33}\) Secondly, the Commission has reinterpreted the definition of general commodities to also embrace household goods shipments.\(^{34}\) Thus, in the future, general commodities carriers will be able to compete for HHG shipments and perhaps form cooperative relationships with existing carrier-agents, freight forwarders, or local cartage firms. However, it is difficult to predict the exact future impact of these new regulatory changes on HHG agency systems.

\(^{30}\) Other specific examples would include travel agents, real estate firms, shippers’ cooperatives, shippers’ agents, and freight forwarders. All of these HHG market entry possibilities are presently circumscribed, to varying extents, by current I.C.C. regulations. See Morash, Regulatory Policy and Industry Structure: The Case of Interstate Household Goods Carriers, 57 LANOECON. 551-55 (1981).

\(^{31}\) See, e.g., Trend Continues Toward Eliminating HHG Agents That Hold Own Rights, TRAFFIC WORLD, June 1, 1981, at 35, 72.


\(^{33}\) Based on the economic theory of regulation and its prediction of cartel-like behavior, see Posner, supra note 1, at 344-45, it is possible to conceive of HHG rate bureaus as enforcing rate uniformity amongst the limited number of nationwide carriers while agency systems are the primary mechanism for uniformity amongst the much more numerous restricted carriers. Thus, a two-tier system of membership control would exist. This paper also suggests that such a system of membership control impacts on service quality.

VI. CONCLUSIONS

This study has provided evidence that only the large household goods agency systems with broad and unrestricted "certificates of public convenience and necessity" benefit from Interstate Commerce Commission entry controls. Thus, neither carriers with restricted operating authorities nor consumers benefit from these regulatory controls. In the case of carriers with restricted authorities, only limited opportunities exist for increased market shares and for efficient carrier operations. Furthermore, despite their better service performance, these HHG carriers with no agents and small agency systems are not financially rewarded for the enhanced service. In total, these conditions may be a primary reason for industry reliance on large agency systems for shipment movements.

For consumer or shipper benefits, prior research has provided evidence that shippers pay substantially more for regulated interstate HHG moving services than for comparable intrastate HHG movements. In turn, this study has provided evidence that most shippers also receive inferior service performance. Thus, the common theory that when rates are regulated, carriers will compete away excess profits by offering excessive services does not appear to hold true for this particular regulated industry. Similarly, the prediction of the "consumer-protection hypothesis" that HHG regulatory controls will result in at least improved service to the shipping public is also not supported by this study.

These results suggest a need for a completely open entry policy for HHG carriers. Similarly, the total elimination of all certificate restrictions for carriers with no agents and small agency systems also seems warranted. As outlined in section V, partial palliatives would not be expected to bring any benefits to consumers, but would rather exacerbate current distortions. Unfortunately, in the aftermath of the Household Goods Transportation Act of 1980 and the Motor Carrier Act of 1980, an open entry policy has not been adopted by the Interstate Commerce Commission. Such a policy position should be reappraised and instituted to benefit both consumers and restricted carriers.

35. Breen, supra note 3, at 178; Breen, supra note 24, at 51.
Casenote: Chicago and North Western Transportation Co. v. United States

ELIZABETH BURCH MICHEL*

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I. INTRODUCTION

The 1970’s saw a tremendous change in the rail industry. Once the dominant mode of both freight and passenger transportation, the railroads found their market shares dropping and their financial health declining.2

1. 678 F.2d 665 (7th Cir. 1982).


Passenger service became the purview of the government-owned National Railroad Passenger Corporation;\(^3\) much of the freight service for the Midwest and Northeast became the responsibility of the government-owned ConRail;\(^4\) and two major transcontinental carriers, the Milwaukee\(^5\) and the Rock Island\(^6\) went bankrupt. As the 1980's began, the industry remained in poor health despite the fact that several significant rail mergers and acquisitions were approved to increase operating efficiencies and enabling the industry to better compete with other modes of transportation.\(^7\)

To help the industry regain financial stability and to assist in the rehabilitation and financing of the rail system, Congress passed the Staggers Rail Act of 1980.\(^8\) Although most of its changes concerned carrier rates, Congress also modified the means by which carriers are able to abandon unprofitable lines. Since 1920, carriers have been permitted to seek authority from the Interstate Commerce Commission to abandon their operations and discontinue their service.\(^9\) If the public convenience and necessity permit, the Commission must authorize the abandonment. After abandonment is authorized and effectuated, the rail carrier no longer serves the shipper and communities on the line being abandoned, even if those parties desire and need service. The abandonment process, however, was often a lengthy one, allowing numerous opportunities for delay.\(^10\)

Therefore, in the Staggers Act, Congress modified the abandonment procedures so that the application was handled more expeditiously. Under the Staggers Act changes, the Commission must issue a final decision in all abandonment proceedings within 255 days of the filing of the application.\(^11\) Those abandonments with little or no opposition are decided within seventy-five or forty-five days, respectively, of the application’s filing.\(^12\)

However, while providing for expedited handling of abandonments, Congress also showed concern for the impact of abandonment on commu-

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5. Chicago, Milwaukee, St. Paul and Pacific Railroad Company (Milwaukee) filed a petition on December 19, 1977, for reorganization.
6. Chicago, Rock Island & Pacific Railroad Company (Rock Island) filed a petition on March 17, 1975, for reorganization.
12. Id. § 10904(b), (c)(2).
nities and shippers. It therefore gave the Commission the unprecedented power to force a railroad to sell the line authorized for abandonment, at fair market value, to a financially responsible entity who would continue the service.\textsuperscript{13}

Prior to the Staggers Act, the Commission had attempted to force abandoning carriers to bargain in good faith with offerors by postponing the issuance of abandonment certificates indefinitely if the offeror and carrier failed to reach an agreement within six months. The Seventh Circuit rejected this attempt by the Commission to create a cram-down provision. The court held that if negotiations failed, a certificate must be issued at the end of the six month period.\textsuperscript{14} Thus, the Commission was left with no power to force the abandoning carrier to negotiate in good faith with the offeror. Instead, it could only provide for the six month suspension of the grant of an abandonment certificate, while negotiations were attempted by the two parties.

Congress recognized the dilemma. A Senate report from the Committee on Commerce, Science, and Transportation states, "a railroad unwilling to consider subsidy or sale of the line can frustrate the intention of section 10905 of 49 U.S.C. by simply refusing to negotiate in good faith."\textsuperscript{15} Congress amended section 10905 so that the intention of the statute could no longer be circumvented. The Commission now had the power to assure good faith negotiations. If negotiations break down, the Commission, at the request of one of the parties, can intervene and set the conditions of the sale.

This "cram-down" provision was first construed by the courts in \textit{Chicago and North Western Transportation Co. v. United States}.\textsuperscript{16} The questions before the court, and the ones addressed by this casenote, are questions of statutory construction.

\section*{II. Background: The Interstate Commerce Commission's Decision}

On December 31, 1979, Chicago and North Western Transportation Company (C&NW) filed an application with the Interstate Commerce Commission (ICC) seeking to abandon approximately seventeen miles of rail line between Ringwood, Illinois, and Lake Geneva, Wisconsin — the "Lake Geneva Line." Authority for such action by the ICC is found at 49 U.S.C. sections 10903-04. C&NW offered evidence showing "the line had been operating at a loss for the most recent three years; that traffic was thin and

\textsuperscript{13} Id. § 10905.
\textsuperscript{14} Chicago and North Western Transp. Co. v. United States, 582 F.2d 1043, 1049 (7th Cir. 1978).
\textsuperscript{16} 678 F.2d 665 (7th Cir. 1982).
was declining; that substantial rehabilitation was required on the line; and that it was incurring sizable opportunity costs from its inability to withdraw its assets from this unprofitable operation." On April 14, 1981, the Commission granted the abandonment.

Responding to the grant of the abandonment application, the Geneva Lake Area Joint Transit Commission (GLA), a "consortium of towns that is dedicated to preserving commuter rail service," offered C&NW $985,000 for the line, pursuant to the offer of financial assistance provisions of 49 U.S.C. section 10905. The ICC found the consortium financially responsible and deemed its offer bona fide.

GLA and C&NW began negotiations pursuant to the statute but failed to agree on the terms of the purchase. The major point of disagreement was the amount to be paid for the land which made up the rail corridor. C&NW’s estimate as to the value of the property and the rail materials escalated as the negotiations continued. GLA, frustrated by the negotiations and its failure to reach agreement with C&NW on the terms of the purchase, petitioned the ICC pursuant to 49 U.S.C. section 10905, which grants the ICC the power to set the terms of the purchase. The ICC, after taking evidence from both parties, set the price and the conditions of the purchase. The price set by the ICC was closer to GLA’s estimate of the price of the line than C&NW’s—$1,003,321. The ICC accepted GLA’s appraisal on both the property and on the price to be placed on the reus-

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17. The Commission’s consideration of opportunity costs in abandonment proceedings is a recent development. As recently as 1979 a majority of the Commission decided that although there was nothing stopping it from using opportunity costs as a factor in abandonment proceedings, there were also no cases explaining how and when it could be used. Texas and Pacific R. — Abandonment, 360 I.C.C. 206, 207 (1979).

After acknowledging that the concept was a valid one, the Commission decided to get comments as to how opportunity costs should be used as a factor in abandonment proceedings. Id. at 208. After analyzing the many comments that were filed, the Commission decided that opportunity costs are a real, and, in some cases, very significant factor in determining whether the line at issue is imposing a burden on interstate commerce.” Abandonment of R.R. Lines — Use of Opportunity Costs, 360 I.C.C. 571 (1980), aff’d sub. nom. Farmland Indus., Inc. v. United States, 642 F.2d 206 (7th Cir. 1981).

Having decided that opportunity costs were factors to be used in abandonment proceedings, the Commission proceeded to find that “a carrier’s opportunity costs could be found by applying an adequate rate of return against the line’s net liquidation value.” Texas and Pac. Ry. Abandonment, 363 I.C.C. 666 (1980). Abandonment 363 I.C.C. 666 (1980).


21. id. at 958-60. C&NW set the price of the corridor at $763,100. GLA’s final appraisal and offer was $275,000. See also Brief for the Interstate Commerce Commission at 7-9. Brief for Chicago and North Western Transportation Company at 6, 28-31, Chicago and North Western Transp. Co.
able rail. The ICC accepted C&NW’s valuation of track and structures exclusive of rail.\textsuperscript{22}

The ICC also set the terms of the purchase; closing was to occur within ninety days at C&NW’s request, and payment was to be by cash or certified check. As to the method of conveyance, the ICC stated: “In light of the clouded title under which C&NW holds most of the property, if GLA is willing to accept a quit-claim deed we have no objection.”\textsuperscript{23}

III. The Statute

In seeking judicial review of the ICC’s decision, C&NW did not challenge 49 U.S.C. section 10905.\textsuperscript{24} However, for a full understanding of the court’s decision it is necessary to discuss the statute under which this cause of action originated.

Under section 10905, a financially responsible person may offer to purchase a rail line within ten days after the ICC publishes its decision in the Federal Register to allow abandonment of that line.\textsuperscript{25} If within fifteen days after publication the ICC determines that the offeror is financially responsible and its offer bona fide, it must temporarily suspend its grant of abandonment so that the parties can negotiate the sale.\textsuperscript{26} However, if the parties cannot reach an agreement within thirty days of the offer, either party may request the ICC to set the price and the terms of the sale.\textsuperscript{27} Following the request, the ICC has sixty days to issue its decision setting the terms.\textsuperscript{28} In no instance shall the price be lower than the fair market value of the line.\textsuperscript{29} Once the ICC has set the terms, the offeror has ten days to withdraw his offer.\textsuperscript{30} If the offeror fails to do so, the terms become binding and he must finalize the purchase. The purchaser must assure continued rail service over that line for no less than two years.\textsuperscript{31}

The purpose of this statute\textsuperscript{32} is to expedite negotiations and give relief to an offeror who is potentially being “held-up” by the abandoning rail carr-

\textsuperscript{22} “Where both offeror and offeree have submitted acceptable appraisals and where it is impossible to determine which valuation is more accurate, we shall accept the figure submitted by the offeree — railroad.” Chicago and North Western Transp. Co. — Abandonment, 363 I.C.C. 956, 961-62 (1981).
\textsuperscript{23} Id. at 963.
\textsuperscript{25} Id. § 10905(c).
\textsuperscript{26} Id. § 10905(d).
\textsuperscript{27} Id. § 10905(e).
\textsuperscript{28} Id. § 10905(f)(1)(A).
\textsuperscript{29} Id. § 10905(f)(1)(C).
\textsuperscript{30} Id. § 10905(f)(2).
\textsuperscript{31} Id. § 10905(f)(4).
rrier. In this manner Congress sought to force abandoning railroads to come to terms with financially responsible offerors so that rail service could be continued where it would otherwise be halted.

IV. THE SEVENTH CIRCUIT’S DECISION

Since C&NW did not challenge the statute, 49 U.S.C. section 10905, the Seventh Circuit was left with two related issues: (1) What was meant by the term fair market value, and (2) once this was determined, what was the value of the property and therefore its selling price?

A. FAIR MARKET VALUE

Because this was the first proceeding interpreting this statute, the ICC had to first determine what was meant by the term fair market value. Analyzing this language, the ICC noted that in another forced sale provision enacted at the same time, Congress provided for the forced sale of non-abandoned rail property at the constitutional minimum value. Moreover, Congress defined the constitutional minimum value as being the greater of net liquidation value or going concern value. In its abandonment regula-

33. Prior to the Staggers Rail Act of 1980, offers of financial assistance to purchase a railroad line being abandoned fell under 49 U.S.C. § 1a(6)(a) (1976). Under this section, permission to abandon a line would be temporarily suspended for six months while the offeror attempted to come to terms with the abandoning railroad as to the purchase of the line. There was, however, no relief for the offeror should the railroad refuse to negotiate in good faith. In this manner the abandoning carrier could hold out for a higher price. Chicago and North Western Transp. Co. v. United States, 678 F.2d at 667-68.

34. The cram-down provision also applies to responsible offers to subsidize an abandoning carrier. The subsidizer pays the railroad the difference between the revenues attributable to that part of the railroad line and the avoidable cost of providing rail freight transportation on the line plus a reasonable return on the value of the line. 49 U.S.C. § 10905(d)(2)(A) (Supp. V 1981).

35. C&NW did, however, challenge the procedures which implemented the statute. C&NW, in its brief stated, "the Commission has failed to provide North Western with any meaningful opportunity to be heard with respect to the fair market value of the Lake Geneva line." Brief for Chicago and North Western Transportation Company at 33, Chicago and North Western Transp. Co. v. United States. The Seventh Circuit addressed this issue at the conclusion of its decision.

We think the procedure whereby the Commission determined the fair market value of the Lake Geneva line was adequate. C&NW does not challenge the constitutionality of the 60-day deadline for the Commission’s valuation. That concession, and another (its brief in this court states, ‘It may be that the fault lies with the exceedingly tight 60-day time limit’), pretty much puts it out of court. Sixty days permit only summary procedures. The Commission acted on a written record based on the submissions of the parties and their written comments on each other’s submission. No doubt there would have been time for some kind of oral hearing . . . But in oral argument in this court C&NW’s counsel disclaimed any desire to cross-examine GLA’s witnesses. This disclaimer implies that oral hearing would have served no purpose. Since the benefits of additional procedural safeguards could have been zero, we need not concern ourselves with what the costs would have been; the procedure was constitutionally adequate under Matthews v. Eldridge, 424 U.S. 319, 335 (1976).

Chicago and North Western Transp. Co. v. United States, 678 F.2d at 671.
tions, the ICC concluded that fair market value also was the greater of net liquidation value or going concern value. These regulations, though issued after the ICC's decision setting the terms of purchase, were used by the ICC to support its position on appeal.

The ICC still had to decide, however, whether the appropriate value in this proceeding was net liquidation value or going concern value. The ICC determined that C&NW, by its request for abandonment, was asserting that the line was a burden on interstate commerce. Therefore, there was no going concern value. The ICC thus interpreted fair market value to be net liquidation value—what the carrier would have received if the line had been abandoned and the railroad had sold off its assets. The carrier salvages the reusable rail line, sells the rest of the rail materials for scrap, and then sells off the real estate underlying the right-of-way.

The Seventh Circuit affirmed the ICC's interpretation of fair market value. The court stated:

But for the sale of the Lake Geneva Line to GLA at a price fixed by the Commission, C&NW would have abandoned the line — that is, would have sold the right of way and track and other property and facilities for nonrail uses and the price it would have received would have been the nonrail market value of these assets, which is what the Commission tried to estimate when it fixed the sale price. The court recognized that the government had a constitutional obligation to give, or determine that a specific party give, just compensation for property that it condemns. This compensation must be an amount equivalent to what the railroad would have received without government intervention; in this instance, the amount the carrier would have been able to sell the assets for subsequent to the abandonment. Compensation under this statute and based on these facts does not mean the market value of a working rail line.

The court went on to discuss C&NW’s contention that net liquidation value was not the appropriate standard. Instead, C&NW asserted that going concern value should be applied. C&NW argued that because the statute intended that rail service be continued for two years, this in fact imbued

39. Id.
40. Chicago and North Western Transp. Co. v. United States, 678 F.2d at 668.
41. Id.
42. Id.
the line with going concern value. GLA would be operating the line in the
same manner as C&NW had in the past. The Seventh Circuit rejected this
contention. The court stated:

We are not sure why this should make a difference. Whatever the intended
use by the government, the condemnee who asks for more than what the
property would have been worth to him if the government had not wanted the
property is trying to engross 'hold-out' values — the very thing, one might
have thought, that the eminent domain power was intended to excuse the gov-
ernment from having to pay.44

And further: ‘[W]e think it irrelevant whether private property is taken for a
new use or to continue an old one, and even question whether this is a
meaningful distinction.45

B. The Value of the Property

Having decided to value the property according to net liquidation
value, the ICC and the Seventh Circuit still had to resolve the specific dis-
putes as to the value assigned to the rail property.

C&NW contended that the ICC should take into account the assem-
bled value of the rail property.46 In this way the value of the property is
substantially increased. GLA, on the other hand, argued that the value of
the property should be determined as if C&NW had actually abandoned the
line—that is, the property’s value if it had been sold off by the abandoning
carrier for nonrail usage. Using this method, GLA placed no value on land
which could not be conveyed if an actual sale of the parcel for nonrail use
had occurred. Therefore, GLA argued, any property which would revert to
the original owner once the line was abandoned was rendered worthless to
C&NW. This included any land that was held by adverse possession or
easement.47

Having decided to rely on net liquidation value, it would have been
inconsistent for the ICC to value the property as a corridor for rail use when
it was prepared to grant C&NW’s abandonment petition on the grounds that
it was unprofitable for such use. Thus, the ICC rejected C&NW’s argu-
ment.48 In affirming that finding, the court noted that, although their con-
clusion that GLA could acquire the Lake Geneva Line at salvage value
might appear harsh, it was inescapable since the proper standard was fair

43. Brief for Chicago and North Western Transportation Company at 13-20, Chicago and
44. Chicago and North Western Transp. Co. v. United States, 678 F.2d at 669.
45. Id.
46. Brief for Chicago and North Western Transportation Company at 14-16, Chicago and
47. Brief for the Interstate Commerce Commission at 21-22, Chicago and North Western
market value.49

V. POSTSCRIPT

In its July 23, 1981, decision setting the price and other terms of sale, the ICC held that if GLA accepted the terms, consummation of the transaction must occur within ninety days of the service date of the decision.50 However, prior to that date, C&NW petitioned the Seventh Circuit for a review of the decision.

On September 28, 1981, GLA filed a petition seeking a stay of the ninety day consummation period because of the court review.51 C&NW concurred in that request. In a decision served October 20, 1981, the ICC agreed to the modification of the consummation deadline.52 It ordered consummation to occur within ninety days of the entry of a decision by the Seventh Circuit.

Since the Seventh Circuit's decision was entered on April 26, 1982, C&NW claimed that the consummation deadline was July 25, 1982.53 However, on July 16, 1982, GLA filed a telegram with the ICC requesting that the alleged July 25, 1982, consummation deadline be postponed until the ICC ruled on the question raised in a petition for clarification filed by C&NW on July 21, 1982. GLA's request was granted by the ICC Chairman Reese H. Taylor, Jr., in a decision served July 23, 1982. Chairman Taylor indicated that a new consummation date would be set by the ICC in its decision addressing C&NW's petition.

In a decision served August 31, 1982, the ICC addressed C&NW's petition for clarification.54 The primary question raised by C&NW concerned the method by which the property would be transferred. C&NW wanted to transfer the property by quitclaim deed.55 GLA, on the other hand, wanted either a warranty deed or a quitclaim deed accompanied by

49. Chicago and North Western Transp. Co. v. United States, 678 F.2d at 670.
51. GLA also sought a stay of the 10-day withdrawal period. That request was denied because: (1) it was late-filed since the 10-day period expired on August 2, 1981, and (2) the 10-day period is statutorily mandated, 49 U.S.C. § 10905(1)(2) (Supp. V 1981). Chicago and North Western Transp. Co. — Abandonment — Between Ringwood, IL and Geneva, WI — No. AB-1 (Sub-No. 70) (I.C.C. served Oct. 20, 1981).
52. Id.
title insurance purchased at C&NW’s expense.\textsuperscript{56} The problem was how to interpret the following paragraph from the ICC’s July 23, 1981, decision: “GLA has not addressed C&NW’s request that the property be conveyed by quitclaim deed. In light of the clouded title under which C&NW holds most of the property, if GLA is willing to accept a quitclaim deed we have no objection.”\textsuperscript{57} C&NW argued that this language was ambiguous and therefore must be clarified by the ICC.\textsuperscript{58}

The ICC granted C&NW’s petition and determined that C&NW would be allowed to convey by quitclaim deed.\textsuperscript{59} It also rejected GLA’s requested title insurance condition but noted that GLA was free to attempt to acquire its own title insurance policy.\textsuperscript{60} The ICC also allowed GLA ten days to accept or reject the terms as clarified in its decision because it concluded that GLA may not have originally agreed to acquire the property by quitclaim deed.\textsuperscript{61} If GLA accepted the clarified terms, the ICC indicated that consummation had to occur within thirty days of the service date of the decision.\textsuperscript{62}

On September 10, 1982, GLA notified the ICC of its decision to accept the terms of sale as clarified by the ICC’s August 31, 1982, decision. Accordingly, pursuant to 49 U.S.C. section 10905(e), the ICC issued a decision on September 23, 1982, dismissing the C&NW abandonment application and authorizing the sale.\textsuperscript{63} Consummation was scheduled to occur on September 30, 1982.

On September 30, 1982, however, GLA petitioned the ICC for a sixty day extension of time to consummate in order to complete financing arrangements.\textsuperscript{64} In its petition GLA noted that the ICC normally provided parties with ninety days to consummate a section 10905 sale and that its request, if granted, would provide the ninety days.

C&NW quickly filed a petition opposing the extension of time.\textsuperscript{65} More-

\textsuperscript{56} Response to Petition for Clarification of the Commission’s Decision served July 23, 1981, Establishing Purchase Price and Other Terms at 3.
\textsuperscript{57} Chicago and North Western Transp. Co. — Abandonment, 363 I.C.C. at 963.
\textsuperscript{58} Petition for Clarification of the Commission’s Decision served July 23, 1981, Establishing Purchase Price and Other Terms at 2-6.
\textsuperscript{59} Chicago and North Western Transp. Co. — Abandonment — Between Ringwood, IL and Geneva, WI, No. AB-1 (Sub-No. 70) (I.C.C. served Aug. 31, 1982).
\textsuperscript{60} Id.
\textsuperscript{61} Id.
\textsuperscript{62} Id.
\textsuperscript{63} Chicago and North Western Transp. Co. — Abandonment — Between Ringwood, IL and Geneva, WI, No. AB-1 (Sub-No. 70) (I.C.C. served Sept. 23, 1982).
over, C&NW requested that the September 23, 1982, decision dismissing its abandonment application be vacated and that it be authorized to immediately abandon the line because GLA had defaulted on its obligations by failing to consummate on September 30, 1982.

In a decision served October 26, 1982, the ICC granted GLA’s request but with conditions attached. First, the ICC indicated that GLA’s failure to comply with its conditions would result in immediate issuance of an effective abandonment certificate. Second, GLA was required to compensate C&NW for any losses incurred during the sixty day extension. GLA was ordered to subsidize C&NW’s operations for the period commencing September 30, 1982, and ending November 29, 1982, or earlier if consummation occurred prior to that date. The subsidy would be calculated according to the ICC’s subsidy regulations, which provide for carrier reimbursement for operating losses as well as a return on assets invested in the line. GLA was given until November 8, 1982 to notify the ICC and C&NW of its decision accepting or rejecting these conditions. Rejection of the conditions or failure to notify the ICC by that date would result in an immediate issuance of an effective certificate permitting abandonment. To put teeth into this decision, the ICC vacated its September 23, 1982, decision that authorized the transfer and dismissed the abandonments.

Because GLA neither accepted nor rejected the conditional extension by November 8, 1982, the ICC issued a certificate and decision on November 10, 1982, which authorized C&NW to abandon the line immediately. C&NW consummated the abandonment on November 15, 1982.

VI. CONCLUSION

As indicated by a 1979 Senate report, the railroad industry is of vital


67. 49 CFR § 1152.27 (1982).

68. After consummating the abandonment, C&NW filed a petition with the ICC seeking an award of $21,116.47 in damages against GLA because of GLA’s failure to consummate the purchase of the line. On April 18, 1983, the Commission issued a decision finding that, “in the absence of any showing of bad faith... the award of monetary damages is not ‘appropriate action.’” Accordingly, the Commission dismissed C&NW’s petition for damages. Chicago and North Western Transp. Co. — Abandonment — Between Ringwood, IL and Geneva, IL, No. AB-1 (Sub-No. 70) (I.C.C. served Apr. 18, 1983).

69. An efficiently operating transportation system is essential to the well-being of the nation. About 20 percent of our total annual expenditures for goods and services goes for transportation of people or freight. More than 12 percent of our total civilian employment is in transportation or related industries, amounting to more than 10 million jobs in 1977. The tremendous demands on the national transportation network to move goods are evident when total freight ton-miles number over 2 trillion annually. Of this total tonnage, railroads carry over 70 percent of coal ton-miles and 60 percent of grain ton-miles. They are also the principal mode for pulp and paper products, automotive products, foodstuffs, chemical and primary metals. Unfortunately, at a time when the need for increased trans-
importance to the nation and is in serious trouble. It is also obvious that if service is disrupted, for any reason, the ramifications will be severe. Shippers will be unable to move their goods, and commuters will be cut off from access to their employment. An abandonment of a rail line is a total and final disruption of service. Shippers and communities can file objections with the ICC when a railroad petitions for abandonment, but these objections are rarely successful. In the fiscal year 1981, 140 applications for abandonment were decided and of those, 139 involving 2,914 miles of rail line were granted.\textsuperscript{70} In the fiscal year 1982, 423 applications for abandonment were decided; 380 involving 5,168 miles of rail line were granted, 40 were withdrawn and only 3 were denied.\textsuperscript{71} These figures will undoubtedly escalate unless the shippers using the rail industry dramatically increase the use of rail lines, and the rail industry experiences a dramatic improvement in earnings.

It is also important to realize that these abandoned rail lines are lost for all time. The possibility of another railroad constructing a new rail line between points that lose service is remote, as the cost of constructing new rail line is prohibitive.\textsuperscript{72}

Section 10905 is not a complete solution to the abandonment problem.\textsuperscript{73} However, it is an important alternative to an almost automatic cessation of service. It also constrains the abandoning railroad from holding up the offeror. The ICC can set the conditions of the sale at the request of one of the parties if the negotiations break down. Since the enactment of the amendment to section 10905, the ICC has received 105 offers of financial assistance. Thirty-eight purchases were made and twelve subsidies were arranged. Five purchase offers are currently pending. Service will continue over these lines for at least two years. The program, it appears, is working. Rail service is continuing where it otherwise would have been permanently disrupted.

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 porta capacity is developing at a rapid pace, the railroads are the weakest sector in our transportation system, and the ability of the railroad industry to meet its future responsibilities to society is considered by many to be in doubt.


71. Figures obtained in an informal discussion with Louis E. Gitomer, Deputy Director Rail Section, Office of Proceedings, Interstate Commerce Commission (Oct. 22, 1982).

72. For example, in 1982 the ICC approved a request by Somerset Railroad Company to construct a 27.4 mile line of railroad at an estimated cost of $44 million. Somerset R. Corp.---Niagara County, NY, 366 I.C.C. 144 (1982). Similarly, on October 4, 1982, the Denver and Rio Grande Western Railroad Company filed an application to construct a 62 mile line at an estimated project cost of $70 million. Finance Docket No. 30044, The Denver and Rio Grande Western Railroad Company, Application to Construct and Operate a Line of Railroad in Carbon and Emery Counties, UT.

GLA felt that rail service was so important to the community that it was formed for the sole purpose of preserving this valuable service:

GLA, made up of local public bodies in Wisconsin and Illinois was created to maintain and enhance rail service on this line. The on-line municipalities, on-line shippers and the public have evidenced their desire for continued train service by their protests and requests for investigation. Indeed, GLA's existence as the first transit commission in Wisconsin and first bi-state rural transit commission anywhere attest to the public's desire to retain rail service.\(^\text{74}\)

The Seventh Circuit preserved the integrity of this very important statute. By using this program, the community and shippers will receive continued rail service, and the railroad will receive the fair market value for its property.

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MARKET DOMINANCE

The Evolution and Implications of the Market Dominance Concept in Railroad Ratemaking

DENNIS M. GAWLIK*
KEVIN B. BOBERG**

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Control of market and shipper abuse through the Interstate Commerce Commission (Commission) has been the cornerstone of railroad regulation in the United States. Pervasive monopoly power in some rail markets coexistent with severe intramodal (i.e., rail versus rail) competition in other markets seemed to warrant some form of economic regulation to protect the interests of both shippers and carriers. Although often interpreted and implemented to protect either shippers or carriers, the tenets of regulation as guardian of shipper and carrier remained unchanged for nearly ninety years despite vastly changing market conditions.

Academics perceived the need for regulatory reforms from increasingly apparent trends in the post-war years. Between World War II and 1980, the railroad share of intercity ton-mileage dipped from 68.6% to 37%. Over the same period, the rail industry experienced a precipitous decline in their share of intercity freight revenue, from 76% to 38%. For 1980, the estimated return on investment (net investment basis) was 4.25% for Class I railroads. Although a twenty-five year high for the industry, this return is still far below that in other industries, and far below the 11% the railroads must have to attract the private capital necessary to maintain service at an adequate level. The effect of declining freight revenue has been anemic returns to owners, jeopardizing the very existence of the rail industry.

The initial justification for regulation of the railroads, monopolization,


2. ASSOCIATION OF AMERICAN RAILROADS, YEARBOOK OF RAILROAD FACTS 36 (1980).
no longer existed. Freight markets once dominated by rail carriers were being eroded by a combination of technological and economic changes. Regulation no longer could be viewed as ensuring economically efficient or fair market results; instead, it had come to be a contributing cause of substantial misallocation of traffic. This development eventually received substantial political attention in the form of the deregulatory movement.

Congress, recognizing that the growth of other modes of transportation had raised serious questions about the necessity for protection against rail monopoly, passed the Railroad Revitalization and Regulatory Reform Act of 1976\(^3\) (4R Act). In the place of functional regulation (e.g., control of maximum rates under all circumstances) the 4R Act introduced a system of selective market price regulations based upon determinations of market dominance.

Under the new system, railroads are viewed as multiproduct-carrying firms operating in several distinct product markets. Each market is characterized by unique conditions of supply and demand. In some markets, sufficient competition may exist to make maximum rate regulation unnecessary; in others, the development of insufficient competition may warrant continued regulation. The market dominance concept, as stated by Congress and later implemented by the Commission, was to be used to distinguish between competitive and non-competitive.

Due in part to the rigidity with which the Commission applied the market dominance principle, the pricing reforms envisaged by the 4R Act were largely unrealized. Prompted by this failure, and the continued financial plight of the railroad industry, Congress passed the Staggers Rail Act in 1980\(^4\) (Staggers Act). The Staggers Act retained the requirement that maximum rate regulation be predicated upon a finding of rail market dominance; but the ICC was directed to redefine its operative definition of market dominance.

\section{Purpose}

Limited rate regulation represents a radical departure from previous regulation schemes. In many ways this type of control is more complex. The Commission has been forced to consider, if not answer, questions which have long plagued policy makers. What is the relevant market in determining market dominance? What factors in the relevant market, once identified, characterize its competitive disposition? How are these charac-


characteristics to be measured without imposing undue data requirements on carriers, shippers and regulators?

The primary purpose of this article is to present an historical accounting of the market dominance principle as it has evolved through congressional enactments and Commission proceedings and regulations. Included in the accounting is a review of the work of A.T. Kearney Consultants (A.T. Kearney), the firm employed by the Commission for technical assistance, which contributed significantly to the formulation of the market dominance principle. This article will also explore factors which may precipitate further changes in the implementation of the market dominance principle through new standards for monitoring market conditions.

II. EVOLUTION OF THE MARKET DOMINANCE CONCEPT

A. HOUSE AND SENATE BILLS

A premise of the House Committee on Interstate and Foreign Commerce in formulating its report on the 4R Act was that if a carrier dominates a market, the maximum rates charged to its customers should be subject to regulation. According to the House committee's approach, the existence of effective competition for any segment of traffic was to be determined by the direct transportation cost, service options, and commodity and shipper characteristics present. It set out, in 1975, to allow for "a wider operation of competitive forces in the market place" because its members believed that, in most cases, competition could locate the most efficient price levels. The House report defined market dominance as follows:

Market dominance shall be presumed in any situation in which (i) in any geographical market there are not at least 2 competing rail carriers or a rail carrier and an alternative mode of transportation both of which compete for the business in the area, or (ii) with respect to any single commodity or type of goods there is an absence of competition between the rail carriers for transport of that commodity, or where there is only one rail carrier, the absence of a competing mode which in fact provides transportation for that commodity in a reasonably effective and competitive fashion.

The House committee intended to exclude general rate increases brought about by rate bureau activity from the Commission's market dominance tests because it did not want to destroy the purpose of the industry-wide

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7. Id. at 12 (emphasis added).
The Senate Committee on Commerce also concluded, in late 1975, that "deregulating and giving flexibility to the railroads [in ratemaking]. . . . can supplant the need for maximum price regulation." The Senate committee intended that market dominance act as a threshold test; a finding of market dominance would only direct the attention of the Commission's investigation toward areas where the possibility of abuse existed. Private interests would still be protected, but carriers would be given greater flexibility. However, the Senate committee's concept of market dominance differed from that of the House in that:

"Market dominance shall be presumed to exist if, prior to or after the publication of a rate, no shipment . . . of the traffic to which the rate applies have [sic] moved by any other carrier or mode of transportation other than by a proponent carrier, during the 12 months preceding the commencement of the [ICC's] proceeding to determine or investigate the lawfulness of the rate as a result of the relationship of the applicable rate . . . of any other carrier or any other mode of transportation, to the rate of the proponent carrier . . . ."

The Commission's role, when utilizing the market dominance principle prescribed by Congress, is to characterize market behavior. As framed initially, market dominance is a measurement or a critical value index against which to measure actual market conditions. If it is determined that actual conditions exceed the acceptable minimal levels of competitiveness, then the law is to presume that the rates charged are reasonable. If it is determined that conditions do not exceed the minimal level, then the rate in question must be reviewed to ensure its reasonableness, because of the presumption of market power in the relevant market.

One final point which emerges from these early congressional deliberations is the role of the Commission as the arbiter of market dominance regulation. Several very difficult problems involved were never adequately addressed by Congress, and thus were left for the Commission to resolve in their case-by-case decisions. An acceptable minimum level of competition was not precisely defined; nor was a yardstick provided for the difficult task of measuring actual market conditions. Furthermore, both the House and the Senate committees implicitly recognized the need to distinguish the determination of market dominance from determination of the reasonableness of rates. The task was delegated to the Commission.

The rudiments of the market dominance concept have remained largely unchanged since these 1975 Committee reports. The methods of

8. Id. at 69. A rate bureau is a group of carriers that establish joint rates, divide joint revenues, claim liabilities, and publish tariffs.
10. Id. at 119 (emphasis added).
measuring market behavior for the traffic in question, and for separating competitive from dominated markets, are unaltered. In the former, it is presumed that rate regulation is unnecessary. In the latter, rate regulation is presumed necessary, but the existing rates are not presumed to be excessive or unreasonable. The functioning and role of the market dominance principle is presented in Figure 1.

**Figure 1**

![Diagram showing the decision process for rate proposals based on market dominance.]

**B. Market Dominance Provisions of the 4R Act**

The market dominance test is to determine the degree of competition, and to assess which competitive forces are present to assure that market conditions are sufficient for just and reasonable rates. It is a test of reasonableness of rates per se. The Interstate Commerce Act was amended in 1976 to define market dominance as "an absence of effective competition from other carriers or modes of transportation, for the traffic or movement to which a rate applies."\(^{11}\)

The purpose of the Interstate Commerce Act (Act) is to protect shippers against abusive rates.\(^{12}\) Congress intentionally avoided the area of "monopoly power" when formulating the market dominance test because of problems created by previous violations of antitrust laws.\(^{13}\) The 4R Act,

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13. As used here, monopoly power refers to the potential ability of a firm to exploit its market position through exploitative pricing, discriminatory practices, or other noncompetitive market behavior without attracting competition. Congress circumvented monopoly power proof through the use of testing for market dominance because it could not adequately define many of the terms it would have to use if it fashioned legislation around a concept that was more theoretical than applicable. Through the use of the market dominance concept, the Commission would be able to con-
in its final form, also stated that:

[No] rate shall be found to be unjust or unreasonable . . . on the ground that such rate exceeds a just or reasonable maximum for the service rendered or to be rendered, unless the [Interstate Commerce] Commission has first found that a proponent carrier has market dominance over such service. A finding that a carrier has market dominance over a service shall not create a presumption that the rate or rates for such service exceed a just and reasonable maximum.¹⁴

Congress instructed the Commission to make a ruling for market dominance within ninety days of a rate increase challenge. In addition, the 4R Act required the Commission to develop rules, standards and procedures for determining when a carrier possesses market dominance over a service rendered or to be rendered at a particular rate or rates. This process was to be carried out within 240 days after the enactment of the 4R Act to provide for a quick and practical determination of the law as it was to be administered by the Commission.¹⁵

Under the new sections of the Act as amended by the 4R Act a rate could not be held to be unreasonably high unless the Commission first found that the railroad possessed market dominance over the traffic. A finding of market dominance, however, is only an initial step in determining if a rate is reasonable. Market dominance is used as a means of identifying transport markets where users have no meaningful modal or rail options.¹⁶ Congress designed the 4R Act to protect shippers in those situations where rate abuse could occur.

C. THE COMMISSION’S INITIAL PRESUMPTIONS

On March 16, 1976, the Commission issued a notice of proposed rulemaking in which certain “factual situations” would create rebuttable presumptions of market dominance in rate increase proceedings. The Commission announced that a lack of effective competition could be inferred in the following situations:
1) where the rate was discussed or considered by rate bureaus; or
2) where no other carrier of any mode had handled a significant amount of the “involved traffic” during the preceding year; or
3) where other carriers had handled a significant amount of traffic but there was no evidence of actual price competition in the past three years; or
4) where the rate exceeded existing rates by 25% or more; or

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5) where the rate exceeded the fully allocated cost of the service by 50% or more; or
6) where the distance between origin and destination exceeded 1500 miles, or if a single line movement, 1200; or
7) where the commodity moving under the rate customarily moved in bulk shipments.\(^\text{17}\)

Evidence relevant to the seven fact situations could be presented by the carrier proposing a rate increase and by a shipper challenging it.

Several executive agencies attacked the notice, arguing that it did not represent the basic objectives of the 4R Act and urging that regulation of these rate increases be liberalized.\(^\text{18}\) The Commission reduced the number of presumptions from the original seven to four by dropping presumptions 4, 6 and 7 entirely from its preliminary list compiled in the notice and altering or combining numbers 1, 2, 3 and 5. In the subsequent interim report, a presumption of lack of competition was held to arise:

1) when a carrier participating in a rate, or, in such discussion, or consideration, does not provide effective competition to the proponent rail carrier for the involved traffic or movement; or
2) when the carrier has handled 70% or more of the traffic affected by the tariff change during the year before the new rate was filed; or
3) when the rate in question exceeds the variable cost of providing the service by 80% or more; or
4) when a shipper or consignee protesting a rate can establish that it has made a substantial investment in railroad equipment that prevents or makes it impractical to use another carrier or mode.\(^\text{19}\)

Furthermore, in a reversal of prior policy, the burden of going forward with the evidence under these circumstances was shifted from the protesting shipper to the proponent carrier. The Commission allowed twenty days for interested parties to comment on the changes made before it issued its final set of rules.

This interpretation of market dominance was still considered by many to miss the thrust of the original legislation. The Report was deemed vague as to whether market dominance could be found to exist unless one of the four presumptions pertained. The Commission further scrutinized all of the


\(^{18}\) Barber, supra note 16, at 10-11. The Attorney General, the Department of Transportation, and the Federal Railway Administration were among those who filed recommendations as required by § 202 of the 4R Act. These groups maintained that most of the new rate increases would trigger the market dominance threshold test as it was then worded. The Attorney General recommended that all the rebuttable presumptions put forward in the notice be either rejected or substantially reworked.

responses it received and issued final rules in Ex Parte No. 320 on September 20, 1976.20

D. Ex Parte No. 320: Special Procedures for Making Findings of Market Dominance as Required by the Railroad Revitalization and Regulatory Reform Act of 1976

In Ex Parte No. 320, the Commission announced a three, as opposed to four, criteria test for establishing a rebuttable presumption of market dominance. Market dominance will be presumed to exist in the following situations:

1) where the market share of the proponent carrier equaled or exceeded 70% of the involved traffic or movement during the preceding year; or

2) where the rate exceeds 160% of variable costs of providing the service; or

3) where the affected shippers or consignees have made a substantial investment in rail-related equipment or facilities which prevents or makes impractical the use of another carrier or mode.21

The Commission further stated that a "rebuttable presumption will arise that a carrier participating in the rate or in such discussion or consideration [under a rate of bureau agreement] does not provide effective competition to the proponent rail carrier."22 Even under these presumptions, the shipper must meet its burden of persuasion at the suspension level by presenting evidence from which the Commission may find that the rates are unreasonable.23

These regulations had an enormous effect on the entire railroad industry. Originally, the Commission sought to presume market dominance in every case where overt collusion was present, such as when a rate was discussed or agreed upon in a rate bureau. This stance was later relaxed in the Commission's final rules so that the presumption was limited to actions within the bureau's formal realm of activity.24

The market share test was based on rulings in previous antitrust cases stating that if the competitors of the railroad in question possessed one-third or more of the traffic, service on a competitive level was probably feasible. The Commission modified the rulings of these antitrust cases and set its target level to require that a carrier would be presumed dominant when it


21. Id. at 23. These tests will be respectively referred to as the market share, variable costs and substantial investment tests.

22. Id. at 23.


24. See Ex Parte No. 320, supra note 20, at 16.
acquired 70% or more of the market. The Commission further ruled that once a case was decided, the market conditions were presumed to remain unchanged until the Commission made a different determination.\(^\text{25}\) Although the Commission was content to merely measure the magnitude and nature of changes in a given market, shippers seemed more concerned with the actual conditions and the continuous adjustment process that occurred in that market.

At the request of many shippers, the second presumption, the variable costs test, was substituted for the fully allocated cost test.\(^\text{26}\) The Commission finally decided that a variable cost test would more accurately reflect the absence of effective competition. It used Rail Form A costing procedures to apply this test.\(^\text{27}\) According to research carried out by the Commission, a ratio of revenue to variable costs between 140 and 150% appeared to be the highest level of minimal market power.\(^\text{28}\) To allow for error, the Commission then assumed market power would appear when a rate exceeded the variable costs by 160%. A rate beyond this level would suggest that market forces did not determine the rail carrier's prices.

The purpose of the third presumption, the substantial investment test, was to protect shippers which had become "captive" due to their heavy investment in rail-related facilities. In using this test, the Commission would consider the size of the investment in relation to the shipper's total costs. This test was included to prevent railroads from exploiting the advantage of being the only transporter of a shipper's goods. The railroads challenged this test on the grounds that it lacked any rational basis; the railroads believed that many supply and demand conditions of equal importance were being overlooked in forming the regulations for captive shippers.


\(^{26}\) Commission Fixes Four Presumptions for Ruling in Market Dominance Cases, TRAFFIC WORLD, August 30, 1976, at 13. A variable cost fluctuates with the business output (e.g. the total cost of materials). Fully allocated costs are those variable costs incurred to produce a particular unit plus a percentage of the business' fixed costs (e.g. rent).

\(^{27}\) The use of Rail Form A costing procedures for determining market dominance created problems for practitioners because:

(1) [its] costs are based on the average costs for all movements on a given railroad;
(2) the use of [this] information always will be retrospective in that costs are derived from accounting data pertinent to operations of the previous year(s);
(3) [its] distributional procedures assumed that all traffic utilized the same vintage mix of plant and equipment;
(4) [a]dditional complications are associated with the manner in which long-run variable costs are estimated; and
(5) [p]ricing according to [its] computed costs gives no recognition to the competitive conditions, the quality of services being offered, the price elasticities of market demand, or to revenue needs.

Boske, supra note 25, at 301.

On October 5, 1977, the Commission issued a report to Congress that was prepared in accordance with section 202(g) of the 4R Act. Section Two of the report dealt with the evaluation of the market dominance provisions. The assumptions, biases and results of Ex Parte No. 320's effectiveness were discussed and estimates of the rail traffic likely to trigger the threshold tests were presented. The Commission estimated that between 48.5 and 70% of interstate traffic then carried by the railroad industry would meet the threshold conditions.

Following the implementation of these tests, the Commission received numerous protests to rate filings that involved claims of unreasonableness. The Commission, however, could not attempt to make a market dominance finding on a number of the cases because the protestant failed to follow procedures laid out in Ex Parte No. 320. Of the successful protests, the market share presumption, which was the most restrictive of the three tests, was used most often to establish market dominance. Several of the markets in cases involving this criterion were found to be captive and the railroads were therefore considered to have market dominance. As of May 1, 1978, market dominance had been found in 36 out of 227 rates protested, with 16 of these rates eventually suspended. The protestant proved injury in 14% of the cases due to unreasonably high rates.

Several firms, principally railroads and power companies, challenged the applicability of the market dominance tests in the courts. In May of 1978, the Court of Appeals for the District of Columbia ruled against the railroads, basing their decision on the Commission's "presumed expertise" in the area of railroad ratemaking. The court assumed that, because this was an untested area of regulation, the Commission's rules and procedures should stand until they could be improved upon at a later date.

E. OTHER COMMISSION DECISIONS CONCERNING MARKET DOMINANCE

In April of 1979, A.T. Kearney, while under contract with the Commission to perform an in-depth analysis of market dominance, released its second interim report. This report presented empirical research and analysis of market dominance and compared alternative approaches to its implementation. Based on the data collected, A.T. Kearney concluded that less than five percent of the nation's rail traffic could be considered market dominant under the rebuttable presumptions. Consequently, it concluded that reserv-

30. Id. at 43.
32. Id. at S-8.
ing maximum rate regulation for noncompetitive traffic was theoretically and practically sound.\textsuperscript{34}

The Commission continued to accept suggestions and comments for revisions in their scheme to improve the market dominance regulations. It realized that the standards and procedures utilized in rulemaking proceedings needed to be modified, revised, or refined to the point where actual market competition was being regulated. The Commission continually reviewed cases brought before it and reexamined its tests in order to develop a coordinated and practical approach to market dominance. The Commission also attempted to minimize unnecessary rate regulation. On February 5, 1979, it issued the first of several notices that helped clarify its position on the presumptions stated in its rules of market dominance.\textsuperscript{35} These policy statements formed the basis for the Commission's stand until the passage of the Staggers Act in 1980.

In issuing a Clarification of Prior Decisions, the Commission reaffirmed its previous position on the use of the variable cost test. The cost presumption indicated, with reasonable accuracy, specific markets in which railroads had market power. The Commission concluded that the variable cost test was a useful tool and that it would continue to be utilized in findings of market dominance. The rebuttable presumptions were not meant to be absolute barriers to rate innovations and the railroads were still considered to have considerable pricing flexibility under the presumptions.

The Commission also expanded, for a short time, its definition of "market" in market dominance cases to include the international markets. In its \textit{Coleto Creek} decision of January, 1980,\textsuperscript{36} the Commission found that none of the three rebuttable presumptions was established by the protestant and therefore refused to review the reasonableness of the rate at issue. It determined that the railroads in question faced effective competition from foreign coal suppliers. Prior to this decision, overseas suppliers had not been considered in maximum rate cases. The \textit{Coleto Creek} fact pattern was not unique, and therefore, the decision could be applied to a wide range of cases involving other markets or other products.\textsuperscript{37}

The \textit{Coleto Creek} decision made it more difficult for shippers to establish that a carrier dominated a market because of the potential for competition from the international marketplace. The relevant geographic market, then, could easily have been defined as the global market. However, this decision was to prove of little consequence; the Commission decided to change the criteria it would use in market dominance cases.

\textsuperscript{34} A.T. Kearney, Interim Report II, supra note 5, at IX-4.


\textsuperscript{36} Incentive Rates on Coal—Axial, CO to Coleto Creek, TX, 362 I.C.C. 572 (1980).

\textsuperscript{37} Boske, supra note 25, at 306.
F. Ex Parte No. 320 (Sub-No. 1)

On January 17, 1980, the Commission issued a notice that made substantial revisions in the regulations which pertained to the determination of market dominance.\textsuperscript{38} The Commission intended to eliminate two of the presumptive tests, the market share and substantial investment tests, and modify the third, the variable costs test. Revisions incorporated recent experience and attempted to provide a clear and predictable measure of what the Commission's response would be to any market dominance case brought before it. The new standards required the party with the burden of establishing market dominance to make a prima facie case that the condition did in fact exist.

A prima facie case of market dominance under Ex Parte No. 320 (Sub-No. 1), required evidence which indicated that "the rate for the traffic or movement exceeded 180% of the variable costs of providing the service."\textsuperscript{39} If the evidence indicated that the rate in question was less than 180% but more than 150% of variable costs, no assumption would be made as to the competitive circumstances. In addition, if the evidence indicated that the rate was less than 150% of variable cost, a prima facie case would be established that no market dominance existed. Furthermore, a zone of reasonableness for rate increases, within which a rate could not be suspended, was established. A rate increase under these circumstances would not be suspended: 1) if the rate was equal to or less than 150% of the variable cost ratio; or 2) if the rate increase was less than a 7% increase annually.\textsuperscript{40} Finally, the limited rate bureau assumption was retained and the issue was to be discussed under a new set of rules that restricted rate bureau activity.

The new threshold conditions continued to utilize information from Rail Form A of Ex Parte No. 338\textsuperscript{41} despite its drawbacks. The upper level of 180% of variable cost was based upon the Commission's experience that a rate in question above this level required further examination; the lower limit of 150% of variable cost was considered to be a close approximation of fully allocated to variable costs. The threshold levels assisted the railroads in obtaining adequate revenue levels and removed another segment of the industry (seeking rate increases which left the rate below 150% of variable costs) from rate regulation.

The burden of proof principle was addressed at length by the Commission in order to clear up any ambiguities that may have arisen over the

\textsuperscript{39} Id. at 3357.
\textsuperscript{40} Id.
\textsuperscript{41} Standards and Procedures for the Establishment of Adequate Railroad Revenue Levels, 358 I.C.C. 844 (1978).
years. In a rate suspension proceeding for market dominance, the burden of persuasion remained on the party that had the burden of proving reasonableness, the proponent. The protestant had to persuade the Commission that the railroad’s information was not accurate or that it was interpreted incorrectly. The burden of proof could be substantiated with any relevant information that either proved or disproved the existence of market dominance for the rate at issue.

Later in that same year, A.T. Kearney submitted their final report to the Commission. The report’s purpose was to help the Commission refine its approach to market dominance and has been cited several times in its deliberations concerning market dominance. Market dominance was an important consideration in the Commission’s railroad ratemaking policies by 1980. However, these new rules were short-lived because Congress amended the 4R Act in 1980, removing this area from the Commission’s jurisdiction.

G. The Staggers Rail Act of 1980

Substantial changes in the procedural aspects of market dominance were advanced in both the Senate bill, and in the later House amendment, prior to passage of the Staggers Act. The Senate bill proposed a jurisdictional threshold level below which the Commission would not have authority to regulate railroad rates. A determination of a maximum reasonable rate was to be based on:

1) the amount of traffic which was transported at revenues below variable cost and efforts made to minimize such traffic; and

2) the amount of traffic which contributed only marginally to fixed costs; and

3) the carrier’s mix of rail traffic to determine whether one commodity was paying a disproportionate share of a carrier’s overall revenues.

The House amendment to the Senate bill required that revenues exceed costs by at least 160% before the Commission would have jurisdiction to determine whether the rail carrier dominated a market. This jurisdictional threshold was expected to increase by five percent in each subsequent year through 1984. The House amendment would also have established a “cost recovery percentage” as the price ratio at which the

45. Id. at 4122.
industry could recover its costs.\textsuperscript{46} The Staggers Act as signed into law by President Carter on October 14, 1980, limited the Commission’s authority to those maximum reasonable rates that were set above a threshold level of 160% of variable costs.\textsuperscript{47} But the Act still required the Commission to determine whether a railroad had market dominance before it could examine the reasonableness of the rate in question. Reasonable rates were defined in section 10701a(3) of title 49. The Commission had to find that a carrier did not dominate a market if the price-to-cost ratio for the period beginning on October 1 of one year and ending on September 30 of the next year was below:

1) 160 percent during the 1980-81 period; and
2) 165 percent during the 1981-82 period; and
3) 170 percent during the 1982-83 period; and
4) 175 percent or the cost recovery percentage (whichever is less) during the 1983-84 period; and
5) the cost recovery percentage for each 12 month period beginning on or after October 1, 1984.\textsuperscript{48}

The cost recovery percentage, which was to establish the relevant rates at a percentage between 170 and 180% of revenue to variable costs, was to be determined by the Commission at a later date. If a rate was above the lower threshold level and was challenged by a shipper, the rate in question would no longer be presumed to have been set by a market dominant carrier. Under these circumstances the question of market dominance, as well as reasonableness, would be settled by the Commission on a case-by-case basis. A carrier would be shown to have market dominance if the rate at issue was demonstrated to be above the threshold.\textsuperscript{49} If market dominance was not found, the rate would then be considered reasonable and removed from the Commission’s jurisdiction.

\textbf{H. Burden of Proof Under the Staggers Act}

The primary burden of proof was shifted from the shipper to the carrier. A railroad proposing a rate increase had to prove that its price-to-cost ratio was below the threshold level for that year. Data from Rail Form A or any other valid costing approach could be used. Once the carrier demonstrated that the rate was below the threshold it established a prima facie

\textsuperscript{46} Id. at 4123. The “cost recovery percentage” would have established only the limits of the Commission’s jurisdiction. Above the threshold, emphasis would have been placed on the revenue adequacy of the movement.
\textsuperscript{49} The Uniform Railroad Costing System (URCS) will replace Rail Form A as the Commission’s primary railroad regulatory costing tool after it has been properly tested and reviewed.
case. A shipper then would have to refute the carrier’s claim and show that the rate in question was above the threshold by either (i) restating the carrier’s figures in a more accurate fashion; or (ii) by presenting a more accurate and reliable method of cost determination. 50 A rate above the lower threshold could be challenged by a shipper, who would have to prove that market power existed or that no transportation alternatives were available.

The Commission could only bring an action independent of a shipper’s complaint when a rate increase placed a rate above the upper threshold or twenty percentage points above the lower price-to-cost threshold, subject to a ceiling of 190%. 51 In addition, any interested party could initiate an independent complaint. In these cases the carrier had the burden of proving the nonexistence of market dominance. If a railroad could not conclusively show that it did not have market dominance, the Commission would proceed to rule on the rate’s reasonableness. On the other hand, if the railroad managed to prove that market dominance did not exist, the rate would go into effect without alteration.

Congress created these new standards for market dominance determinations because it judged the Commission’s previous tests to be restrictive and complex. Congress believed that the railroads would not be able to extract monopoly profits once the protective standards in the Staggers Act were in place to protect the shipper against prior abuses. In addition, these revised requirements implied that the Commission should be more flexible in its interpretation of the law because Congress wanted the railroad industry to achieve adequate returns as soon as possible. Consequently, greater discretion was given to the Commission so that it could modify its procedures for regulating maximum rates for an increasingly competitive industry.

I. Ex Parte No. 320 (Sub-No. 2)

The Commission withdrew Ex Parte No. 320 (Sub-No. 1) because the Staggers Act achieved the same result that the Commission was striving for in its revenue-to-cost ratio. The passage of the 4R Act in 1976, and the Staggers Act in 1980, clearly narrowed the Commission’s rate control jurisdiction. One of the Commission’s primary tasks after passage of the Staggers Act was to interpret and to implement the provisions of section 202. On December 11, 1980, just one week before it withdrew Ex Parte No. 320 (Sub-No. 1), the Commission issued Ex Parte No. 320 (Sub-No. 2). 52 This policy statement significantly altered the Commission’s procedures for determining market dominance.

The Commission's new position of rate reregulation enabled it to design rules more consistent with the intent of Congress and the relevant sections of the Staggers Act, as well as with the prevailing "deregulatory" mood of the day. The thrust of Ex Parte No. 320 (Sub-No. 2) was to allow the railroads to set the majority of their rates outside of the Commission's control of maximum rates.

Ex Parte No. 320 (Sub-No. 2) reflected the Commission's belief that there was no real need for the use of presumptions in the determination of market power because they did not enhance the accuracy of its findings. The presumptions had stressed quantitative rather than qualitative evidence and had become inappropriate for determining market dominance. The cost test had been superseded by section 10701a of the Staggers Act. The market share test was abandoned because of its inability to deal with highly complex factual situations. The substantial investment test was found to be an inefficient base for a presumption of market dominance because shippers were unable to link pertinent rail-related investments to the lack of other adequate transportation alternatives. In addition, Congress' new policy concerning contract rates (section 208 of the Staggers Act) further diminished this presumption's relevance. Only the limited rate bureau test, which was originally intended to be just an evidentiary tool for determining market dominance, remained, because the Commission believed that rate bureau activity automatically lessened competition. Thus, the Commission dropped the use of general standards for an approach more case specific, clearing the way for a new set of rulings and policy statements.

J. GUIDELINES FOR SUBMITTING EVIDENCE

In the place of the rebuttable presumptions, the Commission issued new rules in Ex Parte No. 320 (Sub-No. 2). The Commission's decision listed a set of evidentiary guidelines to be used in finding market dominance. These standards were intended to encourage the submission of more reliable and accurate evidence. The Commission also decided that evidence of geographic and product competition could be presented. 53

These guidelines were separated into four major categories of competition: (i) intramodal competition; (ii) intermodal competition; (iii) geographic competition; and (iv) product competition. Each factor was to be a mandatory requirement. Evidence of each could be used by the carrier to disprove the presence of market dominance in a rate dispute.

The Commission defines intramodal competition as competition be-

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tween two or more railroads transporting the same commodity between the same origin and destination, depending upon:
1) the number of rail alternatives;
2) the feasibility of each rail alternative as indicated by: a) the physical characteristics of the associated routes and; b) by the direct access of both shipper and receiver to the alternatives;
3) the transportation costs associated with each alternative (to determine if actual use of alternatives is due to excessive rates);
4) collective ratemaking among the railroads associated with the rate as evidenced by rate bureau involvement; and
5) evidence of substantial rail-related investment or long-term supply contracts (contracts signed before October 1, 1980, will be given more weight).54

As opposed to intramodal, intermodal competition is competition between rail carriers and other modes for the transportation. Intermodal competition for railroads exists primarily with the motor and water carrier industries, and this guideline was constructed to deal with each of these modes separately. The Commission required that evidence presented by any carrier to indicate competition between rail and water alternatives should show such factors as:
1) the number of alternatives;
2) the feasibility of each alternative as indicated by: a) the physical characteristics of the transportation routing; and b) the access of both shipper and receiver to each alternative; and
3) the transportation cost of each alternative.55

In addition, the Commission indicated that any evidence to be used in establishing effective competition between rail and motor alternatives should refer exclusively to the nature of the product and the needs of the shipper or receiver involved in the movement. Under these circumstances, effective competition could be deduced from information that indicated:
1) the amount of the product in question is transported by motor carrier where rail alternatives are available;
2) the amount of the product that is transported by motor carrier under transportation circumstances similar to rail;
3) the amount of the product that is transported using motor carrier by shippers with similar needs (distributional, inventory, etc.) as the shipper protesting the rate;
4) physical characteristics of the product in question that may preclude transportation by motor carrier; and

54. Id. at 131-35.
55. Id. at 133.
5) the transportation costs of the rail and motor carrier alternative.  

The third substantive guideline, geographic competition, refers to the ability of a shipper or receiver to obtain the product from another source or to ship to another destination. The Commission stated that this form of competition was important for products whose delivery price represents a substantial proportion of transportation costs. Evidence used to establish the potential for such competition should concern:

1) the number of alternative geographical sources of supply or alternative destinations available to the shipper or receiver for the product;
2) the number of these alternative sources or destination served by the different carriers; and
3) the similarity of the product available from each source or required by each destination.  

The Commission explained that to determine whether effective competition of this type actually existed, evidence presented by the carrier should indicate the feasibility of each source or destination in addition to the likelihood of competition of this form. The following types of evidence could be submitted:

1) the distance associated with each alternative source or destination;
2) relevant physical characteristics of the route associated with each alternative;
3) the access of the shipper or receiver to each transportation alternative;
4) the capacity of each source (or destination) to supply (or absorb) the product in question;
5) the transportation cost associated with each alternative;
6) collective ratemaking among the railroads in question as evidenced by rate bureau involvement; and
7) evidence of substantial rail-related investments or long-term supply contracts (contracts signed before October 1, 1980, will be given more weight).  

The final evidentiary guideline is product competition, defined by the Commission as the ability of a shipper or receiver to use a feasible substitute for a particular product. The presence of available substitutes, according to the Commission, can be established by evidence that these substitutes are obtainable through other carriers or modes without substantially greater cost or transportation. The evidence submitted should concern:

1) the use of a substitute product by the receiver or shipper or by others with similar needs and under similar conditions;

56. Id.
57. Id. at 134.
58. Id.
2) the prices of the substitute products relative to the price of the original product;
3) the efficiency of the substitute product relative to the original product; and
4) the explicit and implicit transportation costs of the substitute product and the original product.\textsuperscript{59}

These guidelines are part of a program the Commission started after the passage of the Staggers Act to evaluate tariffs for exemption from rate regulation. The criteria are an integral part of the Commission’s “deregulatory” approach to handling the problems of the railroad industry. They provide both carriers and shippers with a general indication of the type of information the Commission is interested in. The lists are not intended to be exhaustive, nor is each fact a mandatory requirement. Railroads now have the opportunity to recoup more of their costs because the standards allow more room for selective and innovative rail pricing. Potentially, the railroads will be operating under more certainty than at any other time in this century, enabling them to market their services in a more efficient manner.

These substantive criteria, however, make it more difficult for the shipper to prove that a carrier dominates a market. The National Industrial Traffic League (NITL) was among several groups which argued that these standards would make it easier for carriers to raise their prices, as most rates would be outside of the Commission’s jurisdiction.\textsuperscript{60} The NITL felt that its members would not be able to accurately demonstrate their status as captive shippers. Consequently, the guidelines were challenged at the administrative level and in the courts in an attempt to reestablish a greater degree of protection from rate abuse.\textsuperscript{61} These efforts to block the use of the new evidentiary guidelines failed, and the criteria went into effect in August, 1981.

III. ADDITIONAL CONSIDERATIONS

The evidentiary guidelines promulgated in Ex Parte No. 320 (Sub-No. 2) seem better suited to effecting the regulatory reform intent than the Commission’s earlier presumptive standards. The degree of intermodal, intramodal, geographic and product competition should succinctly reflect the major factors affecting the elasticity of demand facing a rail carrier in a particular market. It is these factors which ultimately determine the workability of competition and the ability of the railroad to set rates. Although the market dominance principle now appears well-founded conceptually, certain

\textsuperscript{59} Id.

\textsuperscript{60} Shippers Fight to Save Ability to Contest Railroad Rate Boosts Before ICC, TRAFFIC WORLD, July 27, 1981, at 65.

\textsuperscript{61} Id.
measurement problems portend continued changes in the definition and application of the concept. The remainder of this article will explore possible solutions to some of these problems.

A. CRITICISM OF THE PRESUMPTIONS AND THRESHOLD TESTS

The standards developed under Ex Parte No. 320 (Sub-No. 1) were severely criticized by many different parties affected by their implementation. The main objection to the rebuttable presumptions referred to their generality; at least one of the presumptions would probably exist in any given case brought before the Commission. Because the rate regulations were vague, and potentially hazardous from the carrier’s point of view, the railroads approached the new "freedom" provided by the 4R Act with scepticism and did not take full advantages of its provisions.\(^{62}\)

The threshold tests, particularly the revenue-to-cost ratio test, proved to be less than adequate. While theoretically the best measures of rail dominance, these tests were only able to measure the average profit margin on sales, which is not necessarily correlated with degree of competition or return on investment. As shown in empirical research, the revenue-to-cost ratio is negatively correlated with other measures of rail market power.\(^{63}\) One plausible explanation is that relatively high ratios represent the vestiges of rail market power and subsequent value-of-service rate making techniques.

Charging high rates for expensive commodities and low rates for cheaper commodities was a viable pricing strategy prior to widespread intermodal competition. A combination of questionable managerial practices and ponderous regulation continued this process of differential pricing long beyond its usefulness as a railroad pricing strategy and as a basis of public policy. Indeed, high value commodities are vulnerable to motor carrier competition. Thus, high revenue-to-variable cost ratios may not be indicative of rail market dominance.

The inadequacies of historical rate-to-cost relationships are compounded by the inadequacy of rail costing techniques. According to L.B. Boske, the use of Rail Form A costing procedures as the basis of estimating variable cost only served to make matters worse. The average historic cost concepts used in Rail Form A are inadequate to determine market dominance.\(^{64}\)

B. MEASURING COST

The market dominance procedure, through revenue-to-variable cost

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63. Id. at VII-8.
64. Boske, supra note 25, at 304.
threshold levels, has increased the costing responsibility of the Commis-
sion. In response to the need for a more sophisticated costing system to
produce adequate costing results, the Commission moved to replace the
old costing mechanism, Rail Form A, with the Uniform Rail Costing System
(URCS). Although different from its predecessor in some respects, the
URCS resembles Rail Form A in many important aspects. Both costing
systems:

1) produce cost estimates based on the average cost of individual carriers
   or a group of carriers, or regional group of carriers;
2) incorporate an accounting-based approach to costing, relying on annual
   operating expense and traffic data reported by the carriers; and
3) rely on historic special studies to supplement the required annually re-
   ported operating expenses and statistics.\textsuperscript{65}

Rates should reflect prospective costs to arrive at decisions on future
operations. Since it relies on average historic system costs, the URCS may
prove inadequate for rate making purposes. Revenue-to-cost ratios must
be oriented toward the future cost of rail service and the overall investment
of the carrier in order to be of value in proceedings resolving issues of mar-
ket dominance.\textsuperscript{66} The URCS has yielded inconsistent results in its initial
application and may eventually be beset by the same problems which
plagued Rail Form A costs.

The URCS relies heavily on regression analysis to calculate the reve-
une-to-variable cost threshold level in market dominance proceedings. The
variable cost portion of operating expenses declined in 1978, 1979 and
1980 according to this analysis.\textsuperscript{67} The problem with this result is that as
the variable cost portion of operating expenses declines, the possibility that
a given rate will lie above the revenue-to-variable cost threshold level in-
creases. Instead of more rates lying outside the Commission’s jurisdiction,
potentially more rates will become subject to a full review under evidentiary
guidelines.

The Commission appears to be somewhat at a loss to explain the
changing behavior of railroad costs. The Commission’s Bureau of Ac-
counts, the group responsible for implementing the URCS, states that the
inconsistent nature of costs may be due to several factors.\textsuperscript{68} The answer
may lie in a fault in the regression or the format used, only making it appear
that variable costs are declining. If it is indeed a technical problem, the
URCS can be corrected. However, if the change reflects a fundamental

\textsuperscript{65} BUREAU OF ACCOUNTS, INTERSTATE COMMERCE COMMISSION, AN INTRODUCTION TO THE UNIFORM

\textsuperscript{66} A.T. Kearney, Interim Report II, supra note 5, at VIII-16.

\textsuperscript{67} ICC Reaches Cost System But Mulls Figures That Could Expand Rate Power, TRAFFIC
WORLD, June 28, 1982, at 28.

\textsuperscript{68} id.
shift in railroad operating structure the entire threshold test will have to be reconsidered, if not eliminated. Otherwise, the Commission, rather than the market, will be determining the reasonableness of the majority of rates. This regulatory scheme also has the drawback that it imposes substantial information requirements.

C. DATA GATHERING BURDEN

In submitting its final report on market dominance standards to the Commission, A.T. Kearney wrote that they "anticipate significant administrative [and legislative] impacts from [their] research."69 Apparently this study did have a significant impact, for a major portion of it is reflected in the Commission's evidentiary guidelines. Therefore, the market dominance guidelines can be evaluated in terms of the criteria suggested by A.T. Kearney:

1) easily understood approaches and requirements;
2) ready availability of required data;
3) minimum cost for data preparation;
4) emphasis on competitive forces to control maximum rates;
5) adequate provision for shipper protection if market forces are inadequate to provide that protection; and
6) minimized Commission involvement consistent with the public interest.70

In addition, any market dominance standard, or set of evidentiary guidelines, should ensure a regulatory system that balances the needs of carriers, shippers, and the public.

Railroads should have little difficulty in supplying the additional information necessary to defend a rate change proposal, at least with respect to the revenue-to-variable cost threshold levels established by the Staggers Act, due to the Commission's general reporting requirements. Although much of the cost information required by the guidelines is publicly available, it is not as readily accessible to the shippers as it is to the railroads. Lack of access to information, combined with other evidentiary requirements, place opponents of rail rate changes at a disadvantage to the railroad proposing the change. Asymmetric access to and burden of information gathering is inconsistent with a regulatory system designed to protect shipper interests if competition fails to do so. The NITL's rebuttal to evidentiary guidelines reflects concern for this type of regulatory failure. Furthermore, recent changes in the rate bureau's role in setting rates and the types of rate changes carriers can propose may cause the alleged inequities to increase.

Rail rate bureaus may not permit individual carriers to discuss, partici-

70. Id. at XI-6; see also Boske, supra note 25.
pate in, or vote on the single line rates of another carrier. With respect to interline movements, a carrier may only discuss, participate in, or vote on the applicable rate if it practically participates in that movement. After January 1, 1984, if there are interline movements over two or more routes between the same end points, rail carriers are not permitted to discuss, participate in, or vote on rates except with a carrier which forms part of a particular single route.\footnote{49 U.S.C. § 10706(a)(3)(A) (Supp. V 1981).} These changes should lead to an increased number of rates filed by individual carriers and provide for greater rate competition in rail markets. While potentially beneficial, these actions will require substantially greater use of the market dominance guidelines, thus increasing both time and cost in meeting data requirements.

In conjunction with limiting rate bureau antitrust exemptions, acceptable forms of rate proposals are being circumscribed. General or across-the-board rate increase proposals have reflected the rise in operating costs and decline in cash flows sufficient for capital expenditures since World War II.\footnote{D. Harper, Transportation in America: Users, Carriers, Government 465 (2d ed. 1982).} A general rate increase created to deal with these problems would obviously neglect the unique demand and supply conditions of a given market. As of January 1, 1984, general rate increases, currently limited to joint rates, are to be eliminated altogether;\footnote{49 U.S.C. § 10706(a)(1) (Supp. V 1981).} thus, unique market conditions must be incorporated in future rail pricing strategies.

In fiscal year 1980, the Commission received 63,113 railroad freight rate tariffs.\footnote{94 ICC Ann. Rep. 113 (1980).} The rate making changes outlined above will likely precipitate a greater number of individual rates being filed with the Commission, each of which must be measured against the revenue variable guidelines. Greater market-oriented pricing, then, may only exacerbate inherent information gathering burdens or inequities. These potential problems were at least partially recognized.

\section*{D. The Scope of Limited Regulation}

Several authors have advocated that the Commission move in the direction of reducing individual shipper and carrier data requirements.\footnote{A.T. Kearney, Final Report, supra note 43, at XI-7; Boske, supra note 25, at 307-10.} Common to these proposals is a programmatic approach to the market dominance principle whereby the Commission systematically, upon its own initiative, would review individual rail markets to assess the workability of competition. If a market is sufficiently competitive, rates would be presumed to be reasonable. If competition is not workable, the reasonableness of the rate in question would then be evaluated. Other than the
change in information gathering responsibility, these proposals would retain the concept of limited regulation. It appears that the Commission, if so disposed, could undertake this course of action.

Title 49 empowers the Commission to exempt any person, class of persons, or a transaction or service by a railroad upon a finding that regulation is not necessary to carry out the national (rail) transportation policy, and either the service is of limited scope or the regulation is not essential to protect shippers from the abuse of market power. Referring to the statement of rail transportation policy, we find that the policy of the U.S. government in the regulation of railroads is to allow, to the maximum extent possible, for competition and the demand for services to establish reasonable rates; and to maintain reasonable rates where there is an absence of effective competition and where rail rates provide revenues which exceed the amount necessary to maintain the rail system and attract capital.

To date, the Commission has used its exemptive powers extensively. When important traffic segments are considered, only the rail transport of fresh fruit and vegetables, miscellaneous agricultural commodities, and the rail portions of trailer-on-flatcar and container-on-flatcar service have been exempted. The exportation of coal moving by rail via Gulf and Atlantic ports, and rail boxcar traffic is being considered for exemption. These segments of traffic account for large portions of all intercity traffic moved by rail, and the granting of exempt status by the Commission would have a tremendous impact on ratemaking policies.

Several points emerge from the above analysis. First, the criteria by which all regulation is to be judged is very similar to the criteria A.T. Kearney suggested for judging any Commission-established guidelines. Second, those markets already exempted were designated as such in order to be consistent with the national rail policy; regulation was deemed unnecessary because either the service provided was of sufficiently limited scope or workably competitive markets had developed. Given the importance of TOFC/COFC traffic to rail carriers, it is safe to conclude that the effective competition is central to Commission exemptions. It appears, therefore, that there is little conceptual difference between the application of Commission exemptive powers and the market dominance concepts. If a traffic segment qualifies to be relieved of rate regulation under one measure, it should logically be relieved of regulation under the other as well. Thus,

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when regulatory reform advocates are convinced of the ubiquity and consequential benefits of rail market competition, exemptions from regulation may become more common, thereby circumventing the entire market dominance mechanism altogether.

E. OTHER PRICING CONSIDERATIONS

The effect of shipper bargaining power is currently not considered under a market dominance analysis. Empirical evidence suggests that the sources of this bargaining power are intramodal competition, multiplant capacity, availability of alternative sources of supply and attractiveness of the commodity in terms of carrier costs and services.82 The essence of shipper bargaining power is intramodal, geographic and product competition. Underlying the latter two factors is the availability of intermodal competition. These are the same four types of competition adopted by the Commission in Ex Parte No. 320 (Sub-No. 2).

Intramodal competition in the railroad industry is potentially significant, but at present cannot be relied on to protect shippers due to pricing agreements between railroads through rate bureau activity. However, intrarail competition, and therefore shipper bargaining power, should increase due to the rate making changes brought about the by Staggers Act. A recognition of this type of shipper bargaining power should be incorporated into any review of market dominance standards. Although contract service is at least nominal evidence of shipper bargaining power, no other recognition is found per se in the new guidelines. Carriers should be permitted to introduce shipper bargaining power as additional evidence of shipper alternatives for both geographic and product competition.83

In the future, market dominance standards should also reflect any special circumstances in rail movements. The Staggers Act attempted to incorporate such circumstances, at least with respect to seasonal traffic. This type of traffic is found in all regions of the country and on most Class I railroads. A major shortcoming of previous legislation, specifically the 4R Act, was that if any new rate was specifically labeled as a demand-sensitive or seasonal rate, the rate could automatically be subject to protest by shippers. The railroads then would be required to file supporting evidence, even when the movement was declared non-market dominant. However, A.T. Kearney believed that to ensure adequate carrier revenues legislation should integrate seasonal/peak concepts, and any revision in the market dominance standards must recognize the special needs of peak and seasonal pricing strategies.84 By eliminating the special designations for peak

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84. Id. at IX-8.
and seasonal rates of the 4R Act, the Staggers Act has moved in Kearney's recommended direction. Yet, it remains to be seen how the new guidelines meet these special needs, and if they will prove to be at all successful.

Questions also remain as to the correct implementation of market dominance provisions even should the guidelines incorporate the shipper bargaining power and seasonal/peak rate issues. Various alternatives advanced propose that an \textit{ex ante} determination of competitive markets be made by the Commission. With these allowances for special pricing considerations, presumably more use would be made of rate making freedoms than in the past.

IV. Conclusion

Current market dominance standards reflect both the Congress' and Commission's firm belief in the effectiveness and desirability of competition. In the current marketplace, railroads are seldom in a position to display monopolistic tendencies because competition is so pervasive. If the assumptions of regulatory reform are correct, pricing freedom will achieve the results intended: the rail industry would receive a reasonable rate of return on its investment while marketing its services in a competitive environment, and shippers would possess adequate protection against carrier rate making abuse through the application of the market dominance and the corresponding zone of reasonableness principles found in the Staggers Act.

If these assumptions prove wrong and competition fails to materialize, we may find that the railroads do in fact possess substantial market power and use specific rate increases and a differentiated rate scale to further a system of unequal pricing. Railroads would thus be able to exploit imperfections in the transport market to their own advantage, while remaining outside the Commission's jurisdiction or influence. In this event, legislation similar to that existing before passage of the 4R Act, or some viable alternative, may prove to be necessary to provide for judicious regulation.

However, the market dominance concept, as drafted in its present form, is sufficiently flexible to allow for increased regulation through reinterpretation of the law. It is this flexibility which assures continued evolution of not only the market dominance concept, but of rail economic regulation.

Predatory Pricing in the Airline Industry: A Case Study — The Policies and Practices of the CAB

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I. INTRODUCTION

This article examines the policies and practices of the Civil Aeronautics Board (CAB or Board) with respect to complaints involving predatory pricing. Those policies are muddled and the practices unfortunately unsuited to the demands of the air transportation market. The large amount of pub-

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licity engendered by the last several years of price warfare throughout the airline industry, particularly with respect to major or so-called glamour routes, such as the transcontinental and New York/Dallas routes; the precarious financial position of nearly all of the major airlines; and the recent spectacular collapse of Braniff, have all served to focus attention on the issue of predatory practices within the industry. The attitude and practices of the responsible government regulatory body should reflect this concern. Review of recent CAB Orders and Policy Statements, however, leads to the following conclusions:

(1) The concepts of unreasonableness, discrimination, and predation, while analytically discrete, are frequently treated in practice as being synonymous or as close complements;

(2) The CAB is clearly predisposed to find against the validity of any complaint charging predatory, discriminatory, or unreasonable pricing. In particular, the standards by which the CAB judges complaints of predatory pricing are, for all practical purposes, nearly impossible to meet;

(3) Finally, we present two theories which support the need for a full and formal investigation involving charges of predatory pricing. The first

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2. See infra Section IV.
3. In analyzing any potential case of predation before the CAB, one must make reference to the various sources of raw data available from the CAB. A short description of the types of documents and their utility to the practitioner follows.

All certified air carriers must file Forms 41 and ER 586 on a monthly basis. Form 41 contains financial and operating data concerning the carriers' 48-state operations. The information is available to the public in printed form. Form ER 586 contains services segment data for each carrier, including the load factors for each route flown. A separate Form ER 586 must be filed every month for each route a carrier services, and individual forms must be filed for each change in the type of service provided on a given route. So, for example, if a carrier operated three different types of aircraft on the same route during a given month, three separate forms would have to be filed. So, too, if a plane was forced to land at an unscheduled point along its normal route, due to inclement weather on a single occasion, a separate form would have to be filed. The data contained in Form ER 586 is available only on magnetic tape; these tapes may be purchased from the CAB, and can be read by an IP Sharp terminal.

The CAB also compiles, on a quarterly basis, Origin and Destination (O&D) Surveys, which are surveys of 10% of all passengers emplaned in all markets (city-pairs) served by certificated air carriers. Included in the Surveys are absolute numerical, and percentage, figures for each carrier's passenger traffic in a given market, both for the current quarter and for year-to-date. Bound volumes of all Surveys are available in the CAB's library. All O&D Survey data is also available on magnetic tape.

A Costing Methodology manual, describing in great detail the current methodology used by the Board in estimating fully allocated and marginal costs for a given market, is available from the CAB's Office of Economic Analysis, as are other useful pamphlets.

The CAB's library contains, among other things, all bound CAB Reports through 1977, the bound O&D Surveys, a full range of industry literature and the legislative history of the Federal Aviation Act of 1958, as amended by the Airline Deregulation Act of 1978. Copies of all CAB publications, including Orders and Regulations issued within the last twenty four months, are avail-
possibly successful theory focuses on a case in which a competitor targets the complainant’s most lucrative markets; the second focuses on the complainant’s potential bankruptcy as a result of predatory pricing. The following pages review the history and development of the CAB’s policy with respect to predatory pricing and the rationale behind its current position.

II. GOVERNING LAW

Section 1002(d) of the Federal Aviation Act of 1958 (the Act) provides inter alia:

(1) Except as provided in paragraph (2) or (4) of this subsection, whenever, after notice and hearing, upon complaint, or upon its own initiative, the Board shall be of the opinion that any individual or joint rate, fare, or charge demanded, charged, collected or received by any air carrier . . . is or will be unjust or unreasonable, or unjustly discriminatory, or unduly preferential, or unduly prejudicial, the Board shall determine and prescribe the lawful rate, fare, or charge (or the maximum or minimum, or the maximum and minimum thereof) thereafter to be demanded, charged, collected, or received, or the lawful classification, rule, regulation, or practice thereafter to be made effective.

(3) Whenever, after notice and hearing, upon complaint, or upon its own initiative, the Board shall be of the opinion that any individual or joint rate or charge demanded, charged, collected, or received by any air carrier . . . is or will be unjustly discriminatory, or unduly preferential, or unduly prejudicial, or predatory the Board shall alter such rate, charge, classification, rule, regulation or practice to the extent necessary to correct such discrimination, preference, prejudice, or predatory practice.

(4) The Board shall not have authority to find any fare for interstate or overseas air transportation of persons to be unjust or unreasonable on the basis that such fare is too low or too high if —

(B) with respect to any proposed decrease filed after October 24, 1978, the proposed fare would not be more than 50 per centum lower than the standard industry fare level for the same or essentially similar class of service, except that this provision shall not apply to any proposed decrease in any fare if the Board determines that such proposed fare would be predatory.4

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(2) The following provisions of this chapter (to the extent such provisions relate to interstate and overseas air transportation of persons) and the authority of the Board with respect to such provisions (to the same extent) shall cease to be in effect on January 1, 1983:
"Predatory" is defined in section 101 of the Act as meaning "any practice which would constitute a violation of the antitrust laws as set forth in section 12 of title 15."5

Section 411 of the Act, which was modeled on section 5 of the Federal Trade Commission Act, provides that the CAB has the authority to investigate and resolve complaints involving charges of "unfair or deceptive practices" or "unfair methods of competition."6 In interpreting section 411 in Air Florida v. Eastern Air Lines (Air Florida II), the Board stated:

As a result of the Airline Deregulation Act of 1978, P.L. 95-504, 92 Stat. 1705 (October 24, 1978), the Board must rely primarily on competition rather than regulation as the means of obtaining the best possible air transportation system. Sections 102(a)(4), (9) of the Act, 49 U.S.C. 1302(a)(4), (9). Accordingly, we doubt that we should use Section 411 as a means of imposing our views of competitive propriety on airline industry fare reductions except where a practice is deceptive, illegal (whether under the antitrust laws, the Act, or another statute), or offensive to a well-established public policy.7

The Board went on to cite certain passages of the Senate Report8 accompanying the Act for the proposition that "Congress did not intend us to hold fare reductions unfair which [do] not violate the antitrust laws."9 In summary, then, the CAB has attempted to distinguish three analytically distinct types of pricing behavior, i.e., reasonableness, discrimination, and predation. CAB practice in defining each of these areas is discussed below. Unfortunately for certain airlines and for consumers on certain routes, the distinction among the three has not been clearly delineated by the Board.

III. CAB PRACTICE

A. REASONABLENESS

Any fare which falls within the "zone of reasonableness" established by section 1002(d)(4) of the Act is not subject to suspension or to the

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(B) Section 1374 of this title (except insofar as such section requires air carriers to provide safe and adequate service).

(D) Sections 1462(d)(1) and (d)(2), (e), (g), (h), and (l) of this title.


7. CAB Order No. 81-1-101, at 10 (June 21, 1980) [hereinafter cited as Air Florida II].


Board's jurisdiction over the justness and reasonableness of fares.\textsuperscript{10} The Board implemented the mandate of section 1002 in its Policy Statement 80 (PS-80).\textsuperscript{11} Based primarily on the profitable lowfare experiences of Southwest Airlines and Pacific Southwest Airlines, the Board provided that "[e]ac'h carrier should have the opportunity to set fares in each market [or city-pair] within a zone ranging to 50 percent below the ceiling fare."\textsuperscript{12} Furthermore, carriers are allowed to set fares in each market at seventy percent below the ceiling fares on forty percent of their weekly available seat miles (ASM), thus allowing lower prices for "off-peak" periods. No fares set within this zone will be suspended by the Board on account of the fare's reasonableness absent the following extraordinary circumstances:

(1) The high probability that the fare would be found to be unlawful after investigation;

(2) \textit{There is a substantial likelihood that the fare is predatory} so that there would be an immediate and irreparable harm to competition if it were allowed to go into effect;

(3) The harm to competition would be greater than the injury to the traveling public if the proposed fare were unavailable; and

(4) The suspension is in the public interest.\textsuperscript{13}

Obviously, then, absent a clear indication that a challenged fare is predatory, it will never be subject to suspension by virtue of being unreasonable. So, for example, if a carrier were to offer a "substantial" discount fare between Denver and Dallas, similar to that offered by certain carriers periodically during 1981, it would not be subject to suspension or review as long as it fell within the zone of reasonableness.\textsuperscript{14} It is approximately 647 miles

\textsuperscript{10} Air Florida II, supra note 7, at 3.


\textsuperscript{12} The "ceiling fare," as it is designated in PS-80, or "standard industry fare level" (SiFL), as it is designated in § 1002 of the Act, is the lowest unrestricted competitive fare in a given market that was in effect on July 1, 1977, adjusted not less than semi-annually by the "percentage change in actual operating costs per available seat-mile (ASM) for interstate and overseas transportation combined." Establishment of the Interim Industry Fare Level, CAB Order No. 80-12-96 (December 18, 1980) (establishing the SiFL formula effective January 1, 1981).

\textsuperscript{13} 14 C.F.R. § 399.32(b) (1983) (emphasis added).

\textsuperscript{14} The stark SiFL "50%" rule represents a legislated figure which is completely detached from any consideration of an individual firm's marginal, average variable, or average total, costs. Moreover, it ignores the fact that "a detailed case-by-case analysis associated with a rule-of-reason approach permits consideration of the variety of specific structural and behavioral aspects of the particular dominant firm's situation that are relevant to a determination of whether the firm was violating the antitrust laws. The rule-of-reason approach . . . allows the decisionmaker to go beyond loose language and mechanical rules to the specific conduct of the dominant firm and the implications of that conduct for economic efficiency and other goals of antitrust law." Joscow & Kleverick, A Framework for Analyzing Predatory Pricing Policy, 89 YALE L.J. 213, 216-17 (1979) (footnote omitted) [hereinafter cited as Joscow-Kleverick]. See Scherer, Predatory Pricing and the Sherman Act: A Comment, 89 HARV. L. REV. 869 (1976) [hereinafter cited as Scherer]. Scherer,
between Denver and Dallas. Utilizing the prevailing SIFL formula,\textsuperscript{15} we find that the current SIFL for the Denver/Dallas city-pair is $108.57 (rounded to the nearest penny); fifty percent of the SIFL is approximately $54.29, or less than any of the seemingly ultralow fares, including Delta's $59.00 fare, that were offered, one-way during 1981.\textsuperscript{16} Accordingly, a discount fare, absent clear evidence of predation or discrimination, would not be subject to a charge of unreasonableness. Furthermore, pursuant to ER-1072,\textsuperscript{17} any carrier establishing a fare within the zone of reasonableness need not submit economic data in justification of the new fare.

B. DISCRIMINATION

Policy Statement 93 (PS-93)\textsuperscript{18} establishes the CAB's policy on price discrimination. To begin with, discrimination is defined in PS-93 as "the act of charging different customers prices that differ by varying proportions from the costs of serving them." The Board then goes on to state:

In our notice, we recognized the fact that the industry's existing fare structure may contain elements of price discrimination for a variety of reasons which include regulatory considerations as well as the economic conditions of supplier market power and differing consumer price sensitivity. Among the regulatory factors are the Board's willingness to permit discounted fares that may not correspond to airline cost savings, so long as they are available to any passenger who complies with ticketing restrictions, and the Board's decision to construct the Standard Industry Fare Level on a system basis without taking into account factors other than mileage that affect costs.\textsuperscript{19}

Accordingly, the Board announced that it would find a fare to be unreasonably discriminatory only if:

1. There is a reasonable probability that the rate will result in significant long-run economic injury to passengers or shippers;

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\textsuperscript{15} The 1981 SIFL used in the example consisted of a flat terminal charge of $24.97, plus $1.366/mile for each of the first 500 miles, plus $1.041 for each of the next 147 miles.

\textsuperscript{16} Cf. the discussion of promotional pricing in Areeda-Turner, supra note 14, at 713-15.

\textsuperscript{17} 43 Fed. Reg. 39,536 (1978) (amending 14 C.F.R. § 221.165(d)(4)).


\textsuperscript{19} PS-93, supra note 18.
(2) The rate is in fact discriminatory according to a reasonable cost allocation or other rational basis;

(3) The rate does not provide transportation or other statutorily recognized benefits that justify the discrimination; and

(4) Actual and potential competitive forces cannot reliably [sic] be expected to eliminate the undesirable effects of the discrimination within a reasonable period.20

In essence, therefore, a complainant must show not only that a rate or fare is discriminatory, but also that injury results from the discrimination and that the situation will not be corrected by the action of competitive market forces alone. The necessary injury must be to the public ("passengers" or "shippers") or to the forces of competition generally; one carrier's loss is probably insufficient. The CAB, in adopting this policy, rejected the argument that legitimate low-fare pricing would be frustrated due to cross-subsidization of discriminatory rates by revenues from supra-normal fares established elsewhere, on the following basis:

It is assumed that a large carrier will set prices above cost in markets where it enjoys market power in order to underwrite markets where it competes against a smaller low-fare innovator. However, in the competitive environment which our policies are fostering, this source of funds would evaporate as the new competitors are attracted into high profit markets. Furthermore, the incentive for such predatory pricing, the prospect of charging substantially higher fares after the smaller competitor is driven from the market, will also be reduced as entry freedom increases the likelihood that a new competitor would enter the market to undercut the excessive fares.21

This decision was predicated on an assumption that after deregulation, entry could be presumed to be free enough so that competitors would arise to fill the vacuum created by departure of a carrier from a market.22

The leading CAB decisions in the area of discrimination involve complaints stemming from the Transcontinental Low-Fare Route Proceeding.23 The complaints filed pursuant to Transcontinental were instituted by World Airways, World Transport Development Cooperative, and Amos E. Heacock, d/b/a Air Transport Association, challenging the new discount fares between New York/Newark and Los Angeles/San Francisco, which were approved by the Board for Pan American, American, United, National and TWA in direct competition with World's standard low fare. The complaints involved charges both of predation24 and of discrimination. Complainants' primary discrimination arguments were addressed by the Board in New

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21. PS-93, supra note 18, at 36,061.
23. 80 C.A.B. 316 (1979) [hereinafter cited as Transcontinental].
24. See infra text accompanying notes 26-34.
York-Los Angeles Fares of Pan American World Airways (Pan American).\(^{25}\)

Based on PS-93 and Pan American, it is unlikely that a complaint based on a claim of discrimination would be subject to a full formal Board investigation to the extent that it relied on theories of cross-subsidization or of impermissible travel restrictions that affected only certain classes of passengers or certain routes. Furthermore, it would be extremely difficult to prove the probability of significant long-run economic injury to passengers or shippers, as opposed to injury to a competitor, in the absence of evidence of predation. Accordingly, only the third and crucial area of our analysis, predation, remains as a potentially viable cause of action.

C. Predation

The CAB is predisposed to find against claims of predation.

Predatory pricing would . . . be impossible under airline reform. Such pricing tactics by the larger airlines are only sensible if a competitor, once driven out of a market, cannot reenter it. Only then can the predator raise his prices (and his profits) after the competition is gone. This cannot be the case in the deregulated environment because carriers could always enter new markets at will aided by the most mobile capital investment in industry today — the modern jet aircraft.\(^{26}\)

In accepting the basic validity of Senator Percy’s analysis\(^ {27}\) that preda-

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25. First, the suggestion that all discount fares offered on multi-class flights unjustly discriminate against those who cannot meet their travel restrictions would, if accepted, define discount fares out of existence. Obviously, this result is not required by the Act. As a matter of policy, the Board looks favorably upon discount fares that are freely available to all classes of person who can meet their restrictions. These restrictions, so long as they relate to conditions of carriage or to other factors specified by Congress, render discount fare services “unlike” normal fare services and therefore raise no discrimination issues under Section 404(b) of the Act. Second, the contention that the magnitude of the discount from normal fares must be closely related to differences in cost of service was rejected outright by the Board in Phase 5 of the DPFI [Domestic Passenger Fare Investigation] and has even less validity today in light of the new statutory mandate favoring low fares. Finally, discount fares with travel restrictions and restricted introductory fares, are unlikely to attract traffic that would otherwise travel on unrestricted low-fare services, especially if the discount fares are higher priced (as they are in this case) and if their restrictions were as “artificial” and “unreasonable” as complainants contend.

CAB Order No. 79-4-57 at 2-3 (April 6, 1979) [hereinafter cited as Pan American].


27. Senator Percy’s premise has two basic defects. First, certain types of aircraft can only fly certain routes on a long-term profitable basis, e.g., wide-bodied craft are only suited to lengthy, transcontinental-type trips. For that matter, larger aircraft cannot be accommodated at some airports, such as National Airport in Washington, D.C.

More importantly, while aircraft may be physically mobile, the acquisition of terminal space at airports is frequently not obtainable on nondiscriminatory terms and has often been a subject of controversy and litigation. See, e.g., Brief of the Bureau of Consumer Protection, Southwest Airlines Automatic Market Entry Investigation, CAB Docket No. 34582 (May 17, 1979); City of Dallas v. Southwest Airlines, 371 F. Supp. 1015 (N.D. Tex. 1973), aff’d, 494 F.2d 773 (5th Cir.), cert. denied, 419 U.S. 1079 (1974) (Southwest I); Southwest Airlines v. City of Dallas, No. CA 3-3-74-
Predatory pricing is unlikely in a deregulated environment, the Board, in Air Florida II, adopted four criteria for determining whether it would initiate an investigation of predatory pricing in a given case. Those criteria are as follows:

(1) Did the competition set fares below marginal cost in any city-pair at any time?28

(2) If so, did the competition persist in losing money after the fares had been shown to be unprofitable?

(3) Could the competition reasonably have hoped to attain and maintain a position of monopoly power?

(4) Did the competition accompany its fare reductions with increased flight schedules in order to gain market share?29


28. In footnote 2 of Swift Air v. Golden Gate, 87 C.A.B. 1823, 1824 (1980) the Board provided the caveat that, where predatory intent is well-established, predation may exist even where fares are set above marginal cost. Presumably, such intent will only be well-established prior to formal investigation in situations similar to the Air Florida series of cases, where the propriety — and legality — of Eastern’s so-called “tag-end” fares, there in issue, previously had been the subject of several formal proceedings and investigations by both the Board and the Justice Department.

29. See Air Florida II, supra note 7. In sum, the Board essentially adopted the Areeda-Turner “AVC” (average variable cost) test, first articulated in Areeda-Turner, supra note 14, despite the fact that, as we have seen, the overarching 50% SIFL Rule is completely divorced from Areeda-Turner’s concept of average variable cost. The Areeda-Turner article was the first attempt to develop a per se legal standard designed to distinguish predatory conduct from competitive conduct based solely on cost-price analysis suggested by economic theory. It proposed the Average Variable Cost rule; setting price at or above a firm’s average variable cost of production is considered competitive; setting price below this point is per se illegal. But see Shimer, Predatory Pricing: The Retreat From the AVC Rule and the Search for a Practical Alternative, 22 B.C.L. REV. 467, 469 (1981). See generally Hay, The Economics of Predatory Pricing, 51 ANTITRUST L.J. 361 (1983).

The Board, however, has adopted and persistently applied the AVC test at a time when the test was coming under increasingly strong and persuasive criticism in both judicial and academic circles. See, e.g., Transamérica Computer Co. v. International Business Machines Corp., 698 F.2d 1377 (9th Cir. 1983) (prices exceeding average total cost may be predatory and so presumption of legality should be rebuttable; rejects per se test); William Inglis & Sons Baking Co. v. ITT Continental Baking Co., 668 F.2d 1014 (9th Cir. 1981) (rejecting per se rule and instead imposing burden-shifting procedure); D.E. Rogers Assocs. v. Gardner-Denver Co., 718 F.2d 1431 (6th Cir. 1983) (adopting test set forth by Ninth Circuit in William Inglis & Sons Baking Co., and permitting “the introduction of any evidence, in addition to cost price figures, to illuminate the rationale behind the
In addition, the Board will only suspend a fare challenged on the basis of predation, pending investigation, if a four-part test is met:

1. The high probability that the fares would be found unlawful after investigation;
2. The substantial likelihood that the fare is predatory so that there would be an immediate and irreparable harm to competition if it were allowed to go into effect;
3. The harm to competition would be greater than the injury to the traveling public if the proposed fare were unavailable; and
4. The suspension would be in the public interest.\textsuperscript{30}

\textsuperscript{30} Defendant’s pricing policy’’); Chillicothe Sand & Gravel Co. v. Martin Marietta Corp., 615 F.2d 427, 432 (7th Cir. 1980) (explicitly rejecting an absolute cost rule by indicating an intent to consider other factors in evaluating the establishment of a prima facie case); California Computer Prods., Inc. v. International Business Machines Corp., 613 F.2d 727, 743 (9th Cir. 1979) (expressing reluctance to apply test in all cases); Transamerica Computer Co. v. International Business Machines Corp., 481 F. Supp. 965, 995 (N.D. Cal. 1979) (explicitly rejecting test as incorrect when applied to most cases of alleged predatory pricing); O. Hommel Co. v. Ferro Corp., 472 F. Supp. 793 (W.D. Pa. 1979) (same); Clinton Frames Issues in Predatory Pricing Law, 44 ANTITRUST & TRADE REG. REP. (BNA) 1042 (1983); Baumol, Quasi-Permanence of Price Reductions: A Policy for Prevention of Predatory Pricing, 69 YALE L. J. 1 (1979); R. Bork, supra note 14; Josow-Klevorick, supra note 14; McGee, supra note 14; Scherer, supra note 14; Shimer, supra; Vawter & Zuch, A Critical Analysis of Recent Federal Appellate Decisions on Predatory Pricing, 51 ANTITRUST L.J. 401 (1983); Williamson, Predatory Pricing: A Strategic and Welfare Analysis, 87 YALE L. J. 284 (1977). Cf. Sunshine Books, Ltd. v. Temple Univ., 697 F.2d 90 (3rd Cir. 1982) (Third Circuit assumes, without deciding, that Areeda-Turner test is appropriate standard, but endorses William Inglis & Sons Baking Co. about validity of conflicting methods of accounting); MCI Telecommunications Corp. v. American Tel. & Tel., 708 F.2d 1081 (7th Cir.), cert. denied, 104 S. Ct. 234 (1983) (Seventh Circuit adopts longrun incremental cost as the appropriate standard for judging predatory pricing). But see Barry Wright Corp. v. ITT Grinnell Corp., 46 ANTITRUST & TRADE REG. REP. (BNA) 6 (Jan. 5, 1984) (First Circuit, rejecting Ninth Circuit’s rule that certain price cuts are unlawful even when resulting revenues exceed total costs, adheres to traditional test for predation).

So, for example, the Transamerica court stated:

A conclusive presumption of the legality of an unprofitable low price, merely because it is above marginal cost, a cost which is all but incapable of proof, would truly be a defendant’s paradise.” This court rejects it.

Transamerica, 481 F. Supp. at 995 (footnote omitted).

The National Comm’n for the Review of Antitrust Law and Procedures, Report to the President and the Attorney Gen. 149, 151, 166 (1979) concluded that the AVC rule was too restrictive in its exclusions of such considerations as intent and market power, and recommended amending the Sherman Act to include a standard for production that took intent and market power into account. See Shimer, supra, at 493.

The rationale behind the Commission’s position has been well articulated elsewhere:

[Areeda-Turner] rely exclusively on economic cost data to indicate the existence of predation. While objective cost data may be all that is required to solve what is strictly an economic problem, predation is not strictly an economic problem. It is a violation of the Sherman Act. Predatory pricing involves a price reduction with the aim of driving competitors out of business, so as to enjoy large profits in the long run. Proof of predatory pricing may be used to infer the specific intent required as part of an attempt to monopolize case. Thus, an examination of the intentions or reasons behind management’s decision to make the price reduction is relevant in identifying predation.

Id. at 481.

\textsuperscript{30} Reduced Fares Between New York/Newark and Los Angeles/San Francisco Proposed
It should be noted that this four-part test is the same test used to determine whether a fare should be suspended on reasonableness grounds pending investigation if the fare is otherwise within the zone of reasonableness established by section 1002 of the Act.

In light of the above, therefore, it will be difficult for any complainant to make out even a *prima facie* case of predation, sufficient to warrant fare suspension and a formal investigation by the Board. This conclusion is borne out by the fact that only once in recent years has the CAB found a situation to involve predation. That was the pre-deregulation case of *Hughes Airwest, Competitive Fares (Airwest)*. Airwest proposed to establish round-trip discount fares in the Yuma/Los Angeles and Yuma/Phoenix markets. The Yuma/Phoenix market was one of only two profitable routes in the system of Cochise Airlines, an exempt commuter carrier. The Airwest discount involved a thirty percent fare reduction to nine percent below the prevailing DPFI standard on the affected routes. On all other routes Airwest set fares at one hundred thirty percent of DPFI. In finding predation with respect to the proposed Yuma/Phoenix fare, the Board focused on the following facts: (1) Airwest had narrowly targeted its price reduction at two Cochise markets, one of which was crucial to Cochise’s survival; (2) Airwest would be subsidizing its losses on the two Yuma routes with income from its other profitable markets; and (3) if Airwest was successful in driving Cochise out of the Yuma/Phoenix market, it would have an effective monopoly therein.

From a careful reading of *Airwest* it is apparent that under the Board’s *current* policy the case most likely would be decided differently. First, the proposed Airwest price of ninety-one percent of DPFI is clearly within the “zone of reasonableness” established by section 1002(d)(4)(B) of the Act. Second, the discrimination component of *Airwest*, i.e., the charge of cross-subsidization, was firmly rejected after deregulation in *Pan American*. Third, Airwest’s flights apparently may have been operating at above marginal cost; only passengers willing to accept a three-day maximum stay restriction would have qualified for the discount. We can assume that at least a significant portion of Airwest’s passengers would have been full-fare customers. Finally, with deregulation, barriers to entry on the local Yuma/Phoenix route presumably would be quite low. In view of the philos-

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31. 74 C.A.B. 926 (1977) [hereinafter cited as *Airwest*].

32. Domestic Passenger Fare Investigation (DPFI). The DPFI standard was the pre-deregulation SIFL equivalent.

33. *See Airwest*, supra note 31; *Swift Air*., supra note 28, at 1828; *Air Florida I*, supra note 1, at 2069 n.6.

34. *See supra* text accompanying note 25.
ophy of deregulation, the CAB most likely would trust the action of competitive market forces to bring about new entrants if and when Airwest began to reap monopoly profits.

The only solace that can be reaped from Airwest is the Board's focus on the targeting of a particular competitor for below-cost pricing. The Board stated that Airwest had proposed "this particular discount in only two markets in its entire system, one of which is the backbone of Cochise's system." It is unclear whether Airwest had proposed or instituted other types of discounts elsewhere in its system, although it is implicit from the Board's statement that it had not. Exactly what the Board intended in Airwest, however, will remain uncertain; the analysis presented therein is very muddy. At best, the Airwest analysis appears most appropriate in a regulated environment.

D. PREREQUISITES TO PROVING PREDATION BEFORE THE BOARD

The leading post-deregulation decisions on predation are Swift Aire, the Air Florida cases, and the Transcontinental Low-Fare Route Proceeding cases. These decisions establish that three major problems exist in showing predation before the CAB.

First, as the Board stated in Air Florida III: "Eastern correctly points out that the test is not harm to an individual carrier but whether there is substantial likelihood of immediate and irreparable harm to competition in the marketplace." Therefore, a carrier has the burden not simply of showing that it will be injured, but rather that overall competition will be injured. This test establishes an extremely high threshold level of proof. As an example of the difference between the two analyses, consider a hypothetical major market where the second largest carrier has over forty percent of total passengers emplaned on that route. If that carrier were to withdraw from the market, overall market concentration ratios might in fact be improved, thus giving passengers greater choice and enhancing "competition."
Second, as the Board stated in *Pan American*:

Both the Board and Congress, however, have recognized and accepted the validity of marginal cost pricing, *i.e.*, setting fares, in appropriate circumstances, without regard to assigning fixed per-passenger costs. Marginal cost pricing is especially useful in evaluating the cost of airline services in competitive operations. In this instance, Pan Am’s introductory and discount fares appear in line with short-run marginal costs and are otherwise consistent with a marginal cost pricing strategy. Moreover, there is no outward evidence that the $99 introductory fare is designed to drive competitors from the market, because it is very restricted and carries an expiration date that virtually precludes the opportunity to inflict any significant competitive damage on other carriers.\(^{42}\)

As long as it is clear that the flight in question would be flown anyway and that the discount fares are only being utilized to increase load factors and fill up otherwise empty seats, marginal cost pricing will be applied. Theoretically, marginal cost pricing equates the value of the resources used to produce the good (in this case, air transport) with the utility of the good produced to the consumer. Marginal costs for airlines will always be very low,\(^{43}\) consisting of such items as additional food, beverages, baggage handling, ticketing, reservations and the fuel needed to move the bodyweight of the extra discount passengers.\(^{44}\) In the *Transcontinental* cases, the routes would have been flown anyway, with normal coach and first class fares, as part of an overall national route system;\(^{45}\) the discount fares were capacity limited and intended only to fill up otherwise empty

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\(^{42}\) *Pan American*, supra note 25, at 3 n.8.

\(^{43}\) The use of a marginal cost standard will be highly misleading over time:

Areada and Turner incorrectly viewed short-run costs as the sole indicator of efficiency. \(\ldots\) The Areada-Turner approach allows firms to price at AVC, but since AVC is below ATC \([\text{Average Total Cost}]\) this implies that a firm pricing at the legal minimum will not cover fixed costs with the revenue generated by sales of this product.

\(^{44}\) See *Air Florida I*, supra note 1, at 2066. *But see Swift Aire*, supra note 28, at 1827 n.21.

\(^{45}\) Of course, this argument ignored the fact that the market service, defined by the city-pair or transcontinental routing involved, was only viable due to the fact that the difference between marginal costs and average total costs was being made up by cross-subsidization from other, less competitive routes. This is merely the same problem of cross-subsidization faced when analyzing
spaces. In the *Air Florida* cases, Eastern would have been flying its "tag-end" segments anyway, both to provide service equivalent to that of its other long-haul competitors, and to re-position its "aircraft and personnel for purposes of maintenance and system-wide scheduling." Therefore, unless the airline is charging only a single, low discount fare for a route which is itself not merely the "short segment[s] at the end or beginning of a longer-haul flight," (the definition of "tag-end" segments), marginal costs, and not fully allocated costs, will be utilized for assessing charges of predation.

Third, the Board defined predation as occurring "when a firm charges a price for a product that is below cost, with the expectation that by doing so it can drive its rivals out of the marketplace and subsequently raise its price to a monopoly level, recouping its previous losses and earning additional monopoly profits." The Board went on to state that, though predation was possible, sustaining any level of monopoly profits was unlikely due to the increased costs of the additional market share.

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46. *Air Florida I*, supra note 1, at 2064; see also *Air Florida II*, supra note 7, at 5.
47. *Air Florida I*, supra note 1, at 2064.
48. It should be noted that the Board alternately uses the phrases "out-of-pocket," "cash," and "variable" costs to denominate the concept of "marginal" costs.
49. *Air Florida I*, supra note 1, at 2064.
50. Although there is disagreement among the courts and legal and economic scholars concerning the precise standard to be employed, most today recognize that predation is an irrational — and therefore unlikely — strategy in situations where the predator cannot reasonably expect to reap monopoly profits for a sustained period after driving the target company from the market, because of the high cost of predation. The predatory firm not only incurs losses along with its rivals, but, as its market share increases, its proportion of total industry losses tends to increase accordingly.

Consequently, the barriers to entry and exit in a market must be significant in order for predation to be a rational strategy. A firm that monopolizes a market in which entry barriers are low will be constrained from charging monopoly prices by the threat of entry. If exit is also easy, in the sense that a firm with an investment in a particular market can move its capital investment into other markets without substantial costs arising from such a redeployment, a firm will not be deterred from entering the market by the mere threat of predation. It loses nothing if the threat is carried out, and it can always re-enter once the threat is past.

Id. at 2065. The Board's emphasis on the comparative magnitude of losses between predator and victim adopts the same avoidance of both the question of comparative "staying power" by reason of differing financial resources and capital reserves, and the question of actual real-world re-entry and restart-up problems faced by potential successor firms, reflected in Areada-Turner, supra note 14, at 698, 704, 709 and in McGee, supra note 14, at 296-97. Areada-Turner, in fact, seem strongly skewed to favor the continued dominance of larger firms with such "staying power." See Shimer, supra note 29, at 480, 485; cf. Joskow-Kleovorick, supra note 14, at 227-31.

McGee implicitly assumes that the victim has both the capital and foresight to "stick it out," i.e., is not in an already (or initially) weakened—although still competitive—position. To use one
In any major market, it is unlikely that even a strong competitor could ever hope to achieve a monopoly position. Under deregulation, even if such a position was temporarily achieved, re-entry would presumably be so attractive to new competitors as to foreclose the possibility of intermediate or long-term monopoly pricing.

Since deregulation, no complainant has been able to overcome the three hurdles enumerated above. In the *Swift Aire* case, Swift alleged that its competitor, Golden Gate Airlines, had been offering below-cost fares for unreasonably long periods of time in an effort to drive Swift out of the San Francisco/Bakersfield and Los Angeles/Bakersfield markets. The Board estimated Golden Gate’s marginal costs by taking the sum of its operating and direct maintenance expenses. The Board found no predation in light of the following facts. First, in the two pertinent markets, both airlines had willingly engaged in “a fierce competition struggle;” such competition was necessary not just in relation to the other but also to attract travelers who were currently using alternate modes of surface transportation. Second, Bakersfield’s air transport services were currently under-utilized. Third, barriers to entry were and would remain low even though Golden Gate was in fact operating at below marginal costs. Finally, the Board also emphasized that Golden Gate was suffering system-wide losses and apparently had not targeted a particular market for below-cost, cross-subsidized pricing.

In the *Air Florida* cases, the Board rejected Air Florida’s complaint against Eastern on four grounds. First, Eastern’s fares, in the short-haul Florida markets there in question were above marginal cost. Second, Eastern could not have hoped to earn monopoly profits on any of the tag-end routes. Eastern and Air Florida were the lone competitors on only two of the five routes in question, and a *de minimus* number of flights and passengers were involved. Third, Eastern had increased its flight offerings in only one of the five affected markets. Finally, entry barriers to all markets involved were quite low.

The *Transcontinental* cases involved the complaint of World Airways and several other parties that the “‘supersaver’” fares approved by the Board in the New York-Newark/Los Angeles-San Francisco market for five major trunk carriers were predatory. The Board found that the major trunk carriers would not be operating below marginal costs, nor could any one of the major carriers hope to achieve a monopoly position, even if the

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of the “nature” allegories Professor McGee seems so fond of, it should be noted that birds of prey are apt to go after smaller, weakened opponents, not the most vigorous ones, not leaving time for the injured to heal and regain competitive vigor.


52. United, American, TWA, Pan American, and National. The “‘supersaver’” fares competed directly with World’s standard low fare.
complainant, World Airways, was eliminated as a competitor.\textsuperscript{53} Furthermore, at least in the \textit{Pan American} case, the discount fare being offered was very restricted and carried an expiration date.\textsuperscript{54}

In summary, then, it would be extremely difficult, if not impossible, to establish a prima facie case of predation under the Board’s criteria. If a complainant should wish to pursue this line of inquiry, however, certain factors and theories should be considered.

IV. Possible Successful Theories of Predation

There are at least two theories on which a complainant carrier might successfully bring a predation claim before the CAB. First, if the complainant could show that the competing carrier was specifically targeting the complainant’s most lucrative markets for low-cost pricing in the hope of driving the complainant completely from the marketplace, a predatory pricing claim might be viable. The complainant would have to establish a pattern of assaults on its most lucrative domestic markets in the form of low-price discounts that both significantly undercut its own prices and are near or below the competitor’s own marginal costs. Predatory intent arguably would be implicit in such a pattern and, therefore, the complainant might avoid having to show that each of the competitor’s discounted fares was actually below marginal cost.\textsuperscript{55} The complainant would also have to show that the competitor was not offering similar discounts on a significant number of its other routes where it was not head-to-head with the complainant. Furthermore, the complainant would have to establish that the loss of the complainant as a competitor would have significant negative effects on competition in one or more discrete markets.

The second possible theory of action arises in the case where the competitor’s actions in one or several discrete markets could drive the complainant completely out of all markets.\textsuperscript{56} In that case, the competitor might

\textsuperscript{53} The Board here, as in the \textit{Air Florida} cases, ignored the major problems inherent in the AVC test:

While the Sherman Act places primary emphasis on competition, the AVC rule only emphasizes economic efficiency. . . . Federal antitrust policies place great emphasis on competition from as many sources as possible, including new entrants and smaller rivals. New entrants and small producers, however, face higher costs than large or established firms. The AVC rule allows the large or established firms to price below their breakeven point, ATC [Average Total Cost], and well below the corresponding breakeven point for the small or new firms. Thus, the AVC rule seriously threatens the ability of the new or smaller producer to survive.

Shimer, \textit{supra} note 29, at 480 (footnote omitted).

\textsuperscript{54} \textit{Pan American}, \textit{supra} note 25, at 3 n.8

\textsuperscript{55} Of course, to the extent that the competitor offered only a single, below-cost discount fare on a given, established route, fully allocated costs would be the applicable measure and a discrete instance of predation might be demonstrable.

\textsuperscript{56} This is highly possible given the current extremely troubled financial posture of a number
not have to achieve a monopoly position in any given market in order to more than offset its short or intermediate term losses. If the competitor should cause the complainant sufficient injury in its most lucrative markets by means of below-cost pricing, the complainant, in its current precarious financial state, might be forced into bankruptcy and to discontinue flight operations. For example, in the major hypothetical market previously referred to in which the complainant is the number two carrier in terms of passenger load, the complainant’s withdrawal would leave forty percent of the existing passenger traffic in need of alternate air transportation. If the competitor positioned itself for such an eventuality, it might conceivably grow from an initial toehold position vis-a-vis the total passenger enplanements to a significant percentage of the traffic.\footnote{57} While perhaps the competitor could never hope to achieve monopoly power in such a significant market,\footnote{58} the mere fact that it might be able to greatly expand its portion of a highly lucrative market, from perhaps three or four percent of enplanements to ten-fifteen percent, arguably would make such behavior, with its short or intermediate term losses, worthwhile.\footnote{59} Furthermore, to the extent of major national and regional airlines. It is understood, of course, that a complainant or successor might be able to continue to offer competitive air transportation services while in bankruptcy. Cf. Areeda-Turner, supra note 14, at 698: “Although a predator may drive competitors into bankruptcy, their durable assets may remain in the market in the hands of others.”

57. The Board test for predation goes even further than Areeda-Turner and seems to assume that there only can be predation if the predator had hope of attaining and maintaining a position of monopoly power. Areeda-Turner, by studiously avoiding directly linking their test to the attainment of monopoly power, seem to implicitly recognize that predation can be a rational strategy in a market and industry where only something less than monopoly market power is achievable:

\[P\]redatory pricing would make little economic sense to a potential predator unless he had . . . a very substantial prospect that the losses he incurs in the predatory campaign will be exceeded by the profits to be earned after his rivals have been destroyed.\footnote{id.}

58. Not only would the predator stand to pick up load but if, as in Transcontinental and \textit{Pan American}, the competitor being targeted and driven from the market was a leading price-cutter, all remaining competitors, including the predator, could also raise their prices. So, for example, soon after Laker Airlines left the transatlantic market, all competitors’ transatlantic fares were raised substantially. See the rather prophetic discussion of the Laker situation and the argument for a rule requiring the quasi-permanence of price reductions in \textit{Baumol}, supra note 29. Also, concerning the ongoing course of Laker’s private antitrust suit alleging a “classic antitrust conspiracy” involving McDonnell Douglas, \textit{Pan American}, Trans World Airlines, British Airways, British Caledonian Airways, Swissair, Lufthansa, Sabena, and KLM, to drive Laker from the marketplace, and U.S. Justice Department probe of related alleged antitrust violations, see \textit{Averbach, Airlines Admit Attempt to Stop Laker Creditors}, Wash. Post, July 19, 1983, at D7, col. 5; UK-U.S. Governments Hold New Talks on Laker Dispute, \textit{44 Antitrust & Trade Reg. Rep. (BNA) 1056} (May 26, 1983); \textit{Laker Antitrust Suit Against Carriers Will Be Tried in U.S. Court, 44 Antitrust & Trade Reg. Rep. (BNA) 982} (May 12, 1983); \textit{Keeping Up: British Forum Rejected}, Legal Times, May 9, 1983, at 8, col. 2; and \textit{Antitrust Case Spawns a War Between U.S.-British Courts}, Nat’l L.J., Mar. 21, 1983, at 10, col. 3.

59. Joscow-Klevorick would never admit the possibility of a predatory pricing threat in such a situation despite the fact that, by virtue of their own emphasis on an industry-by-industry examination, it becomes clear that the present state of the airline industry may provide a fertile ground for
that the complainant completely stopped all air transport services, the competitor might be able to make similar gains in numerous markets in which both the complainant and the competitor previously had been competitors, thereby more than offsetting its earlier losses in several strategically targeted markets. 60 Of course, the preceding analysis suffers from one serious weakness. That is, in some cases such a scenario may only be possible as a result of unfortunate investment, or internal management decisions, traceable exclusively to the complainant itself. 61

60. As Joscow-Klevorick recognize, different structural considerations will affect the efficiency of any single predatory pricing model when applied to a given industry:

If all markets were identical in their structural and behavioral aspects, then having found the optimal predatory pricing rule for one market, we could apply it with confidence to all others. But, as one might expect, different markets are not identical with respect to the features that determine the sum of the expected error costs and the costs of implementation for alternative rules. Hence, our decision-theoretic evaluative mechanism reveals that no single rule will be best for all market situations; if a predatory pricing rule is formulated with one particular market in mind we cannot be sure that it should be applied to other market situations.

What is needed is an approach that can accommodate important market differences: the characteristics of firms and markets that affect the probabilities of error, the error costs, and the implementation costs of alternative policy approaches.

Joscow-Klevorick, supra note 14, at 218. In our critique of the CAB’s policies above with respect to the airline industry, the danger of applying a single relatively inflexible, mechanical “per se” rule, such as Areeda-Turner’s, is revealed. In essence, the structure of the airline industry as it exists today is far different from the single “dominant” or “monopoly” firm markets suggested or addressed by most commentators. Yet in this industry, perhaps the dominant transportation industry in the nation today, the potential for very real — and serious — predatory pricing practices exists as we have demonstrated.

At the same time, there is a serious increase of price-fixing and attempted monopolization in the industry under deregulation. See, e.g., United States v. American Airlines, 4 Trade Reg. Rep. (CCH) ¶ 45,083 (Case 3044) (Jan. 9, 1984). 61. Furthermore, it should be noted that in Transamerica Computer Co. v. International Business Machines Corp., 481 F. Supp. 965 (N.D. Cal. 1979), the court listed several situations where prices below average total cost might not be predatory, including (1) excess capacity in the industry, and (2) decreasing demand. Id. at 996. Both caveats arguably are currently applicable to the airline industry. In judging any predatory pricing complaint, therefore, the Board should keep in mind that:

Severe excess capacity, in the price-cutting firm due to declining demand or over-expansion of the industry . . . is another legitimate, non-predatory reason for lowering price below ATC. A firm in a declining industry may incur excess capacity because of a decrease in demand for the product. This lowered demand can be satisfied by much less industry capacity, thereby forcing many existing firms out of the industry. Managerial practices indicating a desire to remain a producer in a declining industry is [sic] a legitimate reason for the pricing conduct. Where it is inevitable that some firms will be forced out of the industry, the conduct of cutting prices may be the only alternative open to a firm desiring to remain. Although competitors will be ruined, the motivation behind the conduct is self-preservation, not predation.

Shimer, supra note 29, at 504 (footnote omitted). Accordingly, in the airline industry, suffering from both excess capacity and decreased demand, the Board must decide whether the target’s
V. CONCLUSION

Any complaint charging predation, discrimination, or unreasonable-ness, before the CAB either directly or as the result of removal from district court pursuant to a motion for primary jurisdiction, would have only a small chance of success. In order to have even that small chance, such a complaint should be based on the theories outlined in Section III. Following the filing of a formal complaint, the charged competitor would be allowed to file an answer, and then the complainant would have the opportunity to file a reply.\textsuperscript{62} The Board would then issue an order either granting a formal investigation and possibly suspending the challenged fare, or would deny such an investigation and dismiss the complaint. Given the result reached in the \textit{Swift Aire}, \textit{Air Florida} and \textit{Transcontinental} cases, and for the reasons set forth, the likely result of any foreseeable complaint would be dismissal by the Board. This abdication of regulatory responsibility has resulted from a combination of unclear past Board practice and deregulatory legislation. The reversal of such a trend can probably only be accomplished by forceful corrective legislation.

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The Western Coal Traffic League Case: Condoning ICC Eschewal of Rail Monopoly Ratemaking

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I.  INTRODUCTION

In Western Coal Traffic League v. United States,\(^1\) decided on November 14, 1983, the Court of Appeals for the Fifth Circuit squarely addresses the question of ICC control over railroad rates charged to shippers by a railroad which is the sole connecting link between the origin of shipment and the point to which a shipper must transport his goods. It is appropriate to start with a brief chronology of legislative and administrative events:

1. In 1976, Congress enacted the Railroad Revitalization and Regulatory Reform Act (4R Act),\(^2\) deregulating railroad rates except where there exists market dominance. The ICC was directed to develop standards and procedures for determining whether and when a railroad possesses market dominance.

2. Soon afterward, the ICC in Ex Parte No. 320,\(^3\) pursuant to Congressional directive, established procedures interpreting market dominance as being the lack of effective competition for the specific traffic and movement (from one point to another) to which the rate applied.

3. In 1978, Congress recodified the Interstate Commerce Act.\(^4\) Since the initial task of formulating and commencing the new program under the 4R Act had been accomplished,\(^5\) the authorization to develop such standards and procedures was not included.

4. In 1980, Congress enacted the Staggers Rail Act of 1980,\(^6\) which retained the market dominance concept of the 4R Act but created a series of rising threshold rate levels below which lack of market dominance would be conclusively presumed.

5. In 1981, the ICC in Ex Parte No. 320 (Sub-No. 2)\(^7\) made rules

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\(^1\) 719 F.2d 772 (5th Cir. 1983) (en banc).
\(^3\) Special Procedures for Making Findings of Market Dominance as Required by the Railroad Revitalization and Regulatory Reform Act Report, 353 I.C.C. 874 (1976) [hereinafter cited as Ex Parte No. 320].
\(^5\) See Western, 719 F.2d at 776 n.7. Though the repeal of the language in 1978 is thus recognized by the court, it appears to rely on it as the congressional "mandate" to the ICC in 1981, when it changed its view of geographic and product competition.
\(^7\) Market Dominance Determinations and Consideration of Product Competition, 365 I.C.C. 118 (1981) [hereinafter cited as Ex Parte No. 320 (Sub-No. 2)].
altering its original definition of "market dominance" so as to include consideration of geographic and product competition.

II. THE ISSUE

First, consideration must be given to the manner in which the issue arises. A coal mine in the Powder River Basin must transport coal from its mine in Gillette, Wyoming to Cheyenne to reach various railroads connecting with its potential markets. The Burlington Northern Railroad owns and operates the only rail line between Gillette and Cheyenne. The coal, by the most direct route, might travel over Burlington Northern’s lines to Fort Worth, or over the Santa Fe lines in a somewhat less direct route to Fort Worth. From Fort Worth on to San Antonio or Houston it might proceed over the lines of any one of several different railroads.

Assume that the shipper is a utility in Houston. Burlington Northern charges a rate which the utility considers excessive, and the utility files a complaint with the ICC, asking it to establish a "just and reasonable" rate. The premise on which the shipper bases its complaint is that Burlington Northern exercises market dominance over the transportation involved. The 4R Act of 1976, as amended by the Staggers Act of 1980, provides that where the rate is above a certain threshold figure and the railroad exercises market dominance, the ICC shall determine a rate which is just and reasonable.

The question raised in such a case is whether the Burlington Northern exercises market dominance in setting the rate. If so, the shipper is entitled to have the ICC review the rate and require that the railroad apply a just and reasonable one. If the railroad is not in a position of market dominance, it may set whatever rate it chooses and the ICC may not intervene.

An equitable resolution of the market dominance issue has troubled the ICC, the courts and Congress for at least a decade. Its resolution will have wide ramifications respecting the distribution and choice of the energy resources within the United States and will have pervasive impact on the nation’s transportation policy. Ultimately, it may vitally affect the growth or retardation of industrial development throughout the country. Though the decision in Western meets the issue squarely, it does not deal with it in the historical depth and conceptual breadth that the matter deserves. Indeed, in the narrow ambit within which the majority of the court confines themselves, they are precluded from dealing with the issue comprehensively.

The central issues are: What is "market dominance" and what is that "effective competition" which eliminates it? "Market dominance" was defined in the 4R Act of 1976, as "an absence of effective competition from other carriers or modes of transportation for the traffic or movement to
which a rate applies.’’8 This language remained intact9 after passage of
the amendments contained in the Staggers Act. The dispute between
the majority of the court10 and Judges Rubin and Reavley, who dissented, cen-
tered on the meaning of ‘‘market dominance.’’ The latter two judges, who
comprised the majority of the three judge panel which first heard the
case,11 contended that in order for there to be effective competition, there
must be competition for the movement of essentially the same commodity
from the general vicinity in which the transportation commences to the des-
tination. The majority, on the other hand, held that the ICC may find ‘‘ef-
effective competition’’ from others ‘‘for the traffic or movement to which a rate
applies’’ if there is geographic or product competition. Hence, there is no
market dominance, and the Commission must decline jurisdiction.

The difference in positions may best be shown by exemplar: To use
the hypothetical posed by Judge Brown in the panel decision, if the route in
question is transportation of coal from the Powder River Basin in Wyoming
to Chicago, and the coal purchaser could employ another avenue of traffic
or movement from southern Illinois for the same kind of coal, that could
constitute ‘‘effective competition from other carriers or modes of transpor-
tation for the traffic or movement to which a rate applies.’’12

The dissenting judges take the position that this does not constitute
competition for that traffic or movement to which the rate applies, noting
that the language of the statute does not embrace the concept of general
market competition, but rather competition for the particular haulage. Thus,
in the instant example, they argue that for there to be that ‘‘effective com-
petition’’ which deprives the ICC of jurisdiction, there must be some other
carrier to compete in transporting coal from the Powder River Basin area to
the Chicago area.

The difference between the two interpretations has vast practical impli-
cations. To accept the court’s interpretation is to open up a wide area of
competition. The shipper would have to anticipate all such possibilities in
order to be prepared to negate them and to show that the carrier had mar-
ket dominance and is subject to ICC jurisdiction for the particular transpor-
tation involved. However, under the dissent’s interpretation, the shipper
need only show, for example, that Burlington Northern stands at the turn-
stile, controlling the movement of coal out of the Powder River Basin. Its
burden of proving ICC jurisdiction to consider the reasonableness of the

10. Clark, C.J.; Brown, Politz, Tate, Johnson, Williams, Jolly and Higginbotham, J.J.; Gee,
Randall and Garwood, J.J., recused themselves.
11. Western Coal Traffic League v. United States, 694 F.2d 378 (5th Cir. 1982).
12. Id. at 398.
rate is then clearly identified and the issue is narrowed to tangible and limited factors which can be meaningfully considered.

III. ICC'S FLUCTUATING INTERPRETATIONS

The ICC emphasized these points in its original interpretation of the 4R Act in Ex Parte No. 320:

After assessing the statutory language and considering the need for quickly identifying whether effective competition is present, we have concluded that the appropriate market is the market for transportation services which directly compete with the service outlined in the tariff under consideration. Limiting consideration to direct carrier competition is consistent with the express language of the legislative definition, and is essential to making practical determinations for a short time period.¹³

The Commission rested its decision on an interpretation of the language of section 202 of the 4R Act. Even at that time contentions like those contained in Judge Brown's panel dissent (later adopted in principle by the court) were made by the railroads. However, the Commission rejected such arguments, holding that consideration of geographic and product competition in determining whether or not effective competition existed was not in accordance with the language, "'traffic or movement to which the rate applies.'" The Commission said:

The contention of some of the parties that use of the word "'traffic'" in conjunction with the word "'movement'" requires consideration of a broad range of movements of various commodities moving from various sources to various destinations must be rejected. The 4R Act speaks of "'the traffic or movement to which the rate applies.'" When used in this context in the transportation industry, the word "'movement'" refers to transportation from a single origin point to a single destination point, while the word "'traffic'" commonly denotes transportation services from a named set of points to another point or set of points; from specific origin points or areas to rate groups or blanket areas; or between stated mileage [on particular commodities] in a given territory.¹⁴

From this language it is apparent that the Commission was not merely choosing to accept jurisdiction within a range of permissive authority in which it could eschew jurisdiction. It was accepting the proposition that within the constraints of the language of the statute, it could not eschew jurisdiction on the basis of the existence of geographic or product competition.

Five years later, the Commission in Ex Parte No. 320 (Sub-No. 2)¹⁵ concluded that its reading was unnecessarily restrictive in focusing only on direct carrier competition and ignoring the indirect competitive impact of geographic or product competition. Therefore, it established that there

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¹³. Ex Parte No. 320, supra note 3, at 904.
¹⁴. Id. at 904-05.
¹⁵. Supra note 7.
were four major forms of competition affecting rail transportation: (1) competition by railroad with railroads; (2) competition with railroads by other forms of transportation; (3) geographic competition; and (4) product competition.\textsuperscript{16} If there is competition in any of these respects, the Commission concluded, there is not that market dominance which is the threshold requirement for ICC review of the rate involved. The Commission did not make a reasoned decision on this issue until after the passage of the Staggers Act, and it based its authority in large measure on a comment concerning the ICC's flexibility in appraising effective competition contained in the Conference Committee Report on the Staggers Act.\textsuperscript{17} The Fifth Circuit in \textit{Western} also relies heavily on that language.\textsuperscript{18}

In considering the following hypothetical situation it is easy to see how the ICC holding would apply. A Texas utility can get coal from Wyoming by the Burlington Northern, which controls 100\% of the coal traffic from that state. It can also get coal from Montana by another railroad via another route. Under a cost-based rate determination, the rate offered by Burlington Northern to deliver Wyoming coal would be at 170\% of variable cost. If coal were supplied from Montana, the cost would be much higher because of the greater distance. This rate, if applied to the Wyoming-Texas haul, would be 212\% of variable cost. Burlington Northern is offering to haul the coal from Wyoming to Texas at 212\% of variable cost, saying that such rate is affected by the competition of Montana coal. It therefore contends that there is effective competition which precludes ICC jurisdiction.

The Texas utility contends that a rate of 170\% of variable cost is as much as should be reasonably levied, arguing that it should not be required to pay a rate at 212\% of variable cost which can only be exacted because Burlington Northern has a complete monopoly out of the area where the coal originates. The ICC denies the utility's complaint, asserting that the Montana coal competition is effective to keep the rate no higher than 212\% of variable cost.

\section{IV. The Court's Interpretation}

Though the case stated above is hypothetical, the majority of the three judge panel in the initial determination of this case rejected such a contention:

\textbf{Competition for a movement of coal by rail from coal deposited in Wyoming to a utility company in Texas, for example, is created only if some other carrier is willing to move that product from the same origin to the same destination.}\textsuperscript{19}

\textsuperscript{16} \textit{id.} at 131.
\textsuperscript{17} See \textit{infra} text accompanying notes 25-35.
\textsuperscript{18} See \textit{infra} text accompanying notes 27-31.
\textsuperscript{19} \textit{Western}, 694 F.2d at 390.
The court reversed the panel and supported the theory of the ICC in Ex Parte 320 (Sub-No. 2), with Judges Rubin and Reavley dissenting.

All judges, however, agreed that the language of the 4R Act governs the question of market dominance and that the Staggers Act did not change this governing language. Yet Judge Brown, in his dissent on the panel, had implied that the Staggers Act left the matter of reexamining geographic and product competition to the Commission. He treated the Conference Committee Report as reinstating the 4R Act’s initial delegation of authority to develop standards and procedures relating to the term “market dominance.”

This concept is carried on in the opinion of the court pursuant to the court’s consideration en banc, although the concept is never clearly articulated in Judge Johnson’s opinion. He refers to the authority to develop standards and procedures as if it rests on the actual language of the 4R Act that was deleted.

Judge Johnson, writing for the majority of the court sitting en banc, recognized that “Congress . . . did not alter the market dominance statute enacted in the 4-R Act” but concluded that the ICC’s statutory mandate is broad enough to permit it to use geographic or product competition as that “effective competition” which precludes market dominance and ICC regulation. Moreover, he broadly interpreted that statutory authority to render the fact that “the members of this Court might have construed the statute differently inconsequential.”

He based his decision in part on the Conference Committee Report on the Staggers Act, noting that:

[T]he Staggers Act reflects a reinforced congressional intent to allow the ICC to continue to promulgate standards and procedures for making the market dominance determination. The Conference Commission [sic] Report specifically stated that Congress’ action was “not intended in any way to restrict the ability of the Commission to apply this concept, both in its regulations and individual cases.” . . .

This is particularly significant, since Congress was aware of the ICC’s stated intent to consider product and geographic competition when the Staggers Act was debated.

The citation of the Report is correct if it means that Congress’ action in passing the Staggers Act was “not intended in any way to restrict the ability of the Commission to apply” the concept of market dominance as defined in the 4R Act. However, the analysis reaches too far when it considers this language as permitting the Commission to apply the concept of effective

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20. Western, 694 F.2d at 397.
21. Western, 719 F.2d at 777.
22. Id. See also infra text accompanying notes 49-63.
23. It should be noted that neither the Report nor anything related to the text or the history of the Staggers Act purported to reinstate the provisions of the 4R Act (§ 202(b)) referring to “standards and procedures.” (Footnote added).
24. Western, 719 F.2d at 779-80 (citations omitted).
competition in a way not restricted to such competition for the traffic or movement involved.

The court’s latter interpretation confuses the Commission’s authority to establish standards and procedures which carry out the mandate of the 4R Act with the Commission’s authority to establish its own mandate under the guise of rule-making. The Commission cannot make a rule contrary to its legislative mandate on grounds that this is the best way to meet “the practical realities of day-to-day regulation.” The purport of Judge Johnson’s reasoning is that it not only can do so, but that it has statutory authority to establish the standards and procedures for the “construction of its statutory authority” under section 202(b) of the 4R Act, which authority had been repealed at the time Ex Parte No. 320 (Sub-No. 2) was adopted.

V. The Conference Committee Report

The importance of the language in the Conference Committee Report is greatly over-emphasized. The only reason for discussing it at length here is to show that it cannot be considered an express delegation by Congress of authority which would place this case under the rule in Batterton v. Francis,26 which holds that a court has no congressional authority to disturb agency action taken pursuant to express delegation.

By its very nature, Report language cannot be taken as express delegation of authority by Congress. It is the work of staffers, not house members. It is necessary to give attention to the Report beyond what is merited only because it is the basis of the ICC’s decision in Ex Parte No. 320 (Sub-No. 2) and is relied upon so heavily by the court in justifying the Commission’s broadened view of that competition which negates market dominance.27

A. The Report’s Language Interpreted

The most significant language in the Report is in its first sentences: “The definition of market dominance under existing law has not been altered by the substitute, and it is not intended that there be any change in the meaning of the term ....”28 The explanation might well have stopped there because any further reference to “effective competition” must be considered as restricted under the 4R Act to competition for the

27. Thus, the interpretation in Judge Johnson’s opinion is one in the third degree: It is an interpretation of the Conference Report’s interpretation of the Staggers Act’s interpretation of the 4R Act. Judge Rubin’s opinion simply interprets the 4R Act.
28. HOUSE REPORT, supra note 25, at 4120.
traffic or movement involved. The sentence upon which Judge Brown heavily relied reads:

In maintaining the term market dominance, in addition to statutory changes designed to provide more rate freedom to rail carriers, the Conferees intend that whenever there is effective competition . . . , such competition should continue to function as the regulator of the rate rather than the Commission. 29

Judge Brown reads this section as if the term "effective competition" could be disjointed from the restricting terms of the 4R Act which follow—as if it were competition of any nature so long as it affects the rate. But this interpretation ignores the sentence in the Report that disavows any change in the meaning of the term.

Judge Johnson rests his view that the Staggers Act reflects a reinforced congressional intent to allow the ICC to continue to promulgate standards and procedures for making the market dominance determinations on the succeeding sentence in the Report:

Maintenance of the "market dominance" standard is not intended in any way to restrict the ability of the Commission to apply this concept, both in its regulations and individual cases. 30

But what is this "concept"? It is the concept of effective competition as used and restricted in the 4R Act. It is not a concept of roving authority granted to the Commission to expand the term to include any competition by traffic or movement, or any product obtained from another place. 31

Most importantly, since the language is clearly subject to this interpretation it cannot be taken to be an express authority granted to the Commission to define its own scope of authority under the Interstate Commerce Act.

That the conferees intended "that whenever there is effective competition, such competition should continue to function as the regulator of the rate rather than the Commission" is not in dispute by any party, but it does not answer the question: What is effective competition? The answer to that question must be found in the 4R Act itself. As all agree, "it is not intended

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29. Id., quoted in Western, 694 F.2d at 398 (Brown, J., dissenting) (emphasis added).
31. One difficulty with permitting product competition to be used to oust ICC jurisdiction is that, though that competition may give an option to the purchaser of coal, it does not make the railroad any less dominant over the supplier of coal.

Suppose one of a dozen coal mines is a captive shipper to Burlington Northern Railroad respecting its shipment of coal out of the Powder River Basin to Houston. But suppose the utility in Houston that has contracted for the coal could use foreign oil, and the rail rate demanded is raised to what the market will bear up to a relatively high price for foreign oil at the Port of Houston.

The Burlington Northern may not have a monopoly as supplier of fuel to the Houston utility, but it is in a monopoly position as hauler of coal from the mine. The cost to the utility is the sum of the fuel cost plus the transportation cost, and the railroad's monopoly position will permit it to take the lion's share of the total price of the product at the point of delivery. The railroad can bid down the fuel cost because there are eleven more mines competing to sell their product, but there is only one railroad to move it out of the Basin.
that there be any change of the meaning of [market dominance]" as used in that Act. Therefore, there is not only no intent in the Staggers Act to "restrict the ability of the Commission to apply this concept" but no intent to enlarge it.

Judge Johnson attempts to enlarge it by construing the language beyond its stated meaning, as reflecting some reinforced intent of Congress to expand ICC authority beyond the plain language of the 4R Act. There was, however, never such an intent.

B. Weight and Credibility to be Attributed to Report Language

A conference report should be treated by a court as a useful summary of the bill as it has come out of conference. Unlike the colloquy on the floor and the treatment of amendments offered there and in committee, it is not the direct expression of members, countered and disputed in open debate. It is the impression of staffers as to what has occurred in conference and an attempt by them to cull from this action the intent of the conferees. It cannot be taken as an expression by members of the conference of their intent, because it is usually hurriedly written and seldom perused by a conferee (other than possibly the House and Senate chairmen) before it is printed and circulated on the floor. The conference report involved here is typical, except that it was prepared under greater than ordinary pressure and under conditions of greater than ordinary secrecy.32

Of course, conference reports can be useful charts and records of the interplay of ideas which emerge in the conference discussion of issues. Their usefulness in this respect is proportionate to the time spent in conference and the depth of those discussions. In this case, there were no such discussions with a quorum of members assembled.

The conference on the Staggers Act was called on September 4, 1980. It lasted for exactly nineteen minutes. Senators Cannon and Packwood and six of the House conferees were present. Without discussion with the House conferees, Mr. Florio, Chairman for the House conferees, announced that they had reached an agreement and that the staff would prepare a draft of it. Senator Cannon confirmed the Senate’s agreement, with the reservation that members would have the opportunity to review the final bill and the report before these were filed.

The final language of the legislation and report did not exist at that time. It was prepared in the four days between the meeting and the time the report was presented on the floor. The only draft that was available later that day was an instrument containing many variations from the lan-

32. Members of the Conference Committee were not even permitted to know the number of the room the compilers of the Report were working in.
VI. LEGISLATIVE HISTORY OF THE STAGGERS ACT

It would not seem necessary, given the clear mandate of the 4R Act—that the ICC shall exercise its jurisdiction if there is no effective competition for the movement involved—to explore the legislative history of the Staggers Act. The ICC has so heavily leaned on a scintilla of evidence from this history, (i.e., the Conference Report language), and the court, also relying

33. The author was one of the House conferees on the Conference Committee and can personally attest to the fact that the conference was concluded while he and most of the House conferees were necessarily away from the conference during and immediately after a vote on the House floor. There also was no instrument purporting to be the language of the agreement available to conferees until after adjournment of the conference.


35. The report which was printed and made available to the members at the time they approved the report (which, in accurate form had been printed in the Congressional Record and was on the speakers desk) materially misstated the content of the governing document. The official report on the Speaker’s desk and printed in the record read: “The Conferees do not intend that the Commission alter the jurisdictional threshold by reducing or increasing the items which will be considered as part of variable cost.” The italicized phrase was erroneously omitted from the print circulated as House Report No. 1430.

The altered language carries the implication that the Commission may make the jurisdictional threshold more restrictive by increasing the items considered but not less so by reducing them. The official report makes it clear that the Commission may neither reduce nor increase the items which will be considered part of variable cost.

It should be noted that the language of the official report on this point is balanced and consonant with the changes made in floor amendments, which tended to restrict the Commission’s scope for curtailing its own jurisdiction. To change it in the manner of the erroneous print would tend to move the legislation back to the form in which it left the House Committee. If the omission was accidental, it reflects lack of deliberation; if intentional, a fraudulent intent of someone acting behind the scenes to slant the interpretation of the agreed upon compromise back to the original subcommittee position which had been altered by House floor action. Materials hastily assembled in a report after a virtually nonexistent conference between the House and Senate are weak reeds for a court to lean on in divining legislative intent. They are typically drawn by staffers with a natural bias for interpreting the bill in a manner favorable to the form in which it left the committee or subcommittee where they had worked on it—not as it came to conference from the House and Senate.

Yet the altered view of the ICC in Ex Parte No. 320 (Sub-No. 2) relies on three sentences of the Report discussed in the preceding section and the court gives controlling weight to the ICC’s erroneous interpretation of them.
on this, has come to a conclusion so contrary to the legislative history, that
an analysis is necessary to rebut the interpretation given to it by the Report.

As discussed, the court recognizes that it is the language of the 4R Act
that governs market dominance. Yet Judge Johnson, pointing to the Con-
ference Report, asserts that it "is particularly significant, since Congress
was aware of the ICC's stated intent to consider product and geographic
competition when the Staggers Act was debated."36 Indeed, Congress
was well aware of it, but the dominant assumption that colored the debate
was that the Rail Act would have to be changed if "effective competition"
were to embrace geographic and product competition. The Department of
Transportation was calling for a change in the statutory definition of market
dominance. It proposed to substitute two new jurisdictional tests for the
market dominance criterion set forth in the 4R Act. One would establish a
quite high cost recovery ratio for rail traffic below which the ICC would not
have jurisdiction; the other would provide that carrier rates could be
whatever the carrier could obtain if effective competition existed under a
broadened definition of that term.37

In the administration bill "effective competition" would be present
where there exists an "actual or present potential transportation alternative
. . . for the particular transportation to which the rate applies." Furthermore, effective competition would be deemed to exist if "the consignee is
able to obtain the same commodity in sufficient quantities from another
source at a delivered cost which is not substantially greater than the cost of
the rail transported commodity."38 The administration bill also struck out
the key words in the 4R Act, "for the traffic or movement to which the rate
applies," then substituted for them the words "with respect to the transpor-
tation to which the challenged rate applies." But the administration bill sup-
porters recognized that there could be instances in which, if legislative
standards were not laid out, railroads could seize upon an inordinately high
rate in an isolated and exceptional situation to exercise a monopoly
squeeze, when in fact there was no effective competition. Thus, if a carrier
could avoid regulation by merely pointing to a shipment of coal from some
remote point at a higher rate than that demanded by the carrier for the
particular haul, the railroad would be free to exact anything up to that rate.
Therefore, the Florio approach required a showing that "comparable traffic
has been shipped recently in similar quantities"39 over the route.

36. Western, 719 F.2d at 780.
37. These changes were incorporated into the Rail Act of 1980, H.R. 7235, 96th Cong., 2d
38. See id. § 202 (containing proposed amendment to 49 U.S.C. § 10709). See also H.R.
4000-01.
Thus, even the railroad faction supporting the administration bill was not seeking to displace ICC jurisdiction with altogether standardless authority. Such baseless authority was seized upon by the Commission in Ex Parte No. 320 (Sub-No. 2) and condoned by the Fifth Circuit upon a rationale that it cannot look into the reasonableness of such a construction because Congress has granted only the Commission that authority. But the exercise of such unlimited authority was not one of the options considered in the course of passage of the Staggers Act.

On the other side of the debate was the shipper faction, which had consistently contended that the Coleto Creek case misinterpreted the jurisdictional standard of the 4R Act. This group's leadership was centered in the Subcommittee on Oversight and Investigation of House Interstate and Foreign Commerce, and its position had been enunciated in early 1980 by a Committee Print issued by the Subcommittee. Its position was there stated as follows:

The Subcommittee finds that the ICC's implementation of these market dominance regulations in coal rate cases during the 1977-1979 period comports with the mandate of the 4-R Act. The agency exercised its rate review authority in cases where direct competition was extremely limited or nonexistent. The Commission acted forcefully to issue findings of market dominance where long-term coal supply contracts foreclosed use of alternative carriers and modes.

Judge Brown, referring to the Committee Print, said in his dissent in the panel decision that the Subcommittee praised the ICC's treatment of market dominance. But it praised the ICC's treatment of market dominance as it was applied before the Coleto Creek case. Thus, the Print takes the opposite viewpoint from that for which it is cited. It condemns the departure of the ICC from traditional rulemaking procedures on ground that the new approach subsidizes the railroad's operations in competitive markets. The Print states:

Rate increases approved by the ICC greatly exceed those which would have been deemed reasonable under traditional ICC ratemaking standards. . . . From 1977 to 1979, the ICC justified extraordinary coal rate increases primarily on interpretations of Section 205 of the 4-R Act which are arbitrary, unworkable and inconsistent with congressional directives . . . . The ICC has applied its interpretation of Section 205 so that coal shippers subsidize non-coal traffic. The agency's theory is that coal revenue should subsidize a carrier's operations in competitive markets. Since the 4-R Act deregulates rates in competitive markets, a policy to insulate a carrier from the discipline of ef-

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40. Incentive Rates on Coal — Axial, CO, to Coleto Creek, TX, 362 I.C.C. 572 (1980).
42. Id. at 44 (emphasis added).
43. Western, 694 F.2d at 395 n.3 (Brown, J., dissenting).
ective competition is contrary to congressional intent.44

Thus, the shipper side always took the position that the 4R Act applied the definition of market dominance that excluded geographic and market competition from consideration as effective competition for the movement involved. The railroad side did not insist that the ICC already had authority to recognize geographic and product competition, but rather that it should have such authority, and, of course, their bill would have granted it.

A. The Resolution of House Differences

After extensive debate, a compromise was struck in the Staggers-Rahall substitute which supplanted the earlier amendment45 and became the pertinent part of the enacted bill. The substitute abandoned the immediate application of the cost recovery percentage. Also, it accepted the Eckhardt-Rahall proposal presuming no market dominance for rates less than 160%, but only through September 30, 1981. It moved the threshold upward five percentage points on October 1, 1981, and another five percentage points on October 1, 1982. Then, from October 1, 1983, through September 30, 1984, the threshold figure was to move to the lesser of 175% of variable cost or the cost recovery percentage. After October 1, 1984, the cost recovery percentage was to be used to determine the ICC’s jurisdictional threshold with the qualification that it be not more than 180% nor less than 170% of variable cost.

In the final resolution of the dispute, the House dealt with this issue of geographic and product competition in a rational way. It excluded its use as a jurisdictional barrier, and provided in § 205 that the Commission should commence a proceeding to determine whether, and to what extent, geographic and market competition should be used in determining rate reasonableness. But it expressly excluded consideration of this language (permitting consideration of geographic and product competition) in defining the term “market dominance.”46

The fact that Congress provided this flexibility in the realm of rate reasonableness clearly shows that it did not desire to open the door for the Commission to construe its jurisdictional scope, and it made this clear in explicit terms.47 To permit the consideration of geographic and product

44. IFC Print, supra note 41, at 3 (emphasis added).
45. It did not, however, restore the strucken language referred to supra.
47. § 205 provides in subsection (3)(B): Nothing in this subsection shall be construed as altering the meaning, use, or interpretation by the Commission, the courts, or any party of the term “market dominance,” as defined in section 10709(a) of title 49, United States Code. The enactment of this subsection shall not be considered by the Commission in any proceeding, or by any court on an appeal from that or any other proceeding, to determine the proper scope of the term
competition as jurisdictional barriers would not have merely introduced this factor in determining rate reasonableness, but would have precluded weighing against it the desirability of having railroad competition for the traffic movement to which the rate applied.

Thus, the House, and ultimately Congress, acted in an even-handed way; providing such flexibility to the Commission as Congress chose, but without, as the court erroneously held, giving the Commission a mandate to construct its own area of authority. That area, if there be doubt about it, remains to be construed by the court under the language of the statute, not by the ICC. Congress did not leave the determination of market dominance to conjecture in a committee report; on the contrary, it made the determinations legislatively in the provisions codified as section 10709 of the Interstate Commerce Act. These contain both the market dominance provisions of the 4R Act and the provisions of section 202 of the Staggers Act.

These provisions, and the history that surrounds them, demonstrate that Congress was aware of the ICC’s stated intent to consider product and geographic competition when the Staggers Act was debated, and it dealt with the matter in the final configuration of section 10709. But Congress did not choose to ratify the ICC’s intent to treat these factors as determinations of market dominance. It chose to treat them as being permissible considerations in determining rate reasonableness. The courts should construe the Act in accordance with the intent of Congress so expressed in the language of the Act and in the language of those who actually engaged in its formulation.

B. THE INTENT OF CONGRESS AS REFLECTED BY ACTION AND STATEMENTS ON THE FLOOR

The important point, for purposes of this discussion, is that all the language supportive of geographic or product competition as an element in determining market dominance remained stricken. Thus, the 4R Act’s treatment of market dominance continued intact. The disputants had settled their differences by dealing with the rate-level jurisdictional threshold and by leaving the market dominance jurisdictional threshold as it had been traditionally interpreted.

The most important single expression in the course of this legislative history is the statement of Representative Rahall, who had been active during the floor debate and had been a party to all the main amendments on this issue. He had just co-authored the amendment which struck the compromise between shippers and railroads; this dispute had been so heated

"market dominance" or whether there is market dominance over the transportation to which any particular rate applies.

that Chairman Florio suspended the bill until a compromise had been reached. Representative Rahall stated:

This compromise amendment today is not undoing what the original Eckhardt-Rahall amendment accomplished. . . . It will assure that the Interstate Commerce Commission does not proceed headlong into deregulation without guidelines and without a bill from the Congress . . . .

It should be noted that Mr. Rahall was at that time working on the team with Subcommittee Chairman Florio and full Committee Chairman Staggers and was in complete accord with them. There is nothing in the record that indicates any contradiction or contrary viewpoint. The bill as so amended became law largely as it was compromised in the House.

The statement of legislative intent of Congressman Rahall is far more credible (because of its source, the fact that it was made on the floor, and that it stood without contradiction), than the staffer’s statement so heavily relied upon by the ICC and the court. It encapsulates the situation which existed and is confirmed by all the legislative history.

There were two well understood options on the floor: (1) To retain the market dominance standard as it had been enunciated in Ex Parte No. 320 as having the effect that its language spontaneously yields; or (2) to change it to a clearly enunciated authority permitting consideration of geographic and market competition under guidelines. Congress chose the former course, since no one even proposed consideration of geographic and market competition without guidelines. Nevertheless, the ICC has proceeded “headlong into deregulation without guidelines,” a course which Representative Rahall assured would not be sanctioned. The court in Western Coal Traffic League has sanctioned it on the basis that it can do nothing else, the Congress having willed it so. The Rahall statement accurately reflects the actions and intent of the framers of the Act as being precisely to the contrary.

VII. THE COURT’S ARGUMENT THAT “WE MUST DEFER TO THE AGENCY’S DETERMINATION”

It is clear that the court should have construed the legislation as deciding the question against treating geographic and product competition as competition which precludes market dominance. The court, however, decided that Congress had not given it that option; that only the ICC was empowered to establish a “construction of its statutory authority” by virtue of certain language in section 202(b) of the 4R Act. It is the purpose of this section to show that such is not the case.

It is true, as the court says, that, in the 4R Act in 1976, “Congress not only expected but required the ICC to undertake the task of developing

'standards and procedures' for determining 'whether and when a [railroad] possesses market dominance.' 49 That authority—of a type that is customarily provided in a statute to permit an agency to 'set up housekeeping' under a new provision of law—was in effect on August 21, 1976, when the ICC established Special Procedures for Making Findings of Market Dominance as Required by the Railroad Revitalization and Regulatory Reform Act of 1976. 50

If, indeed, this authority, as delegated to the Commission by the 4R Act, permitted the broad leeway attributed to it by Judge Johnson, the Commission did not use the delegation to stray from the strict construction of the words "effective competition . . . for the traffic or movement to which the rate applies." Thus, it construed the Act as prohibiting it from stretching these words to include geographic and market competition.

Let us assume, arguendo, that the language in section 202(b) of the 4R Act, permitting the ICC to "establish, by rule, standards and procedures for determining . . . whether and when a carrier possesses market dominance," did authorize the ICC at that time to establish a "construction of its [own] statutory authority." This construction is unlikely, and the case that the court cited in support of its holding on this point, Aberdeen & Rockfish Railroad v. United States, is clearly distinguishable. 51 But even if it had done so, there was no such authority extant at the time the ICC (having failed in 1980 to attain such express authority in the 96th Congress) attempted in 1981 to enlarge its own authority to permit it to consider geographic and product competition as a jurisdictional barrier. By that time the language authorizing the development of standards and procedures to implement the 4R Act had been withdrawn. Since the Commission's activities

49. Western, 719 F.2d at 778.
51. 682 F.2d 1092 (5th Cir. 1982). The exercise of authority by the ICC here is very different from that reviewed in Aberdeen, relied on by the court. There the ICC had required that, if a carrier desired to change rates in a tariff required to be posted, it must indicate the changes by use of uniform symbols: (R) to denote reductions; (A), increases; or (C), changes which result in neither. Failure to comply would permit claims for overcharges on grounds that the changed tariffs were unlawful, and such claims could be filed within the prescribed three year limitation period.

Upholding the authority, the court in that case held that the requirement did not raise "difficult issues of economic cost and common carrier responsibility," id. at 1098, and was within the ordinary regulatory authority of the agency. The court recognized, however, that "[s]tatutory construction normally raises only questions of law, which are freely reviewable de novo by the Courts." It further stated that the flexibility permitted under the facts of that case "does not permit us blithely to accommodate each new gloss placed by an agency upon its enabling legislation without troubling ourselves to inquire whether the revised interpretation, ruling or practice remains plausible within the authority conferred by statute." Id. at 1100.

In the instant case the "new gloss" was an interpretation of the agency's basic jurisdiction in the field of railroad regulation with the potential effect of moving the ICC out of that field even when a railroad has complete monopoly control of all railroad transportation out of a given area and when the movement of the goods is not feasible through any other mode of carriage.
under the new concepts had been fully established, Congress omitted this provision in its codification of the revised Interstate Commerce Act, enacted on October 13, 1978.\textsuperscript{52}

This chronology has great significance because the rule in support of which \textit{Batterton v. Francis}\textsuperscript{53} is cited is therefore not applicable. It is that rule which underlies the court's holding that "we must defer to the agency's interpretation of the statute and affirm that interpretation if "it has a reasonable basis in law.'"\textsuperscript{54} The court assumed that, in 1981, the ICC continued to have authority to set standards and procedures under the terms of section 202(b) of the 4R Act, although the majority opinion recognizes that those terms had been repealed. At most, "authority" could be implied, but this is hardly a reasonable basis for finding express delegation to an agency. Therefore, the court was clearly wrong in deeming it "inconsequential" that "the members of this Court might have construed the statute differently."\textsuperscript{55}

A. \textbf{Power Not Delegated to ICC to Determine Own Jurisdiction}

\textit{Batterton v. Francis} would only support the final court decision if Congress had delegated to the ICC the power to define market dominance more narrowly than would be reflected by a literal interpretation of the language of the 4R Act. It is doubtful that power was ever delegated to the ICC to determine in so broad a manner its own authority. It is certain that no such "expressly delegated" authority existed at the time the ICC decided Ex Parte No. 320 (Sub-No. 2).

Thus \textit{Batterton v. Francis}, as applied to the facts of this case, stands for the rule which it ordinarily establishes as applicable when no such express delegation exists: "Ordinarily, administrative interpretations of statutory terms are given important but not controlling significance."\textsuperscript{56} Thus, the court's decision that it could not apply its own judgment to this paramount issue in the transportation field—but must, per force, defer to the agency's interpretation—was not in compliance, but in conflict with the rule in \textit{Batterton v. Francis}.

It is true, of course, that the ICC has the rulemaking power ordinarily implied in an agency's mandate and, within the scope of authority granted it by Congress, may fill in the interstices of the Interstate Commerce Act. But, as the Supreme Court said in \textit{CAB v. Delta Air Lines},\textsuperscript{57} the Board "is en-

\begin{itemize}
\item \textsuperscript{53} 432 U.S. 416 (1977).
\item \textsuperscript{54} \textit{Western}, 719 F.2d at 777.
\item \textsuperscript{55} \textit{Id}.
\item \textsuperscript{56} \textit{Batterton}, 432 U.S. at 424.
\item \textsuperscript{57} 367 U.S. 316 (1961).
\end{itemize}
tirely a creature of Congress and the determinative question is not what the Board thinks it should do but what Congress has said it can do." 58 Unless Congress has expressly given to the agency the power to determine what "it can do," it is the court that has both the authority and duty to make that determination. 59

It has been conclusively shown in previous sections of this article that the court should have taken the position on the market dominance issue that was taken by the panel and the two judges who were in the majority there and who dissented in the en banc decision. But there is yet a more powerful reason for the Supreme Court to grant certiorari in this case. The Court of Appeals for the Fifth Circuit, a strong and competent court, has erroneously deprived itself of independently interpreting the language of the Interstate Commerce Act defining the concept of market dominance. It has limited its consideration to whether the ICC's decision had "'a reasonable basis in law," or was arbitrary or capricious. 60

That the question did not fall in that narrow ambit of determination is amply supported by Volkswagenwerk Aktiengesellschaft v. Federal Maritime Commission. 61 In that case, as here, the question was one of construction of an agency's duty to accept responsibility under an act of Congress. The Court of Appeals for the District of Columbia had affirmed a holding of the Commission, restricting itself to determining only whether the Commission's ruling was supported by "'substantial evidence." The Supreme Court reversed on the basis that "'the issue relates not to the sufficiency of the evidence but to the construction of a statute,"' and holding that reviewing courts "'are not obliged to stand aside and rubber-stamp their affirmance of administrative decisions that they deem inconsistent with a statutory mandate or that frustrate the congressional policy underlying a statute."' 62

Thus, the Court in Volkswagenwerk considered the case on the merits and decided the proper interpretation to be placed on the statutory language involved. The en banc court, in rubber-stamping the ICC's altered view, made the mistake warned against in American Shipbuilding Co. v.

58. Id. at 322.
59. The instant case is in the mold of Delta Airlines v. CAB, 543 F.2d 247 (D.C. Cir. 1976), distinguished in Aberdeen. There, while CAB had authority to require air carriers to transport certain cargo and to reject or suspend tariffs, the authorizing statute required a notice and hearing. The court held that the matter of whether CAB had complied with the statute is for it to decide and overturned the Board.

The en banc decision of the court also cites United States v. American Trucking Ass'n, 310 U.S. 534 (1940). But, although in that case the Court sustained agency action, it did so after considering and construing the statutory language, saying: "'There is, of course, no more persuasive evidence of the purpose of a statute than the words by which the legislature undertook to give expression to its wishes.'" Id. at 543.
60. Western, 719 F.2d at 777.
62. Id. at 272 (Citing NLRB v. Brown, 380 U.S. 278, 291 (1965)).
NLRB: "The deference owed to an expert tribunal cannot be allowed to slip into a judicial inertia ...." 63

VIII. SUMMARY AND CONCLUSION

Congress, in the 4R Act, changed the rail regulation scheme from general regulation to specific regulation of only market dominated traffic. At the time, realizing that a sweeping change from the regulatory scheme which had existed for more than three quarters of a century was being established, it provided that the ICC should promptly establish standards and procedures by which the new concept should be put into effect. This did not mean that the Commission was granted specific authority to establish its own domain under the market dominance test as narrowly or as broadly as it wished. Standards are mechanisms within jurisdictional bounds, not bases for determining these bounds.

The ICC, acting under this authority, established the required machinery in Ex Parte No. 320. The statutory scheme having thus been completed, Congress adopted the revised Interstate Commerce Act in 1978, withdrawing the direction and standard-making authority. At this point the new framework of regulation under the Commerce Act was complete. The jurisdictional determinations which were fixed and intended to remain in place consisted of: (1) the statutory definition of market dominance, and (2) the general standards and directions established under Ex Parte No. 320, specifically delegated by section 202(b) of the 4R Act and impliedly approved by the revised Interstate Commerce Act of 1978. What remained for ICC administrative control was the application of these statutory definitions and standards to specific cases.

The proposed legislation that culminated in the 1980 Staggers Act did not suggest a change from the basic concept of deregulation of traffic where effective competition existed and regulation of traffic where there was none. But it did reopen—wider than the ICC could—the question of what competition should be considered effective.

Ultimately, the two sides of the debate in Congress came to a practical solution. Stated simply, their agreement was that "it is excellent [for a railroad] to have a giant's strength," 64 but it is impermissible for it "to use it like a giant." Thus, as long as the rate did not exceed established thresholds

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64. Oh, it is excellent to have a giant's strength,
   But it is tyrannous to use it like a giant.
W. SHAKESPEARE, MEASURE FOR MEASURE, Act II, Sc. 2, 1.108.
presumed not to evidence the use of monopoly control—or, more accurately, not to evidence market dominance—the ICC would not interfere.

Congress was not able to reach agreement on a change from the market dominance standard in the 4R Act. The more complex and far-reaching concept of the "actual or present potential transportation alternative" test was rejected by adoption of the Eckhardt-Rahall amendment and later, the Rahall-Staggers substitute.

If Ex Parte No. 320 (Sub-No. 2) were to stand, the entire debate and compromise in Congress would come to naught. The result would be that the railroads would enjoy the advantages given them in the compromise that resulted in the Staggers Act, a safe harbor for rates below the applicable threshold. The shippers would be deprived of the advantage they obtained in the compromise—the continuation of the concept of market dominance, confined within the terms of the statutory definition and the workable standards of Ex Parte No. 320, as the jurisdictional basis for rate regulation.

Nothing could more powerfully demonstrate how great this deprivation for shippers would be if Ex Parte No. 320 (Sub-No. 2) were upheld than the ICC's recent decision in Aluminum Association, Inc. v. Akron, Canton & Youngstown Railroad. This case held that the burden "is on the complainants to prove market dominance by demonstrating that there is an absence of effective competition for the traffic to which the challenged rates apply;" second, that the parameters within which the ICC determines "effective competition" are so broad as to make its determinations practically standardless.

It is true that the burden of proof for market dominance has always been on the complainant, but that burden becomes much greater when the shipper is called upon to disprove effective competition for any product from any place. The basis upon which the court in the Aluminum case justifies acceptance of jurisdiction on all four of the "effective competition" tests, linked with the nimbleness and alacrity with which the Commission overturns the decisions on each of them, amply illustrates that, under the ICC's present test, it may decide either way under any conceivable set of facts in which market dominance would have ordinarily existed under the original Ex Parte No. 320. The fact that the burden of proof is placed upon the shipper makes a showing of market dominance impossible against the Commission's determined effort to throw into the equation every possibility of competition of any magnitude, from any place.

66. Id. at 480.
67. The Aluminum case includes product competition from abroad as a means of disproving market dominance, thus bringing in the same concept of geographic competition from overseas that was involved in its Coleto Creek decision. If such competition is to be considered at the
Even the House Commerce Committee, which had accepted the general theory of the administration bill, recognized that if the effective competition concept was to be broadened to include geographic and product competition, the burden would have to be shifted to the railroad side. Congress never considered a third alternative, which would impose a jurisdictional requirement that a complainant prove a standardless negative.

The ICC's action in Ex Parte No. 320 (Sub-No. 2), if upheld, would permit the Commission to bow out completely from control of railroad rates, even when they reflect the most flagrant uses of monopoly power. The history and content of the 4R Act and the Staggers Act clearly show that Congress never intended that the railroad industry should come full circle from an Interstate Commerce Act designed to prevent railroad monopoly to one fashioned to protect it. Unless the Supreme Court grants certiorari in Western Coal Traffic League v. United States, this will be the inevitable result. **

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threshold in determining market dominance, the Loeffer amendment, respecting coal, embraced in § 205(a)(2)(A) can have no effect. It provides that: "For the purpose of this section, any coal imported in the United States for the generation of electricity by utilities shall not be taken into account in the determination of whether coal is available to a consignee from another source." Pub. L. No. 96-448, § 205, 94 Stat. 1895, 1906.

Since the exception is limited by its terms to § 205, and nothing in § 205 is "to be construed as altering the meaning, use or interpretation . . . of 'market dominance,' as defined in section 10709(a) of title 49, United States Code," id., the Loeffer amendment under the ICC's determination here would become meaningless. The ICC would never get to the determination of rate reasonableness (in which it is denied consideration of foreign coal competition) because it would have denied jurisdiction upon that very basis.

If it had been thought by those hammering out the terms of Title II of the Staggers Act that geographic competition was to be considered in the determination of market dominance under § 202 of the Act, clearly the Loeffer amendment would have been added there. Mr. Loeffer cannot be thought to have done a futile thing. The logical conclusion of members was that it was not necessary to so amend § 202 of the Act because the concept of market dominance was not affected under the 4R Act definition by the existence of geographic competition; therefore, it was not necessary to preclude foreign geographic competition.

On May 14, 1980, Mr. Eckhardt, in the mark up of H.R. 7235, offered a lengthy amendment aimed at elimination of the broader concept of effective competition embodied in the "actual or present potential transportation" test of the bill as it came from the Subcommittee on Transportation. It had been argued that such a broad concept made it virtually impossible for a shipper to sustain the burden of proving that there was no such transportation alternative, and the bill, as it emerged from the Subcommittee, placed the burden on the shipper. To counter this argument and to defeat the more extensive changes contained in the Eckhardt amendment, Mr. Madigan, a co-author of the bill, offered a substitute which changed the original language of the bill as it had come from the Subcommittee so as to shift the burden from the shipper to the carrier. Thus the original form resembled, in this respect, the result reached in the ICC's Aluminum case, but the Committee, by adopting the Madigan amendment, chose not to push the railroad advantage to the point to which the ICC has pushed it.

FACULTY COMMENT

Editor's Note: This issue of the Journal marks the inaugural appearance of a Faculty Comment. We hope this contribution and others will incite further debate on matters of topical interest in the transportation field among scholars and practitioners. Such Comments, however, will only reflect opinions of the authors. In our next issue, Professor Robert M. Hardaway of the University of Denver College of Law will respond to Professor Dempsey with a Faculty Comment entitled: Transportation Deregulation 1976-1984: Turning the Tide.

Transportation Deregulation — On a Collision Course?*

PAUL STEPHEN DEMPSEY**

* Based on testimony delivered by the author before the Senate Transportation Committee of the Colorado State legislature, the Iowa Transportation Commission, and a series of papers presented during 1983 before a number of seminars and conferences, including the 9th Annual Meeting of the Shippers National Freight Claims Council, Inc., at Orlando, Florida, the Organizational Meeting of Forward America, Inc., at Little Rock, Arkansas, the 25th Annual Meeting of the National Conference of State Transportation Specialists, at Reno, Nevada, the Annual Meeting of the Interstate Carriers Conference (Refrigerated Division) of the American Trucking Associations, Inc., at Durango, Colorado, the Annual Meeting of the Iowa Motor Truck Association at Fort Dodge, Iowa, and the Annual Meeting of the Colorado Motor Carriers Association at Colorado Springs, Colorado.

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I. INTRODUCTION

One can only observe with fascination that the transportation industry has come full circle, from its genesis in an unrestrained laissez faire economic environment, through almost a century of comprehensive governmental regulation of entry, rates and other corporate activity, and now back to the unconstrained free market. The excesses of the marketplace preceded regulation, and those excesses have reappeared under deregulation.

This article will examine where the great American transportation experiment has been, where it is, and where it appears to be going. It will begin with an analysis of the events which led our nation to establish a regime of economic regulation upon the transportation industry. It will then examine the metamorphosis toward deregulation, and evaluate the results of reducing governmental controls of entry and pricing in the aviation and motor carrier industries. These impacts fall generally into five categories: (1) economic decline of the industry; (2) diminution of safety; (3) discrimination in pricing; (4) deterioration of service; and (5) erosion of carrier liability for loss and damage. Because the rail experiment in deregulation differs in significant respects from motor and air carrier deregulation, it will be explored separately. Finally, this article will summarize and evaluate the political forces which now seek to swing the pendulum away from the grand experiment in deregulation and toward some moderate form of responsible economic regulation.
II. THE GENESIS AND METAMORPHOSIS OF REGULATION

A civilization which does not learn from its history is doomed to repeat it. Throughout recorded history, transportation has consistently been perceived as an industry imbued with a particular public interest. Indeed, long before colonization of the American continents, the common law of England (resting upon foundations established by Roman law) treated certain sectors of the industry as "common carriers," and subjected them to an obligation to serve the public without discrimination in service or pricing.\(^1\) American courts embraced this concept in its common law, and endorsed the legal creature of bailments, under which common carriers were obligated to treat goods entrusted to them with the highest degree of care.

In the United States, congressional interest in regulating transportation was stimulated by the excesses of the railroad industry in the late 19th century. Rail carriers were charging exorbitant rates in their monopoly and oligopoly markets, and predatory rates in their competitive markets. Small communities served by only a single rail line were forced to pay whatever the market would bear; for this they often received poor service, even when they were closer to destination markets than large communities.\(^2\)

It was at first the state governments which attacked the abuses of the rail industry.\(^3\) Such abuses included the bribery of public officials,\(^4\) the

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3. See W. Augello, supra note 1, at 433-36.

4. Bribery of public officials included the efforts of the directors of the Union Pacific to confer large blocks of stock to congressmen and Vice President Schuyler Colfax. S. Morrison, The Oxford History Of The American People 730-31 (1965). In order to promote transcontinental rail interests, Collis P. Huntington effectively bought the California legislature and bribed numerous congressmen. Id. at 732.

Railway builders and owners, like James J. Hill, [entrepreneur of the Great Northern Railway] had the point of view of a feudal chieftain. Members of state legislatures were their vassals, to be coerced or bribed into voting "right" if persuasion would not serve. In their opinion, railroading was a private business, no more a fit subject for government regulation than a tailor's shop. They were unable to recognize any public interest distinct from their own. In many instances the despotism was benevolent; and if a few men became multimillionaires, their subjects also prospered. But Collis P. Huntington, Leland Stanford, and their associates who built the Central and controlled the Southern Pacific were indifferent to all save considerations of private gain. By distributing free passes to state representatives, paying their campaign expenses and giving "presents" to their wives, they evaded taxation as well as regulation.

These exactions and abuses were long tolerated by Americans, so imbued were they with laissez-faire doctrine, so proud of progress, improvement, and development, and so
sale of worthless securities,\textsuperscript{5} and rate and service discrimination between places and persons.\textsuperscript{6} The pricing irregularities were perhaps the most sig-

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\textit{Id.} at 763-64.

5. The Erie Railroad competed with the New York Central at the time, and Vanderbilt wanted to control the competing line. He quietly began purchasing stock to gain control. However, the Erie was owned by Jim Fisk, Daniel Drew and Jay Gould, who got wind of the takeover attempt and began issuing watered stock. Said Fisk, “If this printing press don’t break down, I’ll give the old hog all he wants of Erie.” Although Vanderbilt had himself issued watered stock from time to time, he was taken. Both sides bribed New York legislators and judges in the ensuing struggle over control of the Erie. As a result of such stock manipulation, the Erie was unable to pay dividends for half a century. See N. PLATT & M. DRUMMOND, OUR NATION FROM ITS CREATION 444-45 (1964).

Jay Gould subsequently gained control of the Union Pacific and led it to purchase the inflated stock of other rail carriers he controlled. These actions naturally injured other stock holders and public, for the carriers found it necessary to maintain high rates in order to pay dividends on these inflated stock issues. H. BRAGDON & S. MCCUTCHEN, HISTORY OF A FREE PEOPLE 427 (1967).

6. The economic environment of the transportation industry in the 19th century has been described as follows:

Power railroad companies expanded rapidly, and by the latter decades of the century, they dominated the transportation of America’s goods. Regional commercial and financial interests contributed to the rapidly expanding network of rail line connecting major cites.

The profit opportunities realized by rail companies in many of those market areas often attracted new railroad competitors who, from time to time, would initiate rate wars to attract traffic from the original lines. Competition of this type soon drove out profits for all carriers in the market, and this led to efforts to pool traffic or divide markets to reestablish monopoly profit levels. A dissatisfied member of such a pooling arrangement might resume a rate war to reallocate traffic from other railroads serving the same points. Intermediate points served by only one railroad were captive and, therefore, did not benefit from the price-cutting activities. Accordingly, a railroad rate structure evolved in which rates were generally low, but unstable, between major points served by competing railroads (or in competition with water carriers) and high between points over which shippers had no alternate transportation. One side effect of this rate structure was the accelerated construction of branchlines to very small markets, since traffic that originated at those points did not need to be included in the pooling arrangement.

To complicate matters further, railroads found that by providing rebates, or kickbacks, to selected customers, they could also capture business from competing companies. These practices resulted in different shippers paying varying prices for the same service.

Thus, the transportation market of the late 19th century left almost everyone dissatisfied. The railroads tried to avoid the constant rate wars, rebates to favored shippers, or low rates. Farmers wanted lower rates and protection against discriminatory rate practices. Shippers in competitive markets wanted greater rate stability and assurances that they would not be placed at a competitive disadvantage relative to those shipping the same product from the same or other origins.

\textit{Dep’t of Transportation, A Prospectus For Change In The Freight Railroad Industry} 115-118 (1978) [hereinafter cited as \textit{Prospectus}].

One former ICC Commissioner has succinctly summarized the market abuses which led government to regulate the rail industry:

Turning to the 19th century, we find widespread rail abuses which led to the creation of the present system of rate regulation. The post Civil War railroad expansion was a period characterized by instability of rates, discriminations, destructive competition, and rebates and passes. The practice of granting passes consisted of nothing more than allowing certain shippers the privilege of riding free — a privilege which came to be
significant in convincing Congress of the need to regulate this industry. Preferred shippers enjoyed special rates, underbilling, and rebates. Although cities served by several rail carriers enjoyed a generous level of competition and relatively low rates, those which were only served by a single rail carrier paid comparatively high rates, even when they were closer to destination.

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looked upon by every large shipper as almost a vested right. A rebate was a portion of the transportation charge which a carrier would secretly refund, particularly in order to secure the traffic of a certain shipper. This not only discriminated against the other carriers in competition for the same traffic, but had the effect, in many cases, of placing the shipper’s competitors at a distinct disadvantage. Because the larger carriers could offer larger rebates, and because the larger shippers could offer more incentives to induce rebates, both the small carriers and the small shippers suffered while business became more concentrated.

Rate cutting played havoc with shippers and carriers alike, in localities where rail competition still existed. Rates were often made secretly or subject to change without notice, with the result that ordinary contracts between shippers and receivers became a risky undertaking. Discriminatory rates favored one locality and worked hardships to another; individual shippers were favored at the expense of their rivals.


7. Examples of rail carrier abuses of their monopoly position included the following:

[1]t cost shippers more to send certain goods from Poughkeepsie, New York, to New York City, where there was no choice but the New York Central Railroad, than all the way from Chicago, where the Pennsylvania and Erie railroads competed with it for traffic. The New York Central also charged higher rates in winter, when the Erie Canal was frozen, than in summer, when it was open. Sometimes competing lines kept up rates artificially by a practice known as pooling, whereby companies made agreements to fix rates and divide the profits according to a prearranged formula. Still another abuse was the practice of favoring big shippers over small by granting rebates.


One of Standard Oil’s principal weapons was the rebate (a discount on railroad charges). In 1872 the company made a secret agreement with the railroads running out of Cleveland by which the rates on its products would be from 25% to 50% below those charged other companies. In order to see that the railroads were not tempted by higher rates into carrying its competitors’ oil, Standard Oil had the railroads pay it a “drawback” on every barrel of competitors’ oil shipped. Standard Oil was also furnished with the waybills telling the destination of competitors’ oil.

This agreement gave Standard Oil such an advantage over all other Cleveland refineries that within three months all but five of them were forced to sell out. Once in control of oil refining in Cleveland, Standard Oil moved rapidly toward a national monopoly. It did this by forming an alliance of the strongest companies and ablest men in the oil business, and by gaining control of the transportation of oil.

Id. at 391-92.

8. Rail rates vacillated wildly prior to regulation.

The years of explosive building were also years of chaotic rates. While shipping costs on balance decreased during the eighties, it often took a very discerning eye to recognize the long-range benefits. What the farmer and local merchant did see was an exceptionally erratic rate pattern, now up, now down, seeming to follow no logic beyond the caprice of a distant magnate. As a matter of course railroad executives compensated for a low return on competitive through traffic by adjusting their charges at all noncompetitive points. Sometimes month by month, almost always without notice, townsmen received insulting reminders of their utter helplessness before the fiat of an unknown czar.

The railroads, in the cautious phraseology of the first Interstate Commerce Commission, had “determined at pleasure what should be the terms of their contractual relations with others . . . , [terms] which intimately concerned the commercial, industrial and social life.
As a result, transportation prices were frequently higher on a shorter haul than those on a longer haul on the same line in the same direction.

An example of such excessive competition was that practiced between the Erie and the New York Central railroads on traffic between Chicago and New York. After a series of rate reductions which lowered the price of shipping cattle to less than $1.00 per car, Jim Fisk (President of the Erie), purchased all the cattle available and shipped them aboard the New York Central.9 Discrimination by railroads between large and small shippers also prompted Congress to promulgate legislation in 1887 creating the nation’s first independent regulatory commission, the Interstate Commerce Commission (ICC).10

By the 1930’s, motor carriers had become a major mode of freight transportation. During the Great Depression, cutthroat competitive practices became so excessive that the industry suffered severe economic losses; highway safety was impaired; service became dependable; and rate wars were rampant.11 Congress added motor carriers to the federal regulatory scheme in 1935.

Among the additional reasons which convinced Congress to enact legislation in this field were the need to stabilize economic conditions in the motor carrier industry, and to eliminate cutthroat competition. During the Great Depression there was an oversupply of transportation facilities and intensive competition among truckers. Such competition was depressing freight rates excessively and causing an alarming level of bankruptcies. It was feared that continuation of such unrestrained market forces might well lead to an eventual loss of service and/or higher prices for small shippers and small communities, while the surviving carriers concentrated on high-revenue “cream” traffic.12

of the people.” Far more than a decade’s averages, that feeling of impotence set the townsman’s view of his enemy.

R. Weiße, The Search for Order 48 (1967).

9. A former Congressman summarized the high level of price competition which existed between carriers serving common points as follows:

Rate wars become rampant, each carrier trying to underbid the other with little regard for cost considerations. Much traffic was carried at a loss in the hope that the fierce competition would drive the other carriers out of the business leaving the entire field to the victor, who could then make its own terms with the shipper.

Thus, it was reported that in the late 1860’s, cattle were moved from Buffalo to New York City for $1.00 per car. . . . It has even been reported that in the late 1870’s cattle were carried free of charge from Chicago to Pittsburgh and for $5.00 per car from Chicago to New York.


Congress added airlines to the regulatory scheme only three years later with the establishment of another independent federal regulatory agency, today's Civil Aeronautics Board (CAB). This legislation was promulgated for many of the same reasons which led Congress to enact the Motor Carrier Act of 1935, including the desire to avoid the deleterious consequences of cutthroat and excessive competition, and thereby enhance economic stability, safety, and the sound growth and development of this young industry.\(^{13}\) Further, the CAB was given jurisdiction over the interstate airline industry in order to relieve its perilous economic condition and ensure safe, dependable, nondiscriminatory air transportation between the nation's cities.

That the public has a strong interest in the provision of safe, adequate, dependable and non-discriminatory transportation is reflected in the extent to which American government today contributes to its existence beyond economic regulation — the construction of highways and canals, the distribution of mail, and the provision of urban mass transportation and intercity rail passenger service. If there is no public interest in transportation, should not these contributions of government be left to the free market? One suspects that the nation's arteries would become clogged in chaos if the marketplace were to dictate who would build highways and deliver the mail, and who (if anyone) would shuttle passengers between their homes and work, and at what price. A nation's economy cannot grow and prosper without a healthy and vibrant transportation system to serve it. To say that the marketplace can satisfy all the needs of a diverse nation is to ignore the existence of a strong and unique public interest in assuring the provision of safe, adequate, dependable and non-discriminatory transportation to its citizens. Nothing is so stagnant as a commodity that cannot move from its point of manufacture to its market, at a just and reasonable price, within a reasonable time, and within reasonable limits of safety.

III. THE BENEFITS OF REGULATION

Regulation brought to the transportation industry the stability essential to its growth and prosperity, thereby enabling the nation to enjoy a high level of safe and dependable service at reasonable rates, without discrimi-
nation between shippers or communities, large or small.\textsuperscript{14} Transportation enjoyed a generous level of healthy competition without concentration—an economic environment unequaled in almost all other major American industries.

Prior to deregulation, more than 16,000 regulated motor carriers and perhaps as many as 100,000 unregulated motor carriers served American shippers.\textsuperscript{15} The eight largest motor carriers accounted for only 14\% of the industry's total revenue. In contrast, the eight largest steel manufacturers controlled 65\% of that industry's revenue; the eight largest cigarette manufacturers were responsible for 100\% of cigarettes inhaled by Americans; and the four largest automobile manufacturers accounted for 97\% of that industry's revenues. In stark contrast, the annual gross revenues of 80\% of regulated trucking companies was less than $50,000.\textsuperscript{16} Under regulation, more than forty motor carriers competed in the Minneapolis-Chicago market, and more than seventy carriers "fought it out" in the New York-Boston market.\textsuperscript{17} Only two American industries enjoyed less concentration than did the motor carrier industry—miscellaneous machinery, and feminine wearing apparel.\textsuperscript{18}

A former ICC Chairman has summarized the benefits of economic regulation as follows:

[Transportation] regulation provides a basis for determining and assuring minimum levels of service to all parts of the country at a reasonable rate; even if the demand for trucking services in small towns or intercity areas, or by small shippers, would not justify the same level of service at the same level of rates. By so doing, regulation promotes the economic development of less populated areas. Regulation, by preventing unjust discrimination, can prevent large ship-

\textsuperscript{14} Professor Wagner has pointed out that:

\begin{quotation}
Regulation brings with it a certain stability in achievement of transportation objectives with little discrimination among the various customers (shippers), individual carriers, and basic geographic areas; and rates are kept within reasonable limits.

Regulation affords opportunity to gain rate equity among various shipper groups in different geographical areas and between commodities. And discrimination is lessened.

Certain shippers are forced to employ a limited number of carriers. Such "captured" shippers are potential victims of price gouging if regulations are removed. Regulation offers protection from being charged unreasonable rates and builds confidence in knowledge of the applicable rates. Without regulation, no shipper is certain of transportation costs, thereby creating confusion in both traffic and accounting departments. Carrier selection decisions are also more difficult.
\end{quotation}


pers and large carriers from exercising their market power to compel preferential treatment, where that treatment is not justified by lower costs. The regulatory role adds a measure of stability to the industry by providing a forum for the discussion of changes. Also, it can operate to reduce concentration in the industry by affording a measure of protection to smaller carriers.

Those are significant virtues and they can be realized only if the Government plays a role in allocating economic resources through the regulatory process.19

In essence, economic regulation of transportation sought to insure the protection of public interest values which might not find a high priority among businesses operating in a free market:20 (a) the provision of an adequate

19. Id. at 80 (statement of A. Daniel O’Neal).

This country, prior to the movement for deregulation, possessed an excellent transportation system, envied throughout the world. It was subject to controls which afforded the public with responsive transportation at reasonable, sensible rates. During the 30 years I have been involved in transportation, there has never come to my attention an instance when a shipper of general freight could not obtain service for its traffic. Rates were fair and, generally, nondiscriminatory and nonpreferential, and shippers could readily determine what their competitors were being charged. Carriers, under this system, were permitted reasonable profits, sufficient earnings to afford equipment replacement programs and to obtain efficient vehicles, and the costs of this transportation, historically, were at levels below that of the inflation experienced in our national economy.

D. Baker, Deregulation: Where We Were; Where We Are; Where We’re Going (May 23, 1983) (unpublished address before the Western Traffic Conference, Monterey, Cal.).

20. The free market model depends ultimately on the assumption that the free market will best satisfy public values through the instrumentality of the invisible hand. Yet the evidence is overwhelming that public values and the goals of firms diverge sharply. . . . The enormous volume of fraud that the F.T.C. and various federal, state, and local bodies have uncovered points to the inescapable conclusion that when profits and sales goals conflict with public values, the latter must yield in business calculations. . . . Profits and growth are the supreme values for corporations. If firms’ discretion were further enlarged through the operation of the freemarket principle, we might expect that in some areas their derelictions would expand correspondingly, even if some market distortions attributable to regulation disappeared.


[The ballot of the market place does not provide to man an adequate means of protecting and promoting his interests. . . . In spite of the multitude of individual ballots, continuously cast, there are grave limitations on the capacity of the economic vote:

1. It cannot provide many common services desired by all or by significant groups.
2. It cannot correct abuses and injustices in the operation of the economic system.
3. It cannot deal successfully with the interrelationships and the interdependencies within the economy.
4. Money is the usual means of economic balloting and the lack of it deprives many of the ability to vote.

. . . . . Man has turned to politics and to creation of the administrative state because his ballot in the market place did not satisfy all of his interests.


The existing regulatory system provides for the allocation of resources in the motor carrier industry, not only on the basis of market forces, but also in an attempt to secure certain social objectives. The marketplace allocates resources based on dollar votes cast by consumers in the marketplace. A regulatory system will allocate resources in part
level of service at reasonable rates throughout the nation; (b) the prevention of price or service discrimination between communities or shippers, large or small; (c) the establishment of economic and service stability for the industry and the public it serves, and (d) the reduction of carrier concentration, and concomitantly, the protection of smaller competitors. Regulation conferred upon common carriers both a benefit and a burden. It coupled the opportunity to serve with an obligation to serve, at rates not higher than those deemed by government to be just and reasonable, non-

based on real votes cast by consumers in the legislative and political process. The marketplace will, theoretically, produce the most efficient economic system. But economic benefits are not necessarily the same as social benefits.

Motor carrier regulation provides a basis for determining and assuring "minimum levels" of service to all parts of the country at a "reasonable rate," even if the demand for trucking service in small towns or inner city areas would justify the same level of service at the same level of rates. By so doing, regulation promotes the economic development of less populated areas. Regulation, by preventing "unjust discrimination," can prevent large shippers and large carriers from exercising their market power to compel preferential treatment, where that treatment is not justified by lower costs. A regulatory role adds a measure of stability to the industry by providing a forum for the discussion of changes by all affected parties. It can operate to reduce concentration in the industry, by affording a measure of protection to smaller carriers.

Those are significant virtues, and they can be realized only if the government plays a role in allocating economic resources through the regulatory process. Economic Regulation of the Trucking Industry: Hearings Before the Senate Comm. on Commerce, Science, and Transportation, 96th Cong., 1st Sess. 56 (1979) (testimony of ICC Chairman A. Daniel O'Neal).

In their book, DISMANTLING AMERICA: THE RUSH TO DEREGULATE, Susan and Mark Tolchin have written:

The goal is not a plethora of regulations; quantity does not guarantee quality. The goal is government protection against abuses that threaten our health, safety and lives. Without a shift to constructive policy making in the regulatory arena, the rush to deregulate is a high-risk gamble for the politicians who have championed its cause. It is a theory without a vision, without humanity and without conscience — a false panacea that will create more problems than it cures — and it should finally be recognized as such.

For regulation is the connective tissue of a civilized society. As technological and scientific advances lead us into unknown worlds with unimaginable dangers, society needs more protection, not less. This means more government regulation, intelligently crafted, skillfully managed and sensitively enforced. It means a new appreciation of government's role, born of a new sophistication in public attitudes.


1. The Constitution evidences the drafters' strong belief that there was a need to encourage and regulate commerce in order to ensure an unrestricted flow of essential goods and services. The transportation industry's essential role in the development of commerce and industry was an important reason for its early regulation. Under the regulatory scheme of the Interstate Commerce Act, protection of the public interest has been the dominant focus of policy development. That Congress deemed it necessary to regulate the transportation industry manifested a belief that competition alone would not adequately serve that public interest. Congress also believed that eliminating the discrimination in transportation prices and services, which had stilled competition among communities and shippers, would enhance competition in the remainder of the economy.

discriminatory and nonpreferential. It did this by creating a marketplace environment characterized by a healthy level of competition between a large number and wide variety of safe, efficient and dependable common carriers, who bore a responsibility to serve the public equitably. It was by no means a perfect system. Among its principal faults were a higher level of service competition than might exist without regulation, some inefficiencies in terms of empty backhauls, and some measure of regulatory lag (i.e., unnecessary time consumed as a result of bureaucratic lethargy). Nevertheless, by the mid-1970's the Interstate Commerce Commission had taken important steps to reduce these inefficiencies, and the Department of Transportation began to characterize it as "the finest transportation system in the world . . . [one which] moves more people and more goods usually at less cost and . . . with greater ease than any other nation or group of nations."

IV. **The Rise of Deregulation and Darwinist Economics**

Deregulation of transportation formally began in the late 1970's with President Jimmy Carter's appointment of economist Alfred Kahn to the position of Chairman of the Civil Aeronautics Board. As CAB Chairman, Kahn began interpreting the Federal Aviation Act liberally, diminishing entry barriers and encouraging vigorous pricing competition. Shortly thereafter, President Carter appointed Kahn's colleague, economist Darius Gaskins, to be Chairman of the Interstate Commerce Commission. Legislation solidified the deregulatory momentum in the airline industry. With the strong support of President Carter and Senator Ted Kennedy, Congress

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27. See *The Rise and Fall of the Civil Aeronautics Board*, supra note 13.
promulgated the Air Cargo Deregulation Act of 1977, and the Airline Deregulation Act of 1978. Motor carrier regulation was amended two years later, with the enactment of the Motor Carrier Act of 1980. Finally, the regulatory regime for railroads was further liberalized in 1980 with the promulgation of the Staggers Rail Act of 1980.


Columnist Carl Rowan noted that airline deregulation enjoyed widespread political support at the time such legislation was promulgated:

Note clearly that the chaos of airline "deregulation" is a bipartisan folly. In 1978, the Senate Republicans voted for it 31-0 and Senate Democrats approved it 49-9. In the House, Republicans, voted 118-3 and Democrats 245-5 for a "free enterprise" air travel system.

31. Pub. L. No. 96-448, 94 Stat. 1895. Recent federal legislation has also limited the jurisdiction of state governments over intrastate transportation.

The Transportation Act of 1920 first gave the ICC authority to raise intrastate rates that were so low as to constitute a burden on interstate commerce. The Supreme Court ruled in 1958 that an intrastate rate could not be raised by ICC simply because by itself it was not compensatory. Rather, the entire structure of intrastate rates had to be shown to be inadequate before the ICC could adjust any one rate. The Transportation Act of 1953 reversed that decision. The Act directed the ICC not to consider the totality of intrastate operations in evaluating individual intrastate rates. Further, it permitted the ICC to institute an investigation of an intrastate rate whether or not the rate was considered by a State authority.

The 4R Act modifies the authority of the ICC to adjust intrastate rates in two respects. First, the 4R Act requires a railroad company to file a request for a rate increase with the appropriate State agency, and the agency is given 120 days to decide the matter before it could be considered by the ICC. Second, the ICC is, after that time, empowered to raise an intrastate rate to the level charged on similar traffic moving in interstate or foreign commerce. This section assures that if a railroad company cannot raise intrastate rates to interstate levels through the appropriate State agency, the ICC will be able to make the adjustment without undue delay.

PROSPECTUS, supra note 6, at 124.

Under the Staggers Rail Act of 1980, a state may exercise jurisdiction over intrastate rail transportation, 49 U.S.C. § 10501(b)(1) (Supp. V 1981) only if it submits the standards and procedures it employs in exercising such jurisdiction to the ICC, id. § 10501(b)(2), and the ICC certifies such standards and procedures as being consistent with those employed by the ICC, id. § 10501(b)(3). Such certification shall last five years, id. § 10501(b)(4). In adding this provision to the Staggers Act, it was the intent of Congress "to ensure that the price and service flexibility and revenue adequacy goals of the Act are not undermined by state regulation of rates, practices, etc., which are not in accordance with these goals." H.R. Rep. No. 1430, 96th Cong., 2d Sess. 106, reprinted in 1980 U.S. CODE CONG. & AD. NEWS 4110, 4138.

The Bus Regulatory Reform Act of 1982 provides that intrastate passenger fares of interstate carriers may not be restricted by state law or regulation. Additionally, the ICC is given jurisdiction to determine that an intrastate rate for service over an interstate route is predatory, and to prescribe the applicable rate.

Under the new legislation, an intrastate rate is presumed to constitute an undue burden on
Deregulation was portrayed as offering to Americans the best of all possible worlds. Barry Bosworth told us it would save consumers some $8 billion, a figure subsequently endorsed by Messrs. Kahn and Kennedy. It was to give us a healthier, happier, more efficient industry — one which would provide the public with the wide range of price and service options dictated by consumer demand. It would reduce meddlesome governmental intervention in the marketplace, and eliminate regulatory lag and empty backhauls. Many of the deregulatory zealots must have seen themselves as high priests of economic truth, for they could envision no acceptable religious order than one of laissez faire. To arguments that many carriers would go bankrupt, they responded with platitudes of Economic Darwinism: “the strong and efficient would survive.” To arguments that small and remote shippers and communities would receive poorer but more expensive service, they told us that “this was the way the invisible hand of the marketplace worked.” Its proponents astutely exploited the popularity of the appropriate buzz words — the free market, less government, and competition. Deregulation began to sound as beautiful as “motherhood, apple pie and Chevrolet.”

Unfortunately, “[g]iving up government will require us to resubmit to the evils we had decided to prevent.”


34. See Wilson, The Goals of Transportation Policy, in THE FUTURE OF AMERICAN TRANSPORTATION 23 (E. Williams, Jr., ed. 1971).

35. Former ICC Chairman O’Neal noted that deregulation is a “buzz word, the mere mention of which causes brows to furrow, minds to cloud, and lips to quiver.” Anderson, The Motor Carrier Authorities Game, 47 ICC PRAC. J. 22, 23 (1979).

The deregulation effort was truly bipartisan, enlisting the all-out support of such diverse thinkers as Ralph Nader and Milton Friedman, Senator Edward Kennedy and President Gerald Ford. Liberals had climbed aboard the deregulation bandwagon, because they support anything that vaguely seems to favor small over big companies, and conservatives get behind any and all forms of deregulation.


V. THE IMPACT OF Deregulation in Air and Motor Transportation

A. Economic Decline

Since airline deregulation preceded motor carrier deregulation, let us first examine the airline industry. By 1980, as deregulation began to run its course, airlines broke new economic loss barriers. That year, the airline industry suffered record losses of $280 million.\textsuperscript{37} In 1981, the twelve largest air carriers alone surpassed this threshold by threefold, losing $641 million.\textsuperscript{38} Worldwide industry losses for 1982 were $900 million,\textsuperscript{39} despite the fact that the industry carried 7 million more passengers than it did the preceding year.\textsuperscript{40} Losses for the first half of 1983 exceeded half a billion dollars.\textsuperscript{41} If you add that to the burden of expenditures in interest payments...
on debt, the airline industry’s revenues fell more than two billion dollars short of breakeven during 1982. In fact, 1982’s airline revenues represented the first year-to-year decline in the industry’s history. For more than three years, the industry has suffered operating losses of more than a million dollars a day, or nearly two billion dollars overall. 42 Today, the industry’s debt has ballooned to seventy percent of invested capital. 43

Air New England, Braniff, Continental, El Al, Laker and sixteen other air carriers have entered various stages of bankruptcy since the promulgation of the Airline Deregulation Act of 1978. 44 Carriers such as Air Florida,
Eastern, Pan Am, Republic, Western, and World, have from time to time been placed on the endangered species list.45 During 1982, Pan Am sustained operating losses of $700,000 a day.46 Even traditionally healthy carriers like Delta are feeling the crunch, by posting its first operating losses since 1947.47 A number of the nation’s large air carriers would be thrown into bankruptcy if the financial institutions holding their long term debt (estimated to be $10.1 billion for the sixteen largest airlines) demanded timely payment.48 Prudent bankers, quite simply, are not interested in entering


46. A Gift From the Airlines, Newsweek, Dec. 13, 1982, at 108. To some extent, these losses have been offset by sales of its New York headquarters building ($294 million), and its Intercontinental Hotel Chain ($368 million). The Worst Year for U.S. Airlines, Time, Feb. 22, 1982, at 46; Cuff, Major U.S. Airlines Buffeted by Fierce Headwinds, Denver Post, May 15, 1982, at 11A. During 1982 Pan American lost $485 million — a new U.S. aviation record. The carrier’s immediate cash needs have been satisfied by two public offerings of secured and unsecured notes — debentures and warrants which totaled $250 million. Pan Am Chief Sees Bluer Skies, Newsday, May 11, 1983, at 37. Eastern Air Lines was recently losing $600,000 a day. Its pilots have tentatively approved concessions in excess of $100 million over the next two years, concessions for which they are likely to receive as much as 25% of the company’s equity. ‘[W]ithout an end to the cut-throat competition that has devastated the airline industry, Eastern’s future remains up in the air.’ Eastern’s Pilots Buy A Piece of the Airline, Newsweek, May 23, 1983, at 65. See Eastern Air’s Pay Plan Set for Nonunion Ranks, Wall St. J., June 6, 1983, at 12.


the used aircraft business; and certainly, calling in the outstanding loans would only result in the acquisition of large fleets of jets which, in this depressed economic environment, would be worth little.\textsuperscript{49} These losses have had a ripple effect on aircraft manufacturers such as Boeing, whose earnings have plunged forty-two percent,\textsuperscript{50} and Lockheed, which has recently been forced to virtually abandon commercial aviation.\textsuperscript{51}

One source predicts that "the number of major airlines will probably be reduced to five or six within the next five years as one or two more go into bankruptcy or merge operations with other air carriers."\textsuperscript{52} Another adds that the "airline industry under deregulation is on a course where competition is being wrung out by the creation of an oligopoly of a few remaining large airlines; the public is not being served by this process."\textsuperscript{53} Unemployed workers of Braniff and twelve other airlines have applied for economic relief under the special provisions of the Airline Deregulation Act of 1978, alleging that airline deregulation is the cause of widespread industry unemployment.\textsuperscript{54} The CAB reports that since December of 1979 more than 40,000 full time airline employees have lost their jobs.\textsuperscript{55} At least one commentator has described the promulgation of the Airline Deregulation Act of 1978 as perhaps "the worst disaster in history for the U.S. airline industry."\textsuperscript{56} Another suggests that "some common-sense approach should be figured out that would prevent deregulation from becoming, in effect, a hunting license that enables established companies to pick off the competition. . . . [A]n untrammeled free market is not necessarily synonymous with the public interest."\textsuperscript{57}

\textsuperscript{49} Braniff: First to Fail?, Denver Post, June, 1982.
\textsuperscript{50} The Worst Year for U.S. Airlines, Time, Feb. 22, 1982, at 46; Sing, Braniff Fail Worries Boeing, Denver Post, May 18, 1982, at 1F.
\textsuperscript{52} Gibney, Continuing Airline Losses Predicted, Denver Post, June 21, 1982, at 3C, col. 1.
\textsuperscript{53} Braniff's Chief Executive Officer, Howard Putnam, noted: I think within five to seven years you will have no more than five [out of a current eleven] trunk airlines. Then you will have a whole bunch of Southwest Airlines-type carriers that start up from scratch and work to keep costs in line. As decreed by the law of the jungle, only the strong will survive.
\textsuperscript{54} Martindale, The Economy Gets An OK for Takeoff, OAG FREQUENT FLYER, July 1983, at 38, 39.
\textsuperscript{56} Holsendorf, Act to Help Jobless in Industry, Denver Post, May 18, 1982, at F1.
\textsuperscript{57} Davis, The Great Airline Disaster, Denver Post, Feb. 7, 1982, at 1D.
Since enactment of the Motor Carrier Act of 1980, several hundred motor carriers have gone bankrupt, out of business, or have otherwise discontinued operations.\textsuperscript{58} Dun and Bradstreet reported that almost 400 motor carriers declared bankruptcy during 1980 alone, more than twice the number of the preceding year.\textsuperscript{59} These figures represent only a small percentage of trucking companies which have actually gone out of business, for many have closed their doors without declaring formal bankruptcy.\textsuperscript{60} Carriers which have gone "belly up" accounted for more than $3.2 billion in annual revenues and 65,000 jobs.\textsuperscript{61} Among the established top-100 carriers which have "bitten the dust" of insolvency are Cooper-Jarrett, Eazor Express, Gordon Transport, Hemingway Transport, Johnson Motor Lines, Jones Motor Co., Motor Freight Express, Spector-Red Ball, T.I.M.E.-D.C., and Wilson Freight Co.\textsuperscript{62} Many additional carriers would likely join the ranks of the formally bankrupt were it not for well intentioned (but poorly conceived) legislation promulgated in 1980 which radically increased carrier liability for withdrawal from or termination of ERISA multiemployer pension plans.\textsuperscript{63}

\textsuperscript{58} American Trucking Ass'n., TRUCKLINE, Dec. 15, 1982, at 1.
\textsuperscript{59} Maynard, Trucks Losing Fiscal Race, Atlanta Const., Nov. 20, 1981.
\textsuperscript{60} The High Toll of Quitting the Trucking Business, NEWSWEEK, Nov. 23, 1982, at 53.
\textsuperscript{61} American Trucking Ass'n., TRUCKLINE, Dec. 15, 1982; Lewis, Edited Account of Enforcement Conference Released by ICC, TRAFFIC WORLD, Dec. 27, 1982, at 13. Motor carriers accounting for 16% of industry revenues have gone bankrupt since deregulation was inaugurated. Dr. Irwin H. Silberman has predicted that carriers accounting for another 28% of revenues are also candidates for bankruptcy. Oversight Hearings on the Implementation of the Motor Carrier Act of 1980 (P.L. No. 96-296) Before the Subcomm. on Surface Transportation of the Senate Comm. on Commerce, Science and Transportation, 98th Cong., 1st Sess. (Sept. 21, 1983) (statement of Irwin H. Silberman). In 1976, the revenue market share of the 10 largest motor carriers was 37.9%. As deregulation was intensified, that percentage steadily grew, so that by 1982, these carriers accounted for 48.5% of industry revenues. \textit{id}.

Two large carriers have recently been added to these impressive obituaries. Maislin Transport (with annual revenues of some $200 million) and IML Motor Freight (with revenues of $100 million) have entered Chapter 11 proceedings. One of the major leaders of independent owner operators has predicted that an additional 25 to 50% of such carriers will likely go bankrupt if the Surface Transportation Act of 1982 is not modified. Siegel, ICC Paves Road to Ruin for Truckers, Wall St. J., Oct. 6, 1983, at 26. Additionally, he has suggested that we "get rid of those 'free market freaks' that remain at the ICC and get back to responsible regulation." \textit{id}.

\textsuperscript{63} The Employee Retirement Income Security Act was promulgated in 1974. Pub. L. No. 93-406, 88 Stat. 437 (1974). The 1980 Amendments to the Multi-Employer Pension Plans, by imposing extraordinary termination or withdrawal liability upon regulated motor carriers, have (a) effectively prevented motor carriers from leaving the industry, (b) deterred carriers from buying or selling their assets, (c) deterred carriers from relocating their industries, and (d) deterred lenders
Moreover, the number of independent truckers has dwindled from 300,000 in the late 1970's, to just 100,000 today. Many of the nation's remaining independent truckers, who initially welcomed deregulation, are now having second thoughts, and are calling for a reintroduction of responsible regulation.

De facto deregulation of the motor carrier industry began with the liberalized approach of the Interstate Commerce Commission in 1977 and 1978, when the ICC began issuing operating authority more broadly defined, from a commodity and territorial perspective, than ever before. The nation's economic recession did not begin until 1979. Yet, every leading economic indicator shows that the industry has progressively suffered virtually every year since 1977. For example, return on equity for motor carriers was cut in half from 15.27% in 1977, to 7.51% in 1981. For the first nine months of last year, it was merely 3.88%. In contrast, the return on equity for all manufacturers was 14.5% in 1977, rose to 16.45% in 1978, and

from loaning money to motor carriers. H. Aitken, ERISA and MPPAA: The Effects of Withdrawal Liability On Motor Carriers (July 29, 1983) (address before the 16th Annual Transportation Law Institute at Copper Mountain, Colo.) For example, the sale of T.I.M.E. - D.C. to East Texas Motor Freight Line, Inc., was prevented because the former's withdrawal liability was estimated to be $30 million. Id. The net effect of the 1980 amendments is that many carriers, effectively precluded from selling, buying, moving or going out of business, are cannibalizing their assets.


65. The leader of one association of such truckers noted that "[a] first, a lot of independents thought deregulation looked like the land of opportunity . . . now it looks like annihilation." Id. A prominent California attorney summarized the problem in these terms:

Presently, the compensation being paid to a large percentage of the owner-drivers is insufficient to permit them to properly conduct their operations or continue in business. An owner-driver's typical long line compensation today is 74 to 82 cents a loaded mile, and 50 to 60 cents for deadheading, when performed at the request of the authorized carrier. A low, but a compensation that will permit an owner-driver to barely survive, should be about 85 to 92 cents per loaded mile for a west coast operation, and 95 cents to $1.05 per loaded mile for a transcontinental service. To survive at the lower existing rates, an owner-driver is compelled to violate speed laws, hours of service, and driving regulations, and to cover these violations, he must keep a minimum of two log books. He cannot afford to properly maintain his equipment or suffer any downtime while so doing, for the vehicle must be operated to generate an income and he must forego necessary safety measures. Excessive highway speeds are required, such as a recent traffic violation, reported to me, of an owner-driver who received a ticket while driving his 75,000 pound loaded tractor and trailer across Nevada at a speed of 107 miles per hour. When these operators must replace an engine or a wornout vehicle, it will be their demise, for they are not receiving adequate compensation to recover replacement costs or depreciation and, in fact, are living on their depreciation. Because the equipment dealers have repossessed so many units of the owner-driver, these drivers find it is very difficult to obtain credit and must pay premium prices for the equipment they do purchase. And, if these problems do not finish off such an operator, the approximately $2,000 per year tax increase that will be imposed upon them by the recently passed Surface Transportation Act should do it. The loss of a large percentage of these owner-operators under the present conditions is inevitable and predictable, and there will be a resulting reduction of available truckload service to the shipping public.

D. Baker, supra note 19, at 9-10.
fell to 13.54% in 1981 — a much less steep dive than that experienced by the motor carrier industry.\textsuperscript{66} The motor carrier industry today enjoys the lowest profit margin of all major American industries, with the exception of iron and steel.\textsuperscript{67} The operating ratio of motor carriers (defined as total carrier operating expenses divided by gross freight revenues) grew from 94.76% in 1977 to 98.29% in 1982.\textsuperscript{68} Carrier debt has risen significantly during this period. The debt to equity ratio rose steadily until 1981, from 55% in 1977 to 77% in 1980.\textsuperscript{69} Interest as a percentage of carrier income grew from 15% in 1977 to 70% for the first nine months of 1982.\textsuperscript{70} Curiously, these trends parallel the issuance of operating authority by the ICC. In 1977, 16,606 common carriers held certificates of public convenience and necessity; by 1982, 24,037 carriers had been issued operating authority.\textsuperscript{71} 1982 has been described as the "worst year in history for the I.C.C. regulated motor carriers. The previous low point was in 1960 when the industry achieved an operating ratio of 97.48 — approximately one point better than at present — and a profit margin of 0.83% — 66% better than at present."\textsuperscript{72} The ICC reports that during 1982, net income for the nation's top-100 carriers fell 78% to $64.3 million, and the rate of return on shareholder's equity fell to a paltry 2.9%.\textsuperscript{73}

Net carrier income has fallen 42% since the promulgation of the Motor Carrier Act of 1980.\textsuperscript{74} The Atlanta Constitution noted that the nation's "$48 billion regulated trucking industry is in the midst of a major shakeout, the dimensions of which are unprecedented, and thus, unpredictable."\textsuperscript{75} The Wall Street Journal reported that: "A bankruptcy epidemic is sweeping American business, and there is no letup in sight. . . . Transportation deregulation is contributing mightily to the failure rate."\textsuperscript{76} Forbes characterized the contemporary economic demise in transportation as a "cruel restructuring."\textsuperscript{77}

As was noted in Dun's Business Review:

\textsuperscript{67} Id. at 2.
\textsuperscript{68} Id. at 3, 4.
\textsuperscript{69} In 1981, the carriers enjoyed a one-time tax write-off which reduced the ratio to 60%. Id. at 6.
\textsuperscript{70} Id. at 6.
\textsuperscript{71} Id. at 9.
\textsuperscript{72} Id. at 3.
\textsuperscript{73} Interstate Commerce Comm'n, Press Release (Apr. 11, 1983).
\textsuperscript{74} Rosenak, Address Before the Motor Carrier Lawyers' Ass'n, Washington, D.C. (Jan. 8, 1983).
\textsuperscript{75} Maynard, Trucks Losing Fiscal Race, Atlanta Const., Nov. 20, 1981.
\textsuperscript{76} Petzinger, Jr., Business Failures Hit Post-Depression High, Tide Expected to Swell, Wall St. J., May 24, 1982, at 1.
\textsuperscript{77} Frank, Airlines, ForbEs, Jan. 4, 1982, at 198.
After nearly two years of deregulation under the 1980 Motor Carrier Act, the trucking industry is in turmoil. Following the pattern set by the airlines, competition among truckers has intensified to an unprecedented degree, new carriers have been entering the business at a record rate, and fierce price wars have erupted. Heavy losses have already forced a number of trucking firms into bankruptcy—the beginning of what is expected to be a severe industry shakeout.78

Why is the industry unhealthy? Proponents of deregulation point to poor management, rising fuel prices and the recession, arguing that deregulation did not contribute appreciably to the current industry crisis.79 Melvin Brenner, a former vice president for TWA and American Airlines, has responded to these allegations as follows:

1. The slide of airline earnings started at the very time that deregulation became a fact (i.e., 4th quarter of 1978), and that preceded by many months the jump in fuel prices and the recession.

2. This industry previously experienced the impact of a steep jump in fuel prices plus a recession in the mid-1970s, following the Arab oil embargo. But there was not then the special element of deregulation, and the airlines came through with only a brief, limited financial setback.

3. Granting that Braniff’s problem can partly be blamed on its own in-temperate over-expansion, the same charge cannot be leveled at the many other airlines which are also in deep financial trouble.

Airline economics have much in common with the traditional "public utility," for which it has long been recognized that the public is best served with some containment of normal marketplace forces. That is why regulation was adopted in the first place. That is why every other country in the world still regulates its air transport system. And that is why a Canadian parliamentary committee has just completed a review of the U.S. experience with deregulation, and concluded that Canada should not abandon regulation.80


79. Shifrin, Adams, Kahn Clash on Hill on Air Policy, Wash. Post, Dec. 10, 1981, at D16. The Civil Aeronautics Board has argued that the principal causes of growing unemployment in the airline industry are (a) the general state of the economy, (b) fuel price increases, (c) interest expenditure increases, (d) airline income decreases, (e) fleet reequipping with more fuel efficient and larger aircraft, (f) the grounding of DC-10s, and (g) the Professional Air Traffic Controllers Organization strike in 1981. CAB Plans Employee Reduction Hearings, Av. Week & Space Tech., May 9, 1983, at 33.

80. Brenner, Airline Deregulation Is Clipping Carrier’s Wings, Wall St. J., May 24, 1982, at 21. Professor Frederick Thayer summarized some of the problems of airline deregulation in these terms:

The advocates of deregulation, including most of the major media, pointed to discount fares as evidence of success, resolutely ignoring financial losses and extremely high fares on non-vacation routes. They even refused to acknowledge the new form of cross subsidy; to some extent, business travelers were covering the costs of tourist travelers, a cross-subsidy less justifiable than any other.

The basic problem remains as simple as ever. The airlines, whatever their initial
If indeed high fuel prices and the recession are the principal causes of the industry’s woes, then certainly the current economic upswing and the degeneration of OPEC will save the day.\(^8\) For every penny by which the price of aviation fuel falls, United Airlines alone saves $14 billion.\(^9\) A 10% reduction in the price of aviation fuel will save the industry a hefty $1 billion.\(^\) But one suspects that this is only a part of the story.

The industry’s principal problem is excessive rate wars.\(^\) Deregulation of entry brought a host of new entrants to many heretofore healthy markets.\(^\) By January of 1983, 49,726 new certificates for motor carrier operating authority had been granted by the ICC; this included certification

image as luxury travel for the pampered rich, are as much a public utility as a city bus company, and must be rearranged into a coordinated system which somehow abolishes head-to-head competition. Americans, unfortunately, are very slow to learn.

Thayer, supra note 35, at 227, 230.

Proponents of deregulation often blame the failures of deregulation on the recession and fuel prices. While this reasoning seems plausible on the surface, the facts tell a much different story.

Passenger traffic was actually up in 1982, the most severe year of the recession. But during 1982, the airline industry lost nearly $1 billion. According to Daniel May, president and CEO of Republic Airlines, revenue passenger miles for the twelve-month period preceding October 1982 were 16 percent higher than the twelve-month period preceding the passage of the Deregulation Act. Clearly, the recession is not the only culprit.

The airline industry suffered from the fuel price increases following the Iranian Revolution and the Iran-Iraqi war. But over the two-year period from May 1981 to April 1983, the price of fuel dropped 17.2 cents, saving the industry $1.51 billion. Unfortunately, those savings did not show up on the balance sheet of the embattled airlines; they were all sunk into debilitating fare wars.

A brief look at history shows that from 1973 to 1976, a similar four-year period with an oil price shock and a major recession, the airline industry had net income of more than $1 billion for the four years.

82. The Unrigging of Oil Prices, NEWSWEEK, Mar. 7, 1983, at 64.
84. See Deregulation Breeds an East Coast Air War, BUS. WK., Jan. 26, 1981, at 30; The Worst Year for U.S. Airlines, TIME, Feb. 22, 1982, at 46. Julius Maldris, vice president of Salomon Brothers, predicts that airline rate wars will continue to plague the industry for three reasons: (1) new airlines’ start-up costs are two-thirds lower than those of established carriers; (2) although 93 new aircraft will be delivered during 1983, old planes are generally not being retired; and (3) airline travel agents have been deregulated. Banker Claims Air Fare Wars Will Continue, J. of Com., May 18, 1983, at A2.

Some analysts maintain that no matter what the economy does, no matter how healthy some airlines grow, fare wars are a certainty. As long as some carriers need cash to meet interest payments and payrolls, and as long as upstarts continue to claim their niches in the marketplace, somebody will always be willing to slash prices.

Before the year is out, the stronger airlines could decide to end the bloodletting once and for all by starting fare wars designed to force weaker trunks and entrants out of the marketplace forever. That could bring about one more year of deeply discounted air travel, then a long period of the kind of “price stability” the airlines want so badly.

of 13,806 new carriers. Similarly, more than thirty new air carriers have entered the airline industry. Since transportation is an industry inherently vulnerable to overcapacity, (for an empty seat or a partially filled trailer is an instantly perishable commodity) unconstrained entry must necessarily lead to distress-sale pricing in those markets in which competition is excessive. Thus, motor carriers filed more than 115,000 independent rate ac-


These new air carriers are responsible for less than five percent of market. Martindale, Victims of History, OAG FREQUENT FLYER, Dec. 1983, at 49, 50. Indeed, the Air Transport Association estimates that the new carriers are responsible for only 2.4 percent of the total traffic. Salpukis, Airlines Adapt to Decontrol, N.Y. Times, Dec. 8, 1983, at D1. Former CAB Chairman Alfred Kahn predicts that their market share will never likely exceed "5% of the total travel." Richards, CAB's Ex-Chairman, Alfred Kahn, Looks At Airline Industry He Helped Deregulate, Wall St. J., Oct. 4, 1983, at 35.

88. As former CAB Chairman Secor Browne has noted, the principal reason for deteriorating profits is that "although, like other unregulated industries, airlines suffer from recession and inflation, there has been destructive price competition, and overcapacity — that is, too many seats are chasing too few bottoms." Brenner, Reconlact Air Fares, N.Y. Times, Apr. 14, 1982, at 16. See also Rowen, Airlines: Competing to the Death, Wash. Post, Nov. 11, 1982, at A29.

Professor Frederick Thayer portrays the overcapacity problem under deregulation as follows:

The basic case is easily made for price and capacity regulation of public transportation systems. Suppose, for example, I wish to fly from New York to Los Angeles. Traditionally, three major airlines have offered me seats on flights scheduled in close proximity to meet peak travel demand. In Milton Friedman’s already classic phrase, I was “free to choose” one of the three, thereby leaving the other two with empty seats. The 1978 U.S. policy of deregulation encouraged four additional airlines to offer service on the same route. I now have greater “freedom to choose” (seven alternatives), but the result is six empty seats. This problem is inherent to any transportation system organized to provide “head to head” competition, because the service being offered cannot be held in inventory awaiting other customers; service is destroyed by competition itself. It follows that the greater the direct airline competition, the greater the number of empty seats, the more fuel wasted in moving them about, and the higher the cost per passenger actually moved.

There is no way to deal with the empty seat problem except by limiting the capacity (flight frequency) on any single route. In principle, the problem can be minimized only by eliminating direct competition altogether. If a transportation system is to be so operated, a case can be made for public supervision of safety and prices. This is the classic outline of any industry defined as a public utility.
tions with the ICC during 1981, and more than 180,000 during 1982.\textsuperscript{89} The proliferation of discount airline fares has undoubtedly driven many travel agents to seek psychiatric assistance.

\section*{B. Declining Safety}

Serious questions arise as to whether an unhealthy industry can be a safe industry.\textsuperscript{90} One of the dangers of poor or nonexistent profits for an industry such as transportation is the natural tendency of management to curtail costs; among those which can be significantly diminished are maintenance costs, including mechanic’s wages, spare or replacement parts, and idle vehicle time lost during inspection and maintenance.\textsuperscript{91} Unsatisfactory profits in the rail industry led it to defer maintenance on equipment and trackage, leading in turn, to a repeated series of derailments, often causing loss of human life.\textsuperscript{92} One of the nation’s major air carriers was repeatedly

\begin{quote}
Thayer, supra note 35, at 211.

Available seat miles, one measure of capacity, for example, actually increased from 425 billion in 1981 to 439 billion in 1982.

In an effort to fill those empty seats the industry resorted to heavy discounting. The number of passengers who traveled on discount fares soared from 57 percent in 1980 to 78 percent in 1982. During the first six months of this year that percentage rose to 85.

The analysts and executives agree, however, that deregulation did accelerate the trend toward discount fares. As new carriers began flying in key markets across the country, their main strategy for attracting customers was lower fares. And the result was often bitter fare wars.

Salpukis, \textit{Airlines Adapt to Decontrol}, N.Y. Times, Dec. 8, 1983, at D1. The overcapacity in the airline industry has been studied by Merrill Lynch, which concluded that by the end of 1982, the world fleet consisted of 6,100 transports, of which 900 would not be needed if the aircraft were operated at a 65\% load factor and full utilization. \textit{Conference Foresees Airline Struggles}, AV. WEEK & SPACE TECH., Sept. 26, 1983, at 44.

\textsuperscript{89} ICC Chairman Tells Senate Panel He Favors Early Sunset of Agency, \textit{Traffic World}, Dec. 20, 1982, at 27, 64. The ICC in Ex Parte No. MC-165 also recently exempted contract carriers from the tariff filing requirements of the Interstate Commerce Act. This decision was appealed to the D.C. Circuit Court of Appeals on June 13, 1983; as of the date of this writing, the appeal is still pending.

\textsuperscript{90} One of America’s major daily newspapers discussed the issue in these terms: [T]his is a dangerous time for the airline industry.

Airlines have been pulled apart by deregulation and cut-throat fares, by high fuel costs and low passenger loads. The new pressures have punished the carriers, which lost more than \$1 billion in the last three years. And they are still hampered by an unfinished air traffic control system, because half of its 14,000 controllers aren’t fully qualified.

The airlines and the regulators have to recognize these stresses. They should be aware that these increases increase the risk of human error and mechanical error. . . . For the airlines today, maximum safety requires maximum regulation.

\textit{Safe Skies Require Strict Regulation}, USA Today, May 12, 1983, at 10A.

\textsuperscript{91} Columnist Hobart Rowen characterizes the problem in these terms.

An articulate and well-informed minority understands that the free-market issue is a phony when it comes to deregulation of transportation. Unless somebody cuts corners on services, or safety, deregulation doesn’t lower prices, overall, to the consumer.


\textsuperscript{92} Professor Golbe’s study established that profitable railroads have fewer accidents per mile
cited by the FAA for safety violations prior to its bankruptcy.93

Twenty-six percent of the nation’s airline fleet is already obsolete, and there will be a major need to reequip during the next decade.94 The cost of a moderate size jet is $20 million.95 Without investor confidence, the airlines cannot finance the aircraft they need.96 Although many existing aircraft are obsolete and should be replaced, since the enactment of the Airline Deregulation Act of 1978, cancellations for newly ordered aircraft have grown more than 300%.97 Professor Frederick Thayer of the University of Pittsburgh reminds us that "safety always has suffered when airlines were largely unregulated."98 Indeed, he notes that "deregulation is both inefficient and dangerous."99 It "threatens to give us the worst of all worlds, a combination of many exorbitant fares (to cover empty seats) and a decline in safety."100


95. Julius Malditis, Jr., Vice-President of Salomon Brothers, estimates that 524 of the 2,005 planes operated by the nation’s top 12 carriers are obsolete. Id.


98. Air Line Pilots Ass’n, Press Release (June 15, 1983). Testifying before the House Subcommittee on Aviation, ALPA President Henry A. Duffy remarked, "‘Economics and safety cannot be separated.’ Under regulation, ‘[a]n additional margin of safety [was established] by exceeding, not just meeting Federal Aviation Administration minimums.’ But under deregulation, the airline industry ‘has consistently degenerated to the point of acute anemia.’" Duffy noted that there are certain industries, such as aviation, "where the pressures of the marketplace and the spirit of free competition are at cross purposes with the national interest.” Id.

99. Thayer, The Lowest Fare is Not the Safest, Wash. Post, May 1, 1982, at A21. "Aviation has had a long-established axiom, dating back to the days when 'barnstormers' often slept under their aircraft wings, that the first thing to go when cost cutting begins is some maintenance — and consequently some safety." Reiss, Airline Cost Cutting Has Bearing On Safety, Too, Youngstown Vindicator, June 26, 1983, at B-14.


The eroding federal role in protecting passenger safety has been described as follows:

FAA’s safety function has been affected in a very direct and visible way by deregulation. Because of the growing number of carriers, general aviation inspectors are being used to monitor commercial air carriers. This problem is compounded by the fact that the Civil Aeronautics Board (CAB) is using only a rubber-stamp safety-fitness test for new entrants. CAB is relying on FAA to catch the board’s mistakes, and FAA is strapped for manpower.

The pressure of record losses will not go away. Every airline manager is faced with cost/benefit determinations that must be made in the pressure-cooker atmosphere of an industry dominated by news of bankruptcies, real and threatened.

Orders for new, safer, more efficient aircraft are canceled. And the airlines continue to fly old and tired aircraft that should be replaced.

Duffy, Deregulation 5 Years Later, OAG FREQUENT FLYER, Oct. 1983, at 54, 56. Similar concerns were raised in an editorial appearing in the Washington Post:
Professor Daryl Wyckoff of Harvard University argues that there is a

Budget cuts have reduced the number of FAA safety inspectors by one-fourth. These are the federal employees who monitor the airlines’ maintenance and cockpit procedures for safety problems.

Before deregulation, many airline officials and others argued that deregulating prices, routes and entry into the industry would encourage airlines to let cost competition spill over into safety areas. The federal safety agencies, it was said, would not be able to fight effectively the tide of economic incentives unleashed by competition. Airline officials insist, as you might expect, that they don’t cut corners on safety. But which are we to believe: the predictions of danger made years ago or the reassurances offered today?

The statistics show that airline accidents have been declining for years. On that there is no argument. The harder question is whether the combination of several current trends might not lead to serious problems in the longer run. Those trends include the FAA budget cuts, the economic pressure on airline wages and operating costs and the increasing technical complexity of the equipment itself.


Among the instances when the FAA has discovered safety violations involve (a) Air Pennsylvania, which shut itself down on March 5, 1983, before the agency could impose $18,000 in fines for more than 30 safety violations; (b) Aeromenica, which was grounded in 1982 for operating unsafe aircraft; (c) Guy-America Airlines, which was fined $50,000 on February 17, 1983, for various safety violations. “If any link can be established between financial distress and safety degradation, the bottom 100 constantly recycling commuter carriers referenced above certainly look like prime examples of this relationship.” Review of Airline Deregulation and Sunset of the Civil Aeronautics Board (The State of the Airline Industry Under Deregulation), Hearings Before the Subcomm. on Aviation of the House Comm. on Public Works and Transportation, 98th Cong., 1st Sess. 512 (1983) (statement of Henry A. Dufty, President, Air Line Pilots Ass’n, Int’l). However, the FAA seems to have a reputation of imposing sanctions against only the grossest and most conspicuous of violators. Although aircraft having nine or fewer passengers have a 20 times greater accident rate than those carrying 30 or more passengers, the FAA has been accused of diluting the safety standards for such commuter aircraft. FAA Bends Rules, Says ALPA, FLIGHT Int’L, Nov. 26, 1983, at 1409. Congressman Elliott H. Levitas (D.-Ga.) has expressed serious reservations over the performance of the agency:

I’m disappointed in the dismal record of the FAA in regulating aircraft safety. Legislative action will have to be taken unless the agency acts soon. But, I’m afraid, its too little and too late now.

Quotelines, USA Today, Nov. 3, 1983, at 8A. Other recent concerns have been expressed as a result of the allegedly poor piloting and maintenance procedures of Air Illinois:

The discoveries have heightened concerns about the safety of some financially weak, inexperienced regional airlines that have been assuming a larger role in the nation’s passenger service since Congress approved airline deregulation in 1978.

The trend toward small regional airlines taking over routes once flown by major carriers is continuing at the same time that the Federal Aviation Administration, which regulates airline safety, is reducing the number of its inspectors as a result of the administration’s budget-cutting efforts.

Major trunk airlines, dropping unprofitable routes, no longer serve 166 American cities. Those cities still have passenger service, however, provided by small carriers, usually flying propeller planes.

definite correlation between motor carrier regulation and safety.\textsuperscript{101} His study noted that regulated carriers have a safety and compliance record significantly superior to that of unregulated motor carriers.\textsuperscript{102} These findings confirm those in an independent study commissioned by the Department of Transportation which also concluded that unregulated carriers are less safe than regulated carriers.\textsuperscript{103} In recent years more than 10,000 highway deaths have resulted from accidents involving medium and heavy commercial vehicles. Such accident fatalities are growing at twice the rate of increased truck miles traveled.\textsuperscript{104}

A less healthy industry will likely introduce the public to more intriguing aspects of aircraft maintenance than American Airlines' engine pylons, Air Florida's wing de-icing, Frontier's landing gear, Air Canada's flammable interiors, or Eastern's oil plugs, rings and gaskets.\textsuperscript{105} Must we wait until a school bus full of children is obliterated by an out-of-control semi, with faulty brakes and bald tires, before our public officials recognize that an unhealthy industry is likely to be an unsafe industry?

\textbf{C. PRICING DISCRIMINATION}

Professors Wagner and Dean predicted that deregulation would have the following effects:

\begin{itemize}
\item Pricing could become increasingly unstable if regulations were lessened.
\item Regulation sometimes is credited with ensuring nonpredatory pricing. It is thought that minimum rates provided under a regulated environment prevent or seriously limit a carrier from pricing under cost and, correspondingly, forcing competition out of the marketplace or reducing service levels. Moreover, regulation may better provide for rate equity for various shipper groups among commodities and between geographical regions. It can reduce discrimination.
\end{itemize}


\textsuperscript{102} The inescapable conclusion is that an airline cannot spend money it doesn't have to maintain and improve its safety equipment and procedures. In other words, the economic chaos brought on by deregulation will, sooner or later, erode the safety of our commercial air transportation system.


\textsuperscript{105} Id.

\textsuperscript{106} Id.
Additionally, it may provide a means by which price-gouging can be controlled better.\textsuperscript{106}

Prior to deregulation, there was some measure of cross-subsidization within the transportation industry. While carriers were allowed to serve specified lucrative routes, they were also required to serve geographically related less lucrative or marginal markets as well. Carriers were expected to internally cross-subsidize losses or meager profits in their small community service with their healthier earnings in lucrative markets, and to provide just and reasonable rates to both. Deregulation was designed to end such cross-subsidization.

Actually, cross-subsidization seems merely to have been reversed in direction, rather than eliminated. Today, carriers extract higher rates from small communities to cross-subsidize the losses they are suffering as a result of the intensive competitive battles they are waging for market dominance between larger communities.\textsuperscript{107} Radically intensified entry, coupled with effectively deregulated ratemaking have made it possible for carriers to charge predatory rates in competitive markets (or to large shippers), and cross-subsidize such losses with excessive, discriminatory rates in oligopoly markets (or to small shippers).

While prices have become lower for large shippers or in densely traveled corridors, prices have risen substantially in less competitive markets.\textsuperscript{108} As an example, transcontinental air fares recently fell to $99, one


\textsuperscript{107} See Rowen, Airlines: Competing to the Death, Wash. Post, Nov. 11, 1982, at A27.

\textsuperscript{108} Fares Fair?, TRANSPORT TOPICS, May 24, 1982, at 18.

Senator Mark Andrews (R.-N.D.) noted that "since deregulation air fares across the country have gone up 112 percent. The consumer price index went up 46 percent during the same period." Transcript of CBS News Face the Nation, Oct. 2, 1983, at 12. Hence, the aggregate impact of fare changes since deregulation has been a higher increase than that of the rest of the economy.

Long haul flyers may get cheap fares because of excess competition but shorter hauls cost more and some cities have lost service altogether.

What this adds up to in the end is a greater tendency for higher fares overall for everyone — business and leisure travelers.

\textbf{Seybold, Airline Deregulation — Is It Good or Bad?}, Boston Sunday Globe, Nov. 6, 1983, at T-1.

One traveler described the problems of discrimination he encountered in air service as follows:

I recently had to make an emergency flight to Indianapolis from Los Angeles. Would you believe that the cheapest fare was $369 each way while, at the same time, you could fly all the way to the East Coast from Los Angeles for anywhere from $149 to $160 each way?

According to my atlas (and my calculator) this means that the flight to Indianapolis and back cost me about 230\% of the Los Angeles-to New York City fare even though, on a round-trip basis, I covered 26\% less distance. I call this either gouging, or your typical East Coast/West Coast bias against mid-America. To add insult to injury, of course, there is no way in the world you can fly directly to Indianapolis from Los Angeles. The
way. You may remember that World Airways begged the Civil Aeronautics Board to put an end to predatory pricing in that market. World argued that its $142 fare was not compensatory, even though it was among the most cost effective carriers in the industry. To World's pleas, the CAB turned a deaf ear.

Although a one way transcontinental air passenger ticket recently cost $99, a flight between Washington and Omaha cost $287. Flights between Seattle and Orlando cost $326 round trip while round trip transportation between Seattle and Phoenix costs $437. US Air charged its passengers $24 more between Buffalo and Albany than if they remained on the same plane and flew the 100 additional miles to Boston; the carrier was free to impose a premium rate between Buffalo and Albany because it has no competition in that market.

Recently, it cost $77 to fly between New York and Miami, but $168 to fly 500 fewer miles, between New York and Myrtle Beach, SC. TWA charged $201, or 29¢ a mile, between Peoria and Wichita; American charged $255, or 23¢ a mile, between Lubbock and Dayton. Compare these rates with those charged in competitive markets, such as the $90 charged by American, or 10¢ a mile, between Chicago and Dallas, or the TWA rates of $129, or 6¢ a mile, between Chicago and San Francisco. Since deregulation, air passenger fares between points in California have doubled, on the average. Air fares have increased 116.6 percent in small and medium sized communities since deregulation, while average

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airlines' idea of "direct" is to cool your heels for a couple of hours somewhere along the way — in either Chicago, St. Louis or Louisville.

I know that the airlines are in trouble, and it seems to me that this blatant price discrimination in favor of West Coast/East Coast traffic is symptomatic of the shortsightedness that is wrecking the industry — and it couldn't happen to a nicer bunch of folks.


[In July 1980, a citizen of Tulsa, Okla., paid $230 to fly to Los Angeles, or 18 cents a mile, while fare wars enabled a New Yorker to fly to Los Angeles for $99, or 4 cents a mile. Today the Tulsa passenger pays $279 to go to Los Angeles while the New Yorker pays $179.]


116. W. Augello, *The Deregulation Disaster* (unpublished monograph, 1983). Ironically, it was the experience of California and Texas intrastate carriers to maintain scheduled service at rates significantly below those of their federally regulated interstate counterparts which was emphasized by deregulators to support federal deregulation of air carriage. See Kahn, *Applying Economics to
U.S. fares have increased only 48% during the same period. This "twilight world of airline economics" is beginning to be described by consumers as "outrageous," "unfair," "chaotic" and "nightmarish." In the absence of regulation, less competition almost always means higher fares. When Sir Freddie Laker's airline went bankrupt, transatlantic fares were increased sharply by the surviving carriers. When Braniff went bankrupt, American and Delta raised fares dramatically in markets radiating from Dallas (Braniff's former hub). When Continental abandoned and TWA reduced service in the Chicago-Los Angeles market recently, United and American raised fares sharply. Hence, whatever benefit some communities now enjoy in terms of air fare bargains may "disappear once competition is extinguished." The business traveler pays several times the rate of the individual seated next to him, and both enjoy less leg room. Flights are cancelled or chronically overbooked, schedules are changed, and routes are obliterate.


117. DOT's View of Airline Deregulation Challenged by Small Cities, Labor, TRAFFIC WORLD, June 20, 1983, at 16. Richard B. Keinz, assistant commissioner of the aeronautical division of the Minnesota Department of Transportation, also testified before a subcommittee of the House Public Works Committee that:

It is clear that the objectives of Congress are not being met for many cities and isolated areas. The experience of many cities since the enactment of the Airline Deregulation Act has been a vicious cycle in declining traffic, declining service and rising fares. In part this has been due to a weak economy which has affected these cities and the airlines serving them. To a great extent, however, it has been the result of deregulation.

Id.

118. _Airlines Move to Straighten Out Air Fares_, U.S. NEWS & WORLD REP., May 16, 1983, at 49. One major newspaper recently published an editorial which described the nation's airline industry as in a "state of crisis," with the result that major carriers are undergoing bankruptcy and reorganization as the "Darwinian process" reaches "full throttle." The editorial goes on to call for "an immediate federal review of the growing airline dilemma before it does indeed balloon into a crisis of national proportion." The Airlines' Patchwork Crisis, Seattle Post-Intelligencer, Oct. 2, 1983, at A30.

Inconsistent, unreliable, erratic service at prices which vary monthly from ridiculously low to prohibitively high is hardly in the public interest. Neither the business nor the pleasure traveler finds a hint of health in the current air passenger transportation scheme created by Mr. Kahn.


120. _Airlines_, FORBES, Jan. 5, 1981, at 144.


122. A number of major American corporations have grown increasingly dissatisfied with the inconvenience and cost of commercial air service, and have responded by purchasing their own aircraft:

Commercial trips often involve delays while waiting for flights, switching planes or traveling from airports located far from city centers. And the costs rise if employees are forced to stay overnight because air service is limited.
Motor carrier competition for the traffic of large shippers or densely traveled markets has created a phenomenon which Distribution magazine labels "The Great Trucking Wars." Regional discounting and large shipper discounting has become very pronounced in the trucking industry. One wonders whether such pricing discrimination would have been permitted in an environment of responsible economic regulation. Justice William Douglas, although a vigorous proponent of the free market, characterized the U.S. Supreme Court's position on the issue when he wrote the majority opinion in Georgia v. Pennsylvania Railroad:

Discriminatory rates are but one form of trade barriers. They may cause a blight no less serious than the spread of noxious gas over the land or the deposit of sewage in the streams. They may affect the prosperity and welfare of a State as profoundly as any diversion of waters from the rivers. They may stifle, impede, or cripple old industries and prevent the establishment of new ones. They may arrest the development of a State or put it at a decided disadvantage in competitive markets.

D. SERVICE DETERIORATION

Service to small communities has deteriorated significantly. During the first year of deregulation, 260 cities lost air service. During the first two years of deregulation, 40% of our nation's airports lost service. Two hundred communities lost 50% or more of the service, measured by seats.

Byrne, Kimberly-Clark Seeks to Turn Its Shuttle From Wisconsin to Atlanta Into An Airline, Wall St. J., July 6, 1983, at 27.
123. The U.S. Air-Fare Dogfight, NEWSWEEK, Apr. 19, 1982, at 69.
125. Id. Ernest R. Olsen noted that:

[W]e now have . . . in trucking . . . the same wild climate that existed prior to 1935. . . . Almost anyone can secure authority, charge what he wishes, and operate legally or illegally at will, with little risk of penalty. Large established carriers are getting larger; small and weak carriers are dropping out in substantial numbers. . . . LTL carriers will eventually identify the areas in which they have market monopoly and will act accordingly. Small shippers should be properly armed. . . . The small producers can forget about the railroads; they will serve only volume shippers in the future. . . . The large shipper will command added attention among truckers, with new power to demand reduced rates, as well as special deals.

they previously enjoyed. They previously enjoyed.

Over 100 communities lost all their scheduled service in just the first two years of deregulation; it had taken ten years for a comparable number of communities to lose such service prior to deregulation. Service in less populated states has eroded demonstrably since deregulation. Much of the air service which remains for small communities is provided at taxpayer expense; the federal government paid $113 million in air passenger subsidies during fiscal year 1981. Curiously, no such subsidies will be paid to ensure that small communities receive a rea-

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The fact is that the deregulation of airlines has ignored one of the fundamental precepts of any modern society, i.e., that transportation is so vital to communities and regions that its adequate maintenance cannot be left strictly to the whims of the marketplace.

The zealots who successfully lobbied for deregulation misled Congress into believing that removal of “public utility” licensing of air service would have only minor effects on the air route map. For example, the Kennedy subcommittee of the Senate was persuaded that, with deregulation, route abandonment by the major trunk carriers would affect “routes that, at the very most, account for one-half of 1 percent” of airline traffic.

The clock cannot be turned back to 1978. But this does not preclude some reasonable modification of deregulation so as to overcome its more serious defects. A first step must be a willingness to stop whitewashing this new regime and to face objectively all its consequences — the bad as well as the good.


131. See Duffy, In Wyoming, You Can’t Get There From Here, Denver Post, May 14, 1982, at 1D.

Service has declined in numerous Essential Air Service markets as well. In Kentucky, for example, available seats departing from Essential Air Service Communities have declined 61.3 percent since deregulation. In Missouri, available seats at Essential Air Service cities are down 27.6 percent and nonstop destinations have dropped from 30 to 24. And in Nebraska, departures in Essential Air Service Communities have dropped 53.9 percent since deregulation. There are numerous other examples of the loss of service.

This drop in service greatly discriminates against the individual traveler to and from small cities. Because fewer connecting flights are available to and from smaller cities, travelers are often forced to wait or take other modes of transportation, losing both time and money.

In addition, service reductions inhibit growth in those smaller communities. What business wants to locate in a city that has intermittent air service at exorbitant rates? Cutting off the air lifeline from smaller cities effectively cuts off their growth potential.


133. Chapman, Airlines Soon Will Find It Difficult to Retain Scarce Subsidy Funds, TRAFFIC World, Sept. 6, 1982, at 33. This federal subsidy program for small community service is sched-
sonable level of motor carrier service at nondiscriminatory rates, even
though 65% of America’s communities are completely dependent upon
motor carriage for freight transportation. Further, scheduled air carriers
have frequently been replaced by commuter carriers. Recent statistics in-
dicate that a passenger stands a 300% greater chance of losing his life on a
commuter carrier.

A similar result is occurring in the motor carrier industry. The Wall
Street Journal reported that intrastate deregulation in Florida cost many
small communities their scheduled bus service. Since November 1982,
one of the nation’s largest bus companies has petitioned forty-three states
for permission to eliminate service to more than 1,300 points; one of its
senior executives acknowledged that deregulation had enabled it “to cut
out 90-95% of our small towns.” Intrastate motor carrier transportation
was deregulated in Florida on July 1, 1980, principally because the two
houses of the state legislature failed to agree on a bill designed to extend its

uled to end in 1988. It is likely that deterioration of such service will further accelerate after subsidy
termination.

Binford, airport manager at Laramie, Wyoming, characterized the problems small and remote
communities have faced with commuter airlines:

We’ve had lots of airlines start up, but they don’t seem to last long. Usually an airline
is started by some furloughed pilot who mortgages his home, puts a down payment on
a plane and goes into business. But in the main, they’re undercapitalized and poorly man-
aged and don’t last.

Duffy, In Wyoming, You Can’t Get There From Here, Denver Post, May 14, 1982, at 1D.
136. Ubinas, Bus Deregulation Gains Favor, Worrying Small Towns, Small Operators and Eld-
137. Baker, supra note 19.

The tragedy is that the people who do and must ride the buses are dependent upon
and usually have no other means of obtaining transportation. They are the older, senior
citizens who no longer are economically or physically able to own or operate automobiles.
Young people and school children, who must depend upon bus transportation. Economically
disadvantaged persons, who cannot afford to own or operate automobiles. Business-
es in small cities that must have transportation available to attract and keep
employees. Persons not owning automobiles that require bus service to visit their doctors,
obtain medical services, seek employment, visit relatives or friends.

Id. at 5-6.

For Greyhound, airline deregulation has meant increased competition from new low-
cost air carriers, which have undercut bus fares on routes of 100 to 250 miles, important
runs for the bus industry. Bus deregulation has meant fare wars with Trailways Inc., Grey-
hound’s main competitor, and it raises the specter of fare wars with other competitors.
Bus deregulation also means Greyhound can raise fares and eliminate unprofitable
runs.

138. Id. Interstate deregulation of bus operations has also resulted in a deterioration of service
for small communities. See Cox, Bus Service Loss Isolates Julesburg, Denver Post, Mar. 14,
1983, at 6A.
life beyond its pre-ordained termination under sunset legislation. Florida thereby became the first state in the nation to deregulate trucking. In the year preceding deregulation, state agencies received thirty-four complaints regarding household goods transportation. But in the first month of deregulation, at least one shipper has complained of serious service deficiencies:

... I did not have [these problems] when I was dealing with reputable and reliable truck lines who had the ability to offer service on a year round basis and who operated in a professional manner. Since deregulation some of our regulated carriers have stopped offering service to some areas. Now we have to beat the bushes to cover some of our shipping points.


140. Florida deregulated intrastate transportation on July 1, 1980, as a result of the natural progression of its Sunset legislation; Maine's legislature enacted a deregulation statute which became effective on January 1, 1982; Arizona deregulated on July 1, 1982, by plebiscite. INTERSTATE COMMERCE COMM’N, DEP’T OF TRANSP., REPORT TO CONGRESS ON UNIFORM STATE REGULATIONS 106 (1982). Wisconsin enacted deregulation legislation which became effective on October 1, 1982. WIS. STAT. ANN. § 194.23 (West Supp. 1983-1984). Neither Delaware nor New Jersey have ever imposed any meaningful regulation of intrastate motor carriage. ARIZ. DEP’T OF TRANSP., INITIAL IMPACTS OF MOTOR CARRIER Deregulation in Arizona 4 (1983) [hereinafter cited as INITIAL ARIZONA IMPACTS].

Professors Freeman and Bellock have prepared surveys which analyze the perceived impact of motor carrier deregulation upon Florida and Arizona shippers, receivers and carriers for 1981 and 1982. See Freeman, Motor Carrier Deregulation in Florida: A Preliminary Analysis, 14 TRANSP. L. INST. 133 (1982); Freeman & Bellock, An Analysis of Arizona and Florida Motor Carrier Deregulation and the Implications for State Regulatory Change, 15 TRANSP. L. INST. 13 (1983) [hereinafter cited as Arizona and Florida Deregulation]. Their conclusions indicate that a large majority of Florida and Arizona shippers and receivers during this period perceived deregulation as having increased competition: since deregulation, they have experienced lower rates and improved service. Arizona and Florida Deregulation, supra, at 14-15, 18. Private carriers also supported deregulation in these two states. Id. at 15. In light of the fact that during these two years the nation suffered its most severe recession since the Great Depression, it is not surprising that the excess capacity generated by lower demand for transportation and increased entry generated by deregulation would enhance competition, lower rates and ensure an abundance of service for all shippers. Whether this will continue to be true in the long run is unclear.

Carriers were, however, less enthusiastic about the continuation of deregulation. Most agreed with the shippers’ perception that deregulation had created additional competition. A growing number of Florida carriers saw both rates and profits tumble as a result of deregulation, to the point that now a majority favor a return to a regulated environment. Id. at 16. Forty-four percent of Arizona’s carriers now favor a return to regulation, while only 37% favor continued deregulation. Id. at 18. However, a larger number of household goods carriers in both states tended to view deregulation as enhancing their ability to increase their rates and enjoy correspondingly higher profits. Id. at 16, 18. Professors Freeman and Bellock hedge their findings with the qualification that it is, as yet, too early to draw any final conclusions concerning the wisdom of intrastate deregulation. INITIAL ARIZONA IMPACTS, supra, at 3, 8.

Since deregulation in Arizona, at least three sectors of the motor carrier industry have been the subject of increased consumer complaints: household goods, taxicabs and ambulance service.
The latter assessed such outrageous charges that in November 1982, voters approved a proposition which would restore regulation of ambulance services and charges. Id. at 51.

Seventy-six percent of Wisconsin’s motor carriers opposed deregulation. Among small carriers (i.e., those with five or fewer power units), 82% opposed deregulation. One opponent characterized deregulation as follows: “All it will do is squeeze out the small guy, put a lot of junk on the road, and in a couple of years there will be no small truckers. And the big outfits will be able to charge rates you wouldn’t believe.” Among motor carriers which favored deregulation, many indicated that no regulation was preferable to the irresponsible regulatory approach which had theretofore characterized Wisconsin state government. Wisconsin Deregulation Bill Sparks Controversy, Heads for Assembly, Traffic World, Feb. 15, 1982, at 36-38. Deregulation was also opposed by Wisconsin’s largest and most influential business organization, the 2,800 member Wisconsin Association of Manufacturers and Commerce. Rix, Dreyfus Pressured to Veto Trucking Deregulation Bill, Wis. St. J., April 28, 1982.

Deregulation in Wisconsin was opposed less enthusiastically by larger carriers. Thus, only 54% of those carriers having more than 25 power units opposed deregulation, and 39% favored it. When the vote was called in the Wisconsin Assembly, the bill was heavily supported by urban legislators, and opposed by rural legislators. R. Westley, Wisconsin Motor Carrier Deregulation: Strange Bedfellows Make Politics 19 (address before the Motor Carrier Lawyers Ass’n in Washington, D.C., January, 1983). Since motor carriers have been deregulated in Wisconsin, bus lines have dropped or sharply curtailed service to many rural communities. Rix, Bus Deregulation Means Some Service Cuts, Wis. St. J., Sept. 26, 1982; Thomson, Baseline Freedom Has Fares Jumping Up and Down, Capital Times, Oct. 2, 1982, at 19; Some Bus Routes Dropped After State Deregulation, Wis. St. J., Oct. 6, 1982, at 5. One Wisconsin attorney recently summarized the deterioration of passenger service as follows:

[If I interpret the informal data I have been able to acquire] correctly it appears that Greyhound abandoned 80 Wisconsin points, virtually none of which had alternative service, and added 8 points, most of which already had some existing service. Some of the points abandoned by Greyhound were picked up by other carriers. I continue to hear rumors about other service cuts, but without the regulatory machinery it is difficult to follow these as you well know.


However, 34 states continue to impose economic regulation of motor carriage similar to that practiced by the ICC prior to the promulgation of the federal Motor Carrier Act of 1980. Arizona and Florida Deregulation, supra, at 26.

In Colorado, deregulation opponents successfully defeated sunset of the state’s Public Utilities Commission and a series of bills brought before the Transportation Committees of the state legislature seeking to deregulate various sectors of the industry.

California had been toying with various notions of diluted motor carrier regulation until the results of a state commissioned study were published in late 1981 on the effects of intrastate service and pricing of deregulating the airline industry. Federal preemption of the state’s jurisdiction under the Airline Deregulation Act of 1978 caused fares to rise between 30 and 70% during the first two years of deregulation. Many small communities lost scheduled service, to be replaced by smaller feeder lines, several of which recently entered bankruptcy. See Cal. Pub. Utils. Comm’n., Airline Deregulation in California (1981).

Recently, things seem to have turned sharply away from deregulation in California. For the first time in two decades the state PUC set two matters for oral hearing. PUC Sets Cases for Argument, CALTRUX, May 16, 1983, at 1. Further, the state Democratic party adopted Resolution 49B, calling upon the government to implement its regulatory responsibilities in a responsible manner, and condemning the imposition of transportation deregulation in an "arbitrary, haphazard, and inconsistent manner unaccompanied by reasoned arguments for its imposition."

In Arkansas, a national grass roots political organization (i.e., Forward America) comprised of motor carriers and shippers was recently established, among whose purposes are to:
ciencies, excessive pricing, and loss and damage claims.\textsuperscript{141}

\textbf{E. EROSION OF CARRIER LIABILITY}

Since deregulation was inaugurated, many air carriers have sharply limited their liability for loss and damage. Such unilaterally imposed limitations have been quite imaginative. Prior to airline deregulation, shippers uniformly had nine months and nine days to file a loss or damage claim. Today, the industry imposes at least four different time limits, some as short

\textit{Preserve regulated transportation at both the state and federal level by petitioning Congress to reexamine the grand experiment in the economic theory of deregulation embarked upon by the ICC; and, to foster the recognition by Congress of the historically tested principal that responsible economic regulation of transportation is essential to assure responsible freight service for the public at non-discriminatory rates.}


Although the National Association of Regulatory Utility Commissioners (NARUC) unanimously adopted a Model Act based largely on the federal Motor Carrier Act of 1980, there has been little movement for its adoption by the several states. Professors Freeman and Bellock have summarized the principal reasons for such inertia as follows:

\textit{[T]here is no great outpouring of sentiment at the state level for change and many state commissioners view the federal policy as an unproven experiment. State legislators and regulators are particularly concerned with the effect that deregulation would have on the common carrier obligation and the service received by small and isolated communities or businesses.}

\textit{Freeman & Bellock, State Regulatory Responses to Federal Motor Carrier Regulation, 35 U. FLA. L. REV. 56, 67 (1983).}

\textsuperscript{141}. As one Florida government official recently lamented:

\textit{The moving complaints began to mount. Consumer's inclinations to seek the cheapest price, not realizing that he was dealing with a totally deregulated industry, created a healthy climate for the overnight growth of two men in a pickup style of a van line. In many cases the deal was entirely oral. No written contracts. The companies had no insurance, no blankets, no ropes, no experience at moving furniture. But worse, neither could these moving companies even be located two weeks later when an irate customer filed a complaint to seek redress for a badly damaged piano, a torn mattress or the missing box of dishes. Sometimes our most diligent searches couldn't find any trace of Gonzales & Son Moving Co., when in truth it was only a telephone number and a classified ad in the newspaper.}

\textit{In one case a man moved from Houston, Texas, to Gainesville, Florida, for some $2100. His furniture was offloaded in Gainesville while his house was being finished in a small community about 40 miles away. Two months later his furniture was reloaded on a similar truck owned by the same firm and he was charged $1900 for a forty mile move. The reason — the interstate move from Texas came under the ICC pounds per mile price rules; the intrastate move from Gainesville to that small town was the deregulated move.}

\textit{[A] recent study [indicates] that some moving van lines have raised their prices; one admits to 40%. He says, 'We're going to make all the money we can before the state puts regulation back in.'}

\textit{Statement of Jack Schumaker, Staff Counsel to the Florida Commission of Agriculture, to the Council of State Governments, Southern Legislative Conference, New Orleans, La. (Sept. 1, 1982).}
as 120 days, depending upon the carrier employed. Moreover, two air carriers even insist on the filing of a "notice of intent" to file a claim, one within fifteen days and the other within thirty. Before deregulation was inaugurated, shippers had two years in which to file a suit; two air carriers have now cut this "statute of limitations" in half. Prior to deregulation, shippers had two years in which to file overcharge claims; today there are at least five different time limits, some as short as 180 days. Similarly, the time limits for bringing suit on an overcharge claim have been reduced by some carriers to as little as 180 days, in contrast to the pre-deregulation rule of two years and six months from disallowance.

One year before deregulation the CAB concluded an exhaustive investigation in which it determined that liability limits on domestic air transportation were unconscionable and archaic, and should therefore be raised from 50¢ per pound to the standard established by the Warsaw Convention of $9.07 per pound. But with the promulgation of the Air Cargo Deregulation Act of 1977, air carriers were freed from these requirements. Eleven carriers have since reduced their liability limits to 50¢ per pound. Fourteen have taken a further step by multiplying the 50¢ limitation by the weight of the package lost or damaged. Prior to airline deregulation, excess value charges were limited to 10-15¢ per $100 of excess value declared; since deregulation, twenty-nine carriers have increased these charges to 40¢ per $100. If you combine the new 50¢ per pound ceiling on liability with the increase of excess valuation charges to 40¢ per $100, the aggregate net result is a 3900% increase. Unsophisticated shippers are ordinarily unaware that such provisions have been unilaterally inserted by carriers in their bills of lading until they are faced with a lost or damaged shipment. They tend instead to select a carrier on the basis of price and service, at least until they are faced with a catastrophic loss.

VI. THE RAILROADING OF AMERICA

Widespread marketplace abuses by the railroads served as the initial catalyst for the introduction of economic regulation of transportation in the

145. W. Augello, supra note 143, at 3.
United States in the late 19th century. At least up to now, this article has been somewhat silent as to the deleterious impacts of deregulation with respect to the railroad industry and the shippers it serves. Because the experience of rail carriers has been significantly different than those of air and motor carriers, the author has chosen to treat them separately.

Of course, all modes of transportation share a common economic characteristic — they involve the movement of passengers and commodities between designated points. But of the three modes here discussed, rail transportation more closely satisfies the definition of a natural monopoly, at least for certain types of commodities and geographic regions. Certainly, there is some competition between the motor and rail modes with respect to truckload, box-car, and trailer-on-flatcar long-haul service. And, where time is a factor, some competition exists between air and motor carriage for less-than-truckload traffic. But for large shipments of bulk commodities, rail carriers enjoy a virtual monopoly.

Thus, the price of rail transportation would have to be exceptionally high before Wyoming coal shippers would find it feasible to replace 100-car unit coal trains with a convoy of trucks having an equal capacity, not to mention the associated fuel consumption and highway repair costs. Similarly, the cost of rail carriage would have to be enormously high before Nebraska grain shippers would find it feasible to air lift or catapult their grain to market. And the price of rail movements would have to grow to astronomical proportions before such shippers would find it feasible to lay their own tracks, and build their own railroads to compete with carriers determined to exact monopoly profits. Long before any of these things happened, consumers of coal (i.e., public utilities) would find it feasible to import coal from abroad (they now are); and grain shippers would find the world market for their exports declining (they may well be). Both impacts may further exacerbate our nation’s balance of payments deficit.

Although deregulation has significantly increased air and motor carrier competition by flooding markets with new entrants and greatly increasing the territories they may serve and the commodities they may haul, it has had no such effect on railroads. Indeed, there is significantly more aban-
demonstrated and merger activity than entry in rail transportation, further reducing the number of actors in the nation’s rail oligopoly. Professor William Thoms notes that “[r]egulatory freedom for railroads meant freedom to merge, freedom to abandon trackage, and freedom to change (usually raise) rates.”

After more than a decade of serious and comprehensive merger activity, the nation is today left with but seven major rail carriers, which together are responsible for 85% of revenue ton miles. In the northeast, Conrail is the only major carrier, itself the result of a 1973 merger between the Penn Central and five smaller railroads (the Penn Central was the product of the 1968 merger between the Pennsylvania and New York Central). South of Conrail there are but two large remaining railroads — the CSX and the Norfolk Southern. The CSX is the product of the 1980 merger between the Chessie and the Family Lines (the Chessie resulted from the 1963 merger of the Chesapeake and Ohio, the B&O and the Western Maryland; the Family Lines resulted from the 1971 merger of the L&N and the Seaboard Coast Line — the latter a product of the 1967 merger between the Seaboard Air Line and the Atlantic Coast Line). The CSX enjoyed net income of $367.7 million during 1981 on revenues of $5.4 billion. The Norfolk Southern is the result of a 1981 merger between the Norfolk & Western and the Southern, whose combined earnings that year...


Rail carriers’ freedom under deregulation to abandon branch lines has deprived a number of midwestern grain elevators of rail service. Samuelson, Competition’s Mixed Effects, Wash. Post, Oct. 18, 1983, at E1.

150. Thoms, supra note 147, at 210.

151. Feaver, Major Railroads Poised for Transcontinental Mergers, Wash. Post, June 19, 1983, at F1. These are 1981 figures, the last full year for which industry wide data is available. A revenue ton mile constitutes a ton of freight carried one mile. Id.

152. The five carriers were the Central of New Jersey, the Lehigh and Hudson River, the Lehigh Valley, the Reading and the Erie Lackawanna. See Wilson, Cloudy Future for Conrail, Philadelphia Inquirer, Aug. 21, 1981, at 26; Roberts, Conrail Gets Another Chance, Modern Railroads, Aug. 1981, at 54; Salpukas, Turnaround at Conrail, N.Y. Times, Dec. 4, 1981, at 36.

153. A smaller railroad is being assembled by Timothy Mellon, who purchased the Maine Central, the Boston & Maine and the Delaware and Hudson. Together these railroads traverse almost 4,000 miles. See Guilford Transp. Indus., Inc. — Control — Delaware and Hudson Co., 366 I.C.C. 396 (1982); Harkavy, Mellon to Complete Rail Purchases by Summer, Boston Sunday Globe, Nov. 1, 1981, at 63.


156. See CSX, supra note 154, at 51.
toted $500 million on revenues of $3.59 billion.\textsuperscript{157} In the west, there are four large railroads, the Burlington Northern, the recently merged Tri-Pac (or PacRail), the Southern Pacific, and the Atchinson, Topeka and Santa Fe. The Burlington Northern resulted from a 1980 merger between the BN and Frisco (the BN resulted from a 1970 merger between the Great Northern, the Northern Pacific, the Chicago, Burlington & Quincy, and the Spokane, Portland and Seattle).\textsuperscript{158} Its 1981 earnings were $223 million on revenues of $3.9 billion. Today, it serves twenty-five states and two Canadian provinces, from the Pacific Northwest to the Florida panhandle, from the Prairies to the Gulf Coast.\textsuperscript{159} The Tri-Pac merger of 1982 brought together even a larger system with the merger of the Union Pacific, Western Pacific and Missouri Pacific.\textsuperscript{160} The Santa Fe and Southern Pacific have announced plans to merge to form the nation's third largest railroad. The merged holding companies will have combined assets exceeding $10 billion.\textsuperscript{161}

The Washington Post recently predicted that these seven railroads will likely be merged into as few as three during the next several years:

Over the next decade, a combination of mergers driven by intense competition between trucks and railroads will result in a few --- probably three --- super railroads. Dozens of small branch lines, operated by private owners or state governments, will provide feeder service.

Railroad experts in government, the industry and the financial world are in unusual agreement on that scenario, although most of them would discuss the matter only if they were not identified.\textsuperscript{162}

As has been indicated, deregulation for railroads has in many instances enhanced the ability of rail carriers' ability to raise their rates. However, Congress recognized that not all freight is competitive; in promulgating the Staggers Rail Act of 1980, it did not intend to subject captive shippers to the rigors of the marketplace.\textsuperscript{163} Hence, jurisdiction over reasonableness of rates was left in the ICC under circumstances where market dominance is deemed to exist.\textsuperscript{164} However, the ICC has significantly di-


\textsuperscript{158} See Burlington Northern, Inc. --- Control and Merger --- St. Louis-San Francisco Ry., 366 I.C.C. 862 (1983).

\textsuperscript{159} See A Railroad For the Long Haul, Forbes, Apr. 27, 1981, at 120-26.

\textsuperscript{160} Union Pac. --- Control --- Missouri Pac.; Western Pac., 366 I.C.C. 458 (1982).


\textsuperscript{162} Feaver, Major Railroads Poised for Transcontinental Mergers, Wash. Post, June 19, 1983, at F1.

\textsuperscript{163} See Note, supra note 36, at 308.

luted its jurisdiction over market dominant traffic by pronunclating broad exemptions over TOFC/COFC service, boxcar service, and export coal, as well as its philosophical flirtation with Ramsey pricing. Shippers of market dominant traffic have become increasingly dissatisfied with the rail rate decisions of the ICC. One group which appears to have been adversely affected with rate increase and jurisdictional limitation decisions are shippers of coal. Specifically, coal shippers have alleged the

165. Improvement of TOFC/COFC Regulation, 364 I.C.C. 391 (1980). TOFC is “trailer on flat car;” COFC is “container on flat car.”
168. A rate scheme similar to that of differential pricing (a notion approved in San Antonio, Tex. v. United States, 631 F.2d 831 (D.C. Cir. 1980)) is Ramsey pricing. Rail carriers have suggested that the ICC adopt the principles developed by British economist Frank Ramsey in assessing whether rail rates are just and reasonable. Under Ramsey pricing, shippers are charged a rate which encompasses the variable cost of providing the service, plus a share of fixed costs inversely proportional to the shipper’s elasticity of demand for service. Hence, a shipper of coal which enjoyed the alternatives of either coal slurry pipelines or barge transportation in addition to rail service would receive a lower rail rate than would a similarly situated shipper without such transportation alternatives.

The ICC has estimated that 78% of rail costs are “variable,” and 22% are “fixed.” It is argued that Ramsey pricing will benefit all shippers, because price-elastic shippers will bear some of the fixed costs which, in turn, will reduce the fixed cost burden for price-inelastic shippers, and theoretically, will result in lower rail rates for the latter.

169. The Commission has proposed guidelines in Ex Parte No. 347 (Sub-No. 1), Coal Rate Guidelines — Nationwide, 364 I.C.C. 360 (1980), which would further reduce its role in policing rail rate increases for captive shippers. Essentially, the guidelines provide that rail carriers are free to raise their rates for market dominant traffic up to 14% annually above inflation, unless (a) such rates would exceed the “stand-alone cost” of serving the shipper, (b) such increases are attributable to inefficient rail management, or (c) the rail carrier has achieved revenue adequacy.

“Stand-alone cost” is defined by the ICC as the cost which would be incurred by the shipper if he was forced to serve himself. The reproduction of service capabilities (e.g., construction of track, purchase of locomotives and cars) is measured by the current cost of producing equipment or facilities with equivalent capabilities.

Managerial efficiency is insisted upon by the Staggers Rail Act, which encourages rail carriers to earn adequate revenues under “honest, economical and efficient management.” 49 U.S.C. § 10704(a)(2) (Supp. V 1981). Consideration of this criterion is also suggested by the Long-Cannon amendment to the Staggers Act. The Long-Cannon amendment provides that, in determining whether to investigate a rate, the Commission must assess (a) the amount of the railroad’s traffic that does not contribute to going concern value (i.e., variable costs), and the carrier’s efforts to minimize it, (b) the traffic which contributes only marginally to fixed costs and the extent to which such rates can be raised, and (c) the impact of the rate increase upon national energy and rail transportation policies. 49 U.S.C. § 10707a(e)(2)(B) (Supp. V 1981). Congress has insisted that the ICC assist the railroads in achieving revenue adequacy. 49 U.S.C. §§ 10704(a)(2), 10707a(e)(2)(3)(ii) (Supp. V 1981). The ICC has addressed the criteria relevant to its determination of “revenue adequacy” in Ex Parte No. 393, Standard for Revenue Adequacy, 358 I.C.C. 844 (1978); 359 I.C.C. 270 (1978); 361 I.C.C. 79 (1978); 362 I.C.C. 199 (1980). The Commission concluded that adequate revenues are those which allow rail carriers to earn a return on investment equal to the current cost of capital, so that they would be able to
following deleterious impacts of rail deregulation:

1. Rapid increases in rates for hauling coal, including increases of nearly 15 percent in 1980 and 1981, increases that are far more than necessary to account for inflation.
2. U.S.-produced coal is less competitive with other fuels in domestic markets, slowing the conversions from foreign oil to domestic coal.
3. U.S.-produced coal is less competitive in international markets because of high rail rates, with foreign customers increasingly turning to other nations for their supplies.
4. Many U.S. coal mines have been closed and there is high unemployment among coal miners. Nationally, 32 percent of miners were unemployed during the first quarter of 1982. Unemployment has ranged as high as 60 percent in southern West Virginia and western Pennsylvania, a situation due to a large extent to a general down turn in business, but also affected negatively by ICC rulings.
5. Major coal-hauling railroads have become highly profitable and have been increasingly diverting their capital into other industries, such as real estate, other forms of transportation, and natural resources, a matter which indicates that railroad revenues are significantly in excess of amounts required to recover costs of providing railroad services, including a reasonable rate of return from captive traffic.\textsuperscript{170}

\begin{center}
\textsuperscript{170} Compete with other firms for available sources of financing. Once a carrier has achieved revenue adequacy, the Commission will more closely scrutinize rate increases for market dominant traffic.

The standards adopted by the ICC for determining market dominance have been criticized as a decision which seriously erodes captive shipper protection by injecting the question of geographic and product competition into evidence as to the existence of market dominance in transportation. Whether a shipper could obtain a commodity from a different source or could substitute a different commodity for the freight at issue simply has no bearing on whether there is effective transportation competition for certain movements.

J. Lema, Remarks Before Conference on Coal Transportation (Arlington, Va., 1983). The ICC’s recent efforts in this area have been characterized as follows:

The I.C.C. proposed that the railroads should be permitted to charge 15 percent per year more than presently unreasonable rates for coal traffic — above inflation — until a railroad is revenue adequate and possibly beyond. These increases are to be limited only by the utilities’ purported “option” to build its own railroad. That is nothing less than total deregulation, because it would set the upper limit at precisely the level at which a shipper would go elsewhere. The I.C.C. has set out to tell the monopoly railroad how best to set an optimum monopoly price.

. . . . The I.C.C. is proposing to turn the clock back 100 years and once more let the robber barons loose on the captive traffic. On its centennial anniversary the I.C.C. will have as its most recent legacy the attempt to recreate the very monopoly conditions which it was established to control 100 years ago.


During the past four years, mine prices for coal increased only half as much as the bureau of Labor’s Producers Price Index (PPI) for all commodities. During the same period, rail rates for coal increased one and a half times the PPI — this during a period of severe recession in the American economy. J. Lema, Remarks Before Conference on Coal Transportation (Arlington, Va., 1983).
At the risk of overgeneralizing, the net effect of railroad deregulation seems to be a more desirable economic environment from the perspective of most rail carriers, and a less desirable one from the perspective of most captive rail shippers. Professor Friedlaender noted in her 1969 treatise on the subject that this might well be a result of deregulation:

To the extent that regulation prevents railroads from exploiting their potential monopoly position with respect to noncompetitive bulk commodities, deregulation should lead to increased rates and concomitant reductions in the incomes of the producers of these commodities. This would particularly affect the western farming and mining interests. Furthermore, insofar as rate competition would end the existing discriminatory pricing policies on which many past locational decisions have been based, additional producers would probably be hurt. The millers and small coal producers are especially vulnerable in this respect. Since the present blanket rate structure tends to discriminate in favor of rural and suburban areas, deregulation might also lead to rate increases in these areas.\textsuperscript{171}

\section{The Response of Government . . . or Absence Thereof}

Certainly, government has had both the jurisdiction and the opportunity to prevent these deleterious effects of excessive competition. The relevant regulatory agencies, the Civil Aeronautics Board and the Interstate Commerce Commission, were vested with such comprehensive authority in order to protect the public interest. This protection of the public was deemed essential to moderate the fundamental objective of enterprises competing in the private sector — the accumulation of wealth.\textsuperscript{172} Both agencies have tended to abdicate their essential purpose in recent years.

Despite repeated and vigorous arguments that the CAB should constrain excessive entry and predatory pricing, the agency consistently refused to do either. It has instead insisted that "[i]n healthy competition, producers who are inefficient or make bad decisions may fail, but efficient and well-managed producers can operate profitably . . . [Bankruptcies] can serve a useful purpose . . . by eliminating the inefficient or imprudent operator . . . ."\textsuperscript{173} In response to the economic demise of the industry, former CAB chairman Alfred Kahn responded: "it’s destructive and it’s cruel, but that’s the way the market functions."\textsuperscript{174} The Reagan administra-

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\textsuperscript{171} A. Friedlaender, supra note 33, at 165. In all fairness, however, it must be admitted that Ann Friedlaender has long been a proponent of transportation deregulation.
\textsuperscript{174} Comments like these have generated considerable controversy for Dr. Kahn:
   Said Mr. Kahn, about airline deregulation and presumably with a straight face:
   "There’s a lot of turmoil, but that’s what we intended."
   Are not times hard enough that it seems slightly (at least) off the wall to suggest that creating turmoil across a key industry (let alone the inconvenienced passengers) is a good thing to do?
\end{flushright}
tion has taken much the same approach as its Democratic predecessors, embracing economic Darwinism. Murray Weidenbaum, Reagan's Chairman of the Council of Economic Advisors, said: "The success of individual companies is not a concern to the marketplace — there is no assurance that any particular company is going to survive."\textsuperscript{175}

But if World Airways asks the CAB to restrain the "disastrous and completely irrational fare wars"\textsuperscript{176} of less than $100 in the highly competitive transatlantic market, and alleges that at $142, World itself was not even breaking even, one becomes highly suspect of the agency's wisdom of pursing its deregulatory approach. Certainly, World Airways must be among the most efficient in that market, for its variable and fixed costs are lower than the industry average. If World fails, it will likely not be because, as the CAB insists, it is inefficient or imprudent (unless imprudence is measured by efforts to compete fairly in densely traveled corridors), but it will be because World hasn't the deep pocket of the industry giants to be able to withstand the vicissitudes of the economic cycle, and the predatory pricing practices of its larger competitors. The death of efficient, but shallow pocketed carriers may well be the result of the CAB's blind adherence to the purported virtues of the philosophy of deregulation.\textsuperscript{177}

Unfortunately, the Interstate Commerce Commission has adopted much the same approach, issuing operating authority to thousands upon thousands of applicants who have demonstrated little more than the ability

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\textsuperscript{175} Letter from Bert Cowlan to the Editor, Wall St. J., Oct. 18, 1983, at 33.

The world's finest air transportation system is in a state of utter chaos. This does not speak as badly for Prof. Kahn as it does for the gullible clowns in Washington who heeded his ridiculous suggestions. The consumer has only begun to reap the "'rewards' of deregulation.


\textsuperscript{176} [E]conomists preach that bankruptcies are good in a free market because they eliminate the inefficient operators. This textbook theory overlooks the total cost of bankruptcies. Taxpayers eventually bear much of the cost through the loss of taxes paid by the bankrupt, the cost of unemployment and welfare benefits paid to discharged employees, etc. The public also pays in the form of higher interest rates necessitated by the losses suffered by the banks. Creditors lose and pass along their losses to consumers in the form of higher prices on their goods and services.

These considerations fail to account for the more important cost of bankruptcies — the human pain and suffering experienced by the officials, employees and stockholders of bankrupt companies. How long will the public condone an economic theory which encourages and fosters such tragedies?

Augello, supra note 143, at 9-10. Recently, the Reagan administration announced that it would oppose efforts to re-regulate the airline industry. Schwartz, Re-regulate Airlines? It Won't Fly, Dole Says., Wash. Times, Oct. 27, 1983, at 4B.

\textsuperscript{177} Brenner, Recount Air Fares, N.Y. Times, Apr. 14, 1982, at 16. These efforts by Edward J. Daly, Chairman of World Airways, were particularly interesting inasmuch as World had initially supported airline deregulation. See Salpukas, Labor Distress At the Airlines, N.Y. Times, Oct. 14, 1983, at D2.

\textsuperscript{177} See The Rise and Fall of the Civil Aeronautics Board, supra note 13.
to fill out an application form. In a landmark decision, the ICC concluded that "competition which forces an existing carrier out of business" may be desirable, for "it is preferable to replace an inefficient operator with a more efficient one and promote the introduction of innovative services or prices." Survival of the fittest seems to be at the very heart of Darwinist economics embraced by deregulation advocates. Again, the manifest tragedy of deregulation is that many efficient carriers with shallow pockets must die, for they will find themselves unable to withstand the vicissitudes of the downward cycle of the market and the predatory pricing of their larger competitors.

The Motor Carrier Act of 1980 in no way diluted the traditional statutory opposition to discrimination. Moreover, it introduced a statutory prohibition against predation into motor carrier rate regulation, proscribing excessively low rates which are predatory. However, the ICC has recently taken actions which erode the concept of nondiscrimination in carrier ratemaking.

Among such recent ICC initiatives is a rulemaking proposal which would eliminate the general prohibition against publishing rates restricted to named shippers, receivers and locations. This rule would effectively shift the burden of proving unlawful discrimination to opponents of the filed tariffs through rate protests and formal complaints, a burden they may well find impossible to satisfy. Further, the ICC recently declined the opportunity to establish standards to govern the filing of discount rates. Petitioners had argued that the widespread rate discounting in the industry was causing a significant loss of business and jeopardizing the financial viability of much of the motor carrier industry. They also argued that such discounting was inconsistent with the national transportation policy of establishing reasonable rates without unreasonable discrimination or unfair or

179. In the matter of predatory pricing, we are aware of one major carrier whose owner has given the carrier management advice that they have available the sum of $3,000,000.00 with the advice . . . "if you lose it — ok — but be sure to establish greater market share." When they, and others, have attained dominant market share what will be the end result in pricing? The answer is obvious.
We have recently noted two motor carrier bureau proposals with the sole justification for a proposed increase — "to recoup monies expended in discounts." Shortly thereafter, other bureaus also filed similar increases. No doubt noting the stupidity of such a justification, they cleaned up their language to "profit improvement." Why are we playing games?

What is the role of the Commission Office of Consumer Protection? Who will speak for the consumer, for it is they who eventually pay the cost?
Letter from Joseph F. Queenan to Paul S. Dempsey (Apr. 25, 1983).
182. Id.
destructive practices,\textsuperscript{183} and alleged that "these rates, if they are not related to costs, must necessarily discriminate unfairly between shippers, contrary to the national transportation policy and the specific prohibition of 49 U.S.C. section 10741."\textsuperscript{184} Moreover, the ICC has approved the filing of literally thousands of individual tariffs embracing a wide range of discount tariffs, including introductory discounts of up to 50% to open a new territory, aggregate tender discounts or allowances and volume discounts, discounts specifically limited to named facilities, commodities, or shippers, and blanket discounts.

A review of history inevitably leads one to the strong impression that such activities would never have been tolerated by the agency in prior years. On April 5, 1962, the Interstate Commerce Commission celebrated its seventy-fifth anniversary as an independent regulatory agency. At the formal ceremonies, one of our nation's most brilliant jurists, Supreme Court Justice Felix Frankfurter, delivered an extemporaneous speech — an address which became, due to illness, his last. Frankfurter noted that his first years as a lawyer had been devoted to practicing before the ICC, the next twenty-three years as a professor of law were spent lecturing about the ICC, and the last twenty-three years as a jurist were devoted to lecturing to the Commission. Hence, he was intimately familiar with more than a half century of the agency's activities.

Frankfurter has observed that in the seventy-five years of the history of the Interstate Commerce Commission, the agency "had an unblemished character, and has been manned on the whole by men of high competence."\textsuperscript{185} He proceeded to praise the agency's integrity:

It has maintained not merely formal independence, but actual independence of word and deed, and has been a laboratory demonstration of how economic problems may be worked out by trial and error. Finally, by virtue of all these considerations, the Commission has been a pacemaker, a model, for the subsequent commissions which, in turn, have been created in response to economic and social demands in their fields of activity.\textsuperscript{186}

Frankfurter noted that during its first seventy-five years the Commission had dealt with the issues it confronted pragmatically rather than dogmatically, "distrusting all absolutes, whether of private enterprise or government control." Can the same be said today? Is the ICC still that bastion of unblemished character, striking competence in government,\textsuperscript{187} and independence

\textsuperscript{184} 365 I.C.C. at 712.
\textsuperscript{186} Id. at 244.
\textsuperscript{187} Frankfurter said:

In the first place, the Commission illustrates, throughout its life, unblemished character .... I don't merely mean character in the crude sense of the word, but character in its largest, affirmative sense — character meaning a fastidious regard for responsibility, a
from political influence.\footnote{188} ICC Commissioner Frederic Andre recently remarked that bribes and unlawful rebates should be encouraged, for they constitute "one of the clearest instances that the free market is at work."\footnote{189} Several members of Congress responded by asking for his resignation.\footnote{190}

The Chairman of the Board of the American Trucking Associations recently criticized the Commission because, he said, since deregulation "the ICC virtually encouraged abusive pricing — if not predatory pricing — within the industry. We have to say very clearly that it's not the recession, but the ICC's . . . cavalier implementation of provisions that do not exist in the legislation passed by Congress."\footnote{191} One coal industry representative has vigorously attacked ICC efforts to deregulate rail ratemaking:

The shortest and most accurate summary of what the I.C.C. appears to be doing is that it wishes to put itself out of business and is therefore attempting totally to deregulate all traffic, monopoly or otherwise. This it has been attempting to do by subverting each of the major goals of the Staggers Act designed to benefit and protect shippers.\footnote{192}

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complete divortement between public and private interest, and all other concomitants of a true and worthy conception of public duty. Alas, that cannot be said of all public bodies, but it can be said that this Commission throughout its seventy-five years has had a career of unblemished character.

Secondly, I would say we are here to celebrate as striking a manifestation of competence in government as any I know of in the three branches of government. With all respect for each of those three branches . . . my deep conviction is that . . . this Commission has as high a record of competence as any . . . of the other three branches of government.

\textit{ld.} at 236-37.

\footnote{188} Frankfurter noted:

Thirdly, it is a necessary condition, before a Commission can effectively act, that it be independent. I do not mean independence because the statute says it shall be independent . . . but because Commissioners actively assert independence when the occasion calls for independence.


\footnote{190} Id.


\footnote{192} M. Foldes, Post-Staggers Act, I.C.C. Actions and Shipper Initiatives (address before Conference on Coal Transportation, Alexandria, Va., 1983). These views appear to be widespread throughout the coal industry. Indeed, the industry has specifically complained of the following ICC actions:

1. Promulgated a definition of "rail market dominance" which had the effect of making it nearly impossible for a shipper to demonstrate the need for ICC review of rail rates. That definition was recently overturned and remanded to the ICC by the U.S. Court of Appeals for the Fifth Circuit. However, the ICC has petitioned the Fifth Circuit to rehear the case. The Court has granted the ICC's petition.

2. Issued an unrealistic definition of railroad "revenue adequacy," which definition re-
Shortly after the promulgation of the Motor Carrier Act of 1980, one of the nation's leading transportation attorneys characterized the ICC's failure to satisfy the legislative mandate as follows:

> It is obviously the intent of the Commission to avoid balancing the competing interests, avoid the necessity of showing of broad public need for broad applications, and attempt to utilize the Congressional policy with respect to elimination of restrictions in a manner inconsistent with the Congressional intent.¹⁹³

Numerous attorneys have argued, and several federal courts have concluded, that the ICC has not followed the wishes of Congress in implementing recently enacted legislation.¹⁹⁴ Both the Fifth and Ninth U.S. Circuit Courts of Appeal have been faced with an Interstate Commerce Commis-

³ Results in the absurd outcome that only two relatively small railroads are considered "revenue adequate" despite the evident high profitability of most major coal-hauling railroads.

³ Proposed a differential pricing scheme in which a grossly disproportionate amount of a railroad's fixed costs are borne by coal shippers.

³ Proposed on February 24, 1983 a plan for determining maximum reasonableness for rates for hauling coal, which would allow railroads to impose a "bounty" on coal traffic of 15 percent each year above inflation.

³ Refused to carry out in any serious way the requirements of the Long-Cannon amendment in the Staggers Act, which amendment called upon the ICC to see to it that railroads move to eliminate traffic that was not paying its fair share (non-compensatory traffic) and to avert cross subsidization of competitive traffic by captive movements. Failure to eliminate noncompensatory traffic causes shippers of commodities such as coal to pay excessive rates.

³ Adoption of a railroad-proposed inflation index, which overstates the railroads' cost increases by completely disregarding gains made in a railroad's productivity and efficiency, and, therefore, discourages efforts to achieve such gains.

³ Allowing upward adjustments in rates because of higher costs, while not requiring downward adjustments when railroads' costs decrease.

³ Proposed regulations on March 3, 1983, which deregulate coal export traffic, even though much of this traffic is "captive" to the railroads.


¹⁹³ ASS'N OF ICC PRACTITIONERS, EASTERN TRANSPORTATION LAW SEMINAR 51 (1980) (address of Alan Serby). More recently, he noted:

> A trucking industry already characterized by serious overcapacity and underutilization, has become the beneficiary of a regulatory policy designed and administered to further increase capacity.

The specific intent of present members of the Interstate Commerce Commission, in connection with entry policy, is to grant each and every application filed with the Commission whenever and wherever possible, and to the broadest extent available.


¹⁹⁴ See, e.g., Dempsey, supra note 1. As Justice Felix Frankfurter noted in the "Steel Seizure" cases:

> The accretion of dangerous power does not come in a day. It does come, however slowly, from the generative force of unchecked disregard of the restrictions that fence in even the most disinterested assertion of authority.

Youngstown Sheet and Tube Co. v. Sawyer, 343 U.S. 579, 593 (1952). Professor Donald Harper noted the possibility that the ICC might proceed with de facto deregulation, despite the contrary intent of Congress, when the Motor Carrier Act of 1980 was promulgated.
sion not only determined to act ultra vires with respect to congressionally delegated authority, but to contumaciously ignore judicial decisions attempting to identify perimeters within which the Commission may lawfully act. Confronted with a defiant agency, both circuits have been forced to take the additional extraordinary step of issuing writs of mandamus insisting upon compliance with their judicial decrees. The leaders of the American Trucking Associations, the Teamsters Union, the Motor Carrier Lawyers Association, the National Motor Freight Traffic Association, and the Owner-Operators Independent Drivers Association of America jointly submitted a forceful plea to Congress to stop these ultra vires activities:

In our view, the ICC thwarts the will of Congress and violates the law. In so doing, the ICC exacerbates the deteriorating condition of the trucking industry, contributes to unemployment, and fosters volatile, unlawful rate practices.

A critical aspect of the Act of 1980 is how the ICC interprets its various provisions and how efficiently the Commission works. The success or failure of the Act will be largely determined by the Commission. As in any regulatory system, the persons performing the regulating are more important to its success than the law upon which the regulation is based.

As to interpretation of the Act by the ICC, although the Act of 1980 is more specific in what Congress wants done than most other transportation regulatory legislation has been, there is still room for considerable "interpretation" by the ICC. Should the Commission choose, it can interpret the new law in such a way as to produce almost total deregulation of entry, even though beyond the intention of Congress. If the oversight provision of the Act does not protect against this, the determination of the future of economic regulation of motor trucking will be left by default to the ICC.


195. See American Trucking Ass'ns, Inc. v. Interstate Commerce Comm'n, 659 F.2d 452 (5th Cir. 1981); Amador Stage Lines, Inc. v. United States, 685 F.2d 333 (9th Cir. 1982); Central Forwarding, Inc. v. Interstate Commerce Comm'n, 698 F.2d 1266 (5th Cir. 1983). See also Ritter Transp., Inc. v. Interstate Commerce Comm'n, 684 F.2d 86 (D.C. Cir. 1982); Steere Tank Lines, Inc. v. Interstate Commerce Comm'n, 666 F.2d 255 (5th Cir. 1981).

196. See, e.g., American Trucking Ass'n's v. Interstate Commerce Comm'n, 669 F.2d 957 (5th Cir. 1982); American Trucking Ass'n's v. Interstate Commerce Comm'n, 673 F.2d 82 (5th Cir. 1982).

197. Letter from Bennet C. Whitlock, Jr., Jackie Pressler, Harold D. Miller, Jr., James Harkins, and Mark Perry to Bob Packwood (June 29, 1983). This letter is reproduced, infra note 231. A similar letter was recently sent by Duncan McRae, Sr., Chairman of Forward America, to every member of Congress. Among the conclusions it reached are the following:

[T]here are many of us who do not believe the problems besetting the industry today are necessarily caused by the Motor Carrier Act of 1980. Rather, the problems are created by the fierce determination of the D.O.T. and the present members of the I.C.C. to deregulate the motor carrier industry through administrative fiat. Members of the trucking industry, by and large, do not believe it was the intent of the Congress to summarily deregulate trucking in the Motor Carrier Act of 1980. However, the present membership of the I.C.C., all of whom are avowed and professed deregulators, are effectively deregulating and/or dismantling the trucking industry under the guise of interpreting the Act.

With all due respect, it appears to me that the I.C.C. and the D.O.T., in concert, are prostituting the true intent of the Motor Carrier Act of 1980 and that the Congress is abdicating its responsibility when it allows the Executive Branch to usurp its Constitutional authority in this area.

Letter from Duncan McRae, Sr., to 435 Congressmen (July 4, 1983). Representative Robert A.
It was the intention of former CAB Chairman Alfred Kahn to so "scramble the eggs" (by deregulating comprehensively and expeditiously through the vehicle of administrative fiat) that no one would ever be able to put them back into their shells again. It is no secret that if an agency decides to perform its functions irresponsibly, those members of the public which have traditionally benefited from regulation will ultimately view deregulation as a lesser vice than irresponsible regulation, and themselves call for the death of the beast which has devoured the benefit of the regulatory burden. This, unfortunately, is the point at which many of the nation's airlines now find themselves.

The deregulation zealots appointed by Presidents Carter and Reagan to the Interstate Commerce Commission may have mortally wounded that Grand Old Lady at 12th and Constitution Avenue. With wrecking balls of steel they attacked her very foundation, determined to crush her into rubble, and sew the ground with salt so that nothing would ever grow there again. At that seventy-fifth birthday party for the ICC mentioned earlier, Justice Frankfurter, perhaps prophetically, addressed the possibility that the agency might one day end, not with a bang, but with a whimper:

It is a very wise man who said that institutions do not die, they commit suicide. And you can commit suicide by just ceasing to have life. I hope, and I have the highest confidence, that the Interstate Commerce Commission will remember the other part of the phrase of Ecclesiasticus, "Let us now praise famous men, and our fathers that begat us" and continue to live in the spirit of the men who preceded them. Continue to live in their spirits with reference to your problems and seventy-five years from now there will be an even more appreciative audience and nation grateful to the Commission for its achievement.  

ICC Chairman Reese Taylor, Jr. recently informed the Congress that he would favor sunsetting the agency he heads. The agency already has suffered a reduction in the size of its staff to only two thirds the 2,100 individuals it employed five years ago. Further, Chairman Taylor has made it clear that, irrespective of his personal beliefs on the nature and course of the agency's demise, he plans to "fully support whatever the administration proposes" in the nature of legislation. Again, can the ICC still be characterized as a bastion of unblemished integrity, competence,
and independence? As Frankfurter said, institutions do not die, they commit suicide. The CAB committed suicide by strongly supporting the Airline Deregulation Act of 1978, which scheduled the agency's self-destruction in 1985. Similarly, the ICC may not live to enjoy its centennial celebration in 1987.

VIII. CONCLUSIONS

The benefits of responsible economic regulation of transportation included the provision of an adequate level of service at a reasonable price to all communities and shippers, no matter how large or small. The industry enjoyed healthy competition without industry concentration.

Excessive entry coupled with the abdication of governmental oversight over predatory ratemaking and other unlawful practices (and, yes, the recession as well) have created an economic environment in which the current series of cutthroat rate wars become inevitable. Newsweek summarized the intense problems faced by the airline industry as follows:

Since the Carter Administration began to ease Federal restrictions on the troubled U.S. airline industry in 1977, numerous unprofitable routes have been abandoned. Service has deteriorated, and the airlines are frantically manipulating fares up and down to attract business and to satisfy shareholders nervous about their mounting financial losses. The desperation tactics make air travel more complicated and, since they defy reason, they have brought some big carriers dangerously near financial collapse.

Thomas G. Plaskett, vice-president of American Airlines, described the contemporary economic environment in these terms: "Deregulation has encouraged the concentration of services on major, dense routes, and this has led to excessive, destructive competition and over-capacity. We find it difficult to reconcile such destructive competition with the overall public interest." Richard Ferris, Chairman of the Board of United Airlines,

202. In 1977, the Senate Committee on Government Affairs concluded that "[f]or much of the past fifteen years, neither the White House nor the Senate has demonstrated a sustained commitment to high quality regulatory appointments." Staff of Senate Comm. on Gov't Affairs, 95th Cong., 1st Sess., Study of Federal Regulation xxxi (Comm. Print 1977).

[The Interstate Commerce Commission . . . was, formerly, widely considered the most eminent and effective of all the federal agencies. Past Commissioners, such as Joseph Eastman, Clyde Aitchison, Howard Freas, Rupert Murphy, and others, were experienced, dedicated and revered regulators, who created, molded and developed our renowned national transportation system. But with the enactment of the Presidential Reform Act of 1969, the Chairman, and the Commission itself, fell under the control of the President and his staff, and became a political animal. This condition has been aggravated by the predetermined regulatory philosophies of the latest appointees to the Commission, and their headlong rush to deregulate transportation. And if this means that they must disregard the governing laws, courts, Congress, or anyone else to do so, so be it.

D. Baker, supra note 19, at 10.

203. The U.S. Air-Fare Dogfight, Newsweek, Apr. 19, 1982, at 69.

admitted that "[r]estructuring an industry as large as ours means shakeouts, fallouts, irrational behavior, and a topsy-turvy marketplace." His counterpart in Western Airlines, Neil Berg, noted that "[a]irlines are out there cutting each other's throats and bleeding to death." Similarly, Eli Timoner, chairman of Air Florida, remarked: "It's like lemmings throwing themselves off a cliff. There's no logic to it at this point. It's unbusinesslike." James Worsham, president of Douglas Aircraft Co., said: "The airlines are on a kamikaze path . . . ." He suggested that a blue ribbon panel of airline executives be established to work closely with Congress to solve the industry's problems. One major daily newspaper summarized the contemporary problems of the deregulated airline industry as follows:

Airlines have less room for differentiation [than do department or grocery stores]. . . . They tend to match each other in convenient departures. That leaves little to fight about except ticket prices, and so far they've been pricing themselves to destruction.

That has lowered many fares. But it has created a bewildering world where some passengers pay twice as much as a seatmate, and more for short haul routes than transcontinental flights. Service to many smaller cities is vanishing. The public has cause to join airline employees in hoping order returns to the chaotic skies.

Although initial airline price competition generated additional price sensitive travelers, lower rates for freight will not have the corresponding effect for carriers of commodities, for the freight transportation industry is relatively price inelastic. Nor is an unhealthy transportation industry likely to

206. Id.
208. Mayer, Uncertainty Clouds Future of Airlines, Rocky Mountain News, Apr. 17, 1983, at 98. However, it must be recognized that many air carriers have concluded that no regulation at all would be preferable to the existing governmental environment, or reregulation. As United's Chairman, Richard J. Ferris, noted, "the egg of deregulation has been well scrambled and there is no way to unscramble it." Burkhardt, Airlines, Unions Split on Decontrol Results, J. of Com., June 16, 1983, at A2. See U.S., Carrier Officials Oppose Reregulation in Spite of Losses, Av. Week & Space Tech., June 6, 1983, at 51. United, the nation's largest air carrier, has long been a vigorous opponent of airline regulation.

E.H. Boullion, senior vice president of Boeing, characterized the impact of airline deregulation as stretching the system "beyond the breaking point." He predicts that the market disruptions engendered by deregulation will likely continue indefinitely. Boeing Official Cites Dangers of Deregulation, Wash. Post, Oct. 26, 1983, at D10.

210. Cook, Transportation, Foreges, Jan. 8, 1979, at 56. Nevertheless, even the temporary attributes of airline deregulation may not be repeated in the surface transportation of commodities. As has been indicated, the passenger market is price elastic — lower prices may generate demand from discretionary travelers. However, in the aggregate, the commodities market is almost totally demand-inelastic with respect to the use of transportation services. Between carriers and modes there may be some demand elasticity, but the total market, at any point in time, is virtually finite.
be a safe industry, leading to unnecessary loss of equipment, commodities and, unfortunately, human life. Furthermore, such intensive competition is limited to high density markets, creating inevitable price discrimination against small shippers and small communities. In oligopoly or monopoly transportation markets, rates have risen substantially. Undoubtedly, the incentives for locating industry in rural America will be diminished, while the incentives for locating in urban locations will be correspondingly increased. Urban America seems to be turning its back on the "outback." Moreover, the ripple effect of discriminatory rates upon the American economy will constitute an additional contribution to the economies of scale that large industries already enjoy, thereby exacerbating an environment in which most American industries ultimately become highly concentrated, while smaller competitors struggle, fail or are absorbed into the conglomerate giants. Thus, smaller industries will pay higher prices for transportation serv-

Hence, while air passenger deregulation led to price competition which, in turn, enabled air carriers to fill seats which might otherwise have flown empty, deregulation is unlikely to fill empty areas in motor carrier trailers or rail boxcars. 211. Clearly, there is more at stake than the sanctity of the laws of the marketplace. There is a public interest in assuring that the fundamental ingredients of economic growth are abundant in all regions of our nation, so that the fruits of such growth might be enjoyed by a larger segment of the population. This is, of course, a distribution of wealth concept. A geographic disbursement of economic growth offers the potential for a more equitable distribution of regional growth rates. Moreover, by removing industry from the concentrated urban areas where the industrial revolution was born, the quality of life might ultimately be improved as workers, following industry like a magnet, enable population to become more geographically disparate.

Like communications and energy, transportation is a fundamental component of national, regional, and local economic development. If any of these vital components is deficient, either from a qualitative or quantitative standpoint, investment in industrial plant will not be forthcoming and existing industry may relocate elsewhere. Traditionally, it has been thought that these essential industries were too important to be left to the rigors of the marketplace.

Several of these industries were natural monopolies (e.g., the early railroads, telephone, telegraph, gas, and electric companies, and to some extent, television and radio), which if unregulated would produce in lower quantities and at higher prices than would industries in a competitive market. Regulation seeks to substitute what is lacking in the marketplace by insisting that such natural monopolies produce at a lower price and higher volume than they otherwise might.

Recognizing this distinction, virtually every major industrial nation on the planet treats these industries in a manner significantly different from the rest. In most, the industries are owned and operated by the state. In transportation, most of the rail, motor, barge, and air carriers are socialized, even in Western Europe.

In the United States, the services of transportation, communications, and energy have largely been performed by the private sector, with government serving the role of a vigorous regulator of a wide variety of activities, weighing and balancing the public interest against what would otherwise be the economic laws of the market place. The government plays a dual and perhaps schizophrenic role — on the one hand, it seeks to stimulate the inherent economics and efficiencies of the regulated industries; on the other, it seeks to protect the public from the abuses which these industries might otherwise perpetrate. For the most part, the United States has been able to avoid nationalizing these industries, for private ownership thereof has, on the whole, proven successful. The major exception is rail passenger service.

Dempsey, supra note 24, at 311.
ices, while their larger competitors enjoy relatively lower shipping costs; consumer costs will likely reflect such discrimination.

The prolongation of contemporary rate wars will force even more carriers into bankruptcy or merger, ultimately leading to an economic environment in which there will likely be fewer effective competitors, particularly in those sectors of the industry (e.g., less-than-truckload transportation) where entry costs are relatively high.\footnote{212} Hence, the structure of the transportation industry will come to more closely resemble every other major mature American industry. 

Forbes magazine predicted that, in the short term: deregulation will bring a rash of new competition into the trucking business: competitors who will price-cut their way into the market and set off a wave of mergers that will transform trucking into a far more concentrated business than it is now. The short haul and regional truckers may well be squeezed out and the big national companies — outfits like Yellow Freight, Roadway Express, Consolidated Freightways and McLean Trucking — will come to dominate the industry.

... [L]ong-term deregulation of trucks and rails ... [will] only lessen competition in trucking, encourage prices to rise and could further weaken the railroad industry.

... If the aim of deregulation is to bring freight rates down, the result may

\footnote{212. The critics [of regulation] seem to misunderstand or consciously avoid one of the traditional objectives of motor carrier regulation: although reasonable rates for the industry as a whole may result in higher profit margins for the larger, more economically efficient carriers, they also protect small, marginally efficient carriers. Protection of small carriers, the preservation of diversity, and the willingness to pay the incremental additional price have all contributed to the fundamental foundations of motor carrier regulation, and have preserved a healthy competitive structure. To turn this practice against ... the industry, without first addressing the underlying value judgment that "smallness" should be protected for its inherent value in stimulating innovation in service and price and "largeness" must be restricted for its inherent risks in stifling such economic attributes, is to undermine the traditional objectives of regulation without ever stating an acceptable justification for such a radical change in course.}

Dempsey, supra note 21, at 371.

Professors Wagner and Dean predict that:

To the extent that smaller, less efficient carriers are forced out of business, larger, more efficient companies increasingly may dominate motor carriage. The result may move the industry toward a greater degree of imperfect competition as several large firms dominate. ...

An open-door entry regulation policy may invite a new type of trucker — inexperienced, overconfident, and opportunistic. Many fear an influx of people with little capital, poor or used equipment, and little education coupled with high expectations. Whether such carriers fill a service void is questionable. Although these carriers often cut rates to gain business initially, failures frequently have resulted due to a lack of managerial expertise or cost control; prior to that time, however, there is often less need awareness for safety and service.

One effect of deregulation is that carriers may lessen service to smaller areas and concentrate on the more lucrative, urban centers.

Wagner & Dean, supra note 106, at 415 (citations omitted).
be . . . to reduce rather than enhance competition.213

In the words of Dun's Business Review, we are witnessing a "severe industry shakeout." During the "shakeout," many Americans employed by carriers, and many stockholders of or lenders to transportation businesses will be expected to pay the price of the grand experiment in deregulation.214 Many U.S. air and motor carriers will not survive the transition. The experience of deregulation in both Australia and Great Britain was that following a limited period of intensive competition and carrier bankruptcies, the less-than-truckload sectors of the motor carrier industry became oligopolistic in character.215 Professor Garland Chow's study reveals that deregulation in Australia created an economic environment in which only four major motor carriers survived.216 Many industry experts predict that the ultimate result of transportation deregulation in the United States will be sharply increased industry concentration. As has been indicated, the Washington Post predicted that during the next decade rail mergers will reduce the number of our nation's railroads to as few as three.217 Horizontal integration may well result in the creation of enormous multimodal carriers. Pointing out that

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214. It seems to me that everything that is a product or a service must be paid for by society. If we are talking about the transportation of goods or the transportation of people, we are talking about individuals or companies paying for that transportation not only as individuals but as members of society. If at a particular time or season in our economy through the forces of deregulation or simply because of the era, a group of people pay less for the transportation of goods or services than these services are "worth," they or someone else in society must pay the extra cost. The people involved may pay by the receipt of shoddy or even dangerous transportation service. They may pay for it indirectly by contributing as taxpayers to government subsidies. They may pay for it as members of society by living with the very expensive process of entry into the business world, cut throat pricing, and bankruptcy.

... In the bankruptcy process members of society pay. Creditors lose the money which they have given to the transportation company. Bondholders or stockholders of the company lose and all of those losses are spread often among groups of people who can least afford to accept that loss. People whose pension funds have been invested in a company like Braniff lose or small suppliers who have extended credit for tires, gasoline, and many other forms of service and goods. And finally, society pays when there is an elimination of the competitive force of the small and medium size businesses and conglomerates or large corporations take over.

... The most searing statement which I felt you made was the advocacy by the deregulatory people of the intermodal transportation concept. "Intermodal" is simply another word for the control of transportation services by the railroads or ultimately by corporations which own railroads, and if that occurs, no amount of legislation will reverse process. We will be stuck with an expensive and totally inefficient transportation system within the United States. God Help Us!

216. Id.

The key to the railroads' strength is that they have far more cash and fixed assets than other types of carriers, and far less internal competition. While the number of truckers
carriers such as CSX Corporation (itself the product of the 1980 merger between the Chessie and Seaboard Coast Line Railroads) have begun trucking companies, purchased natural gas pipelines, is expanding its aircraft services operations, and is acquiring a barge company, the Wall Street Journal predicts that “[o]ver the next few years, a handful of giant companies are expected to evolve, each offering global door-to-door service.”218 It went on to point out some of the dangers of such accentuated concentration:

Some observers fear that if a handful of multimodal companies come to dominate the transportation industry, a lack of competition could inflate freight rates.

...[T]he newly powerful rail industry has shown that it is capable of running roughshod over potential competition, a circumstance that has some shippers and elected officials demanding that railroads' power be curbed. Ultimately, with fewer competitors, the United States will likely enjoy higher rates and poorer service than that which existed prior to deregulation.219

The airline industry, too, is likely to become more concentrated as deregulation progresses. “Experts say the shakedown may continue for another five or ten years, with only three big carriers ultimately serving domestic routes and just one U.S. line carrying international travelers.”220 Ultimately, with fewer competitors, the United States will likely enjoy higher rates and poorer service than that which existed prior to deregulation.221

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proliferate, the number of railroads shrinks, with the outlook for no more than six to 10 major rail systems serving the U.S. within five years.

Id. at 18.

218. Id. As an example of rails' enormous political and economic clout, the article pointed out the industry's success in defeating a congressional proposal to promote coal slurry pipeline construction. "Most coal companies are 'captive' to a single railroad and wanted coal slurry pipelines so as to create a competitive situation." Id.

219. Id.

220. The Airlines Hit a Downdraft, NEWSWEEK, Oct. 10, 1983, at 66. Other commentators have affirmed the move toward concentration: "Economists predict that by 1990 there will be four or five giant airlines and a host of specialized, although not necessarily tiny, ones." A Painful Transition For the Transport Industry, BUS. Wk., Nov. 28, 1983, at 83. See Byrne, United's Expansion on West Coast Threatens Future of Small Airlines, WALL ST. J., Nov. 16, 1983, at 33.

221. In 1980, this author predicted that transportation deregulation would proceed through three stages:

In the first, price and service competition are increased, carriers become innovative and imaginative in the types of price and service combinations they offer, and consumers thereby enjoy lower priced transportation. Carriers are free to maximize their profits by leaving unprofitable markets and investing their equipment in more lucrative ones. In the airline industry, lower prices initially generated increased passenger traffic, thereby enabling air carriers to fill seats which might have otherwise flown empty. As has been indicated, air carriers left many of the small, remote, isolated communities of our nation and transferred their aircraft to the more heavily traveled markets. Passengers in these dense markets enjoyed intense pricing and service competition. Airlines generally enjoyed higher profits, at least during stage one.

As a result of the de facto deregulation of entry by the ICC, with a massive increase
Many are now beginning to argue for the reintroduction of some moderate form of responsible economic regulation. The president of one of in both the percentage of applications granted and in the number of applications filed, the motor carrier industry also finds itself in stage one of deregulation. New entrepreneurs are entering the industry, freight prices are being reduced drastically, and less-than-truckload carriers are beginning to lose truckload “cream” traffic to expanded contract carriers and new operators. The larger carriers are likely to respond with their own competitive prices and to reduce service in the less lucrative markets. The first stage is the one to which deregulators point to demonstrate the attributes of deregulation.

The second stage is an embarrassment to deregulators. This is the stage in which the airline industry now finds itself. Because of excess capacity and unrestrained price and service competition, air carrier profits have plummeted; indeed, the industry is experiencing the worst losses in the history of aviation. In order to retrieve some of their operational losses, carriers have begun to raise prices drastically in all but the dense, highly competitive markets in which they may wish to preserve their market share. Thus, airline fares rose 34 per cent from June of 1979 to March of 1980, an increase which far exceeds the increase in the price of fuel as well as other operational cost increases. [Economist Michael Evans] has succinctly summarized the market effects of deregulation upon the airline industry:

“In the short run, deregulation does indeed seem to be the promised land. Prices rise more slowly, productivity increases, service expands, and everyone is happy. However, after the initial euphoria, it turns out that profits are not really increasing after all.

As a result, rationalization of the route structure begins, which turns out to mean price-cutting on primary routes, coupled with higher prices and less service on secondary routes.

When this happens, the gain in productivity slows or even reverses, thereby negating much of the benefits of deregulation. We end up with no improvement, or even higher prices and lower productivity in that industry.”

The continued inability of many carriers to balance their sheets due to the intensive competition they are forced to endure under deregulation will force many carriers to float “belly up” in bankruptcy. This will occur with greater frequency in both the airline industry and the motor carrier industry. During the second stage, prices will continue to be set at reasonable levels in highly competitive markets, and will continue to grow at unreasonable rates in monopolistic or oligopolistic markets. Service will begin to deteriorate in both.

Stage three of deregulation will constitute the ultimate transportation system with which the nation is left. The carriers which have suffered most during stages one and two will, by this point, have gone bankrupt, leaving many markets with very little competition. A monopolistic or oligopolistic market structure will result in high prices, poor service, and little innovation or efficiency. Potential entrants, having witnessed the economic calamity of destructive competition, may be unwilling to enter so cutthroat an industry. Because the economic barriers to entry are greatest in the airline, railroad, and less-than-truckload motor carrier industries, concentration will be greatest here. Small communities will receive poorer service and/or higher rates than they enjoyed under regulation. Small shippers are likely to receive poorer service, poorer liability protection, and/or higher rates than larger corporations. Much of the industry, particularly small carriers, may be unhealthy, leading to some questions as to stability of service. In the end, the industry structure created by the free market may be much less desirable than that which was established under federal economic regulation.


222. Columnist Hobart Rowen has vigorously called for a reintroduction of regulation: “Transportation is not just any old business. Basically, it’s a public utility, which has to be regulated in the public interest. It’s time to re-regulate the airlines.” Rowen, Airline Deregulation: A Bankrupt Policy, Wash. Post, Sept. 29, 1983, at A21. Columnist Carl Rowan echoed these concerns:

It is crucial to America’s economic and social well-being, and surely its security, that we have an airlines system that can be relied upon in peace and war.

Congress deregulated our airlines just enough to perpetrate a disaster. Can it admit
our nation’s largest air freight forwarding companies conceded “with great reluctance . . . that the task (of restoring the air transportation industry to economic balance) can best be accomplished through the reintroduction of moderate government regulation of route entry. . . . We can, by judicious reapplication of regulation, correct excesses that now debilitate us all so extensively.”\footnote{223} Not only carriers are criticizing the grand experiment in deregulation. The Executive Director of the Shippers’ National Freight Claims Council, describing deregulation as a “dismal failure,” urges the reintroduction of responsible regulation, saying:

The obvious solution is to start anew with a sound regulatory policy, carefully administered by transportation-oriented experts instead of economists, and to reinstate air transportation as a public service requiring reasonable prices and service for all citizens and communities on a non-discriminatory basis.\footnote{224}

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to an error, and reverse its action of 1978, when so many of its members voted for a debacle? Let us pray.

Rowan, We Goofoed — Let’s Regulate Airlines Again, Chicago Sun-Times, Oct. 10, 1983, at A25. One CAB Staff Member has prepared an impressive analysis of the relevant financial and statistical data, and concluded that:

The evidenced structural changes have caused and will continue to cause a higher required overall fare level, generally poorer passenger service, and allow significant price discrimination. It is further evident that fares are not cost-based, and that the industry is becoming less productive and failing to share the expected efficiency gains.

. . . . Large short-term consumer gains are coupled with tremendous operating and capital losses by the industry. Improved service quality in some markets is offset by lower quality service system-wide. Increased service competition has lowered unit productivity, increasing cost with little gain in efficiency. So far, I do not believe the gains can be shown to outweigh the losses.

Unfortunately, there seems to be little reason to expect the promised benefits of deregulation to come to fruition.


Senator Mark Andrews (R. -N.D.) has recently introduced a bill, S. 2047, to provide some measure of stabilization for airline rates. See Deregulating America, Bus. Wk., Nov. 28, 1983, at 80.

\footnote{223} Malkin, Second Thoughts, HEREFORD’S NORTH AMERICA, June-Nov. 1982. See also Berg, Needed: A Return To Regulation, TRAFFIC WORLD, Nov. 1, 1982, at 42.

\footnote{224} Augello, supra note 143, at 10.


The returns clearly showed that air cargo deregulation has failed to win the broad, unqualified shipper enthusiasm that had been taken for granted by its early proponents. Although 45 percent cast their vote in favor of deregulation, a large minority (34 percent) preferred a return to some form of regulation. Considering the fact that 21 percent of the 302 respondents had still not made up their minds on the issue, it can be seen that substantially less than half may be regarded at this time as staunch supporters of deregulation.

\textit{Id.} at 6.
An airline labor leader recently asserted that "judging from the destructive impact on airline profits, the declining level of passenger safety and convenience, and the overwhelming burdens placed on airline employees, I can only conclude that deregulation has been a disaster." Academicians are also beginning to join the ranks of those calling for responsible regulation of transportation. Professor Jerold Muskin notes that:

Transportation, as a principal part of the community's physical distribution infrastructure is too important to leave to the uncertain (at best), or perverse (at worst), performance of the free market. . . . The argument that the unconstrained marketplace necessarily functions to produce improved results for our nation is simply wrong. It is a doctrinaire shibboleth. One need not look for examples of market failures that must be cured by government intervention. Highway common carriers stripped of rules, responsibilities and rights, it is submitted, fit into this category.

Similarly, Professor Frederick Thayer argues:

Free market mythology is so entrenched in the U.S. that neither liberals nor conservatives are yet disposed to admit that it is time to begin again. If ever there was a need for a national commission to develop a sensible regulatory system, and to link together the domestic, international, and even military

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As the . . . . survey . . . appears to indicate, air cargo deregulation has been less than a howling success. Two thirds of the Fortune 500 traffic/distribution executives surveyed reported not having been stimulated by deregulation to the point where they increased their air freight usage. Thirty-four percent want regulation; another 21 percent are undecided.

Id. at 38.

225. DOT's View of Airline Deregulation Challenged by Small Cities, Labor, TRAFFIC WORLD, June 20, 1983, at 16-17. This statement was made by Linda A. Puchala, President of the Association of Flight Attendants, before a subcommittee of the House Committee on Public Works and Transportation. She went on to say:

As part of the struggle to survive harsh competition in the deregulated skies, the industry has extended its cost-cutting efforts not only to reducing labor costs, modifying route structures, and trimming passenger service such as food, ticketing, and baggage handling. The airlines are also cutting costs in ways that passengers don't see — ways which reduce the level of safety.


aspects of air transportation, the need is now supranote 35, at 228.

Twenty-seven of the chief executive officers of the nation's coal companies recently informed President Reagan that they were "gravely concerned about actions and decisions of the Interstate Commerce Commission that have been taken in the name of railroad deregulation." They asked the President "to appoint to vacant positions on the Interstate Commerce Commission individuals who would recognize, as Congress did by passing the Staggers Rail Act, that adequate protection for captive shippers must be continued." The coal industry, the electric utility industry

228. Thayer, supra note 35, at 228.

[7] Those who undermine our transportation system are changing the kind of country we have, and changing it for the worse. As deteriorating transport raises internal trade barriers, we will move toward a Balkanized economy. A Balkanized economy means reduced efficiency, reduced competitiveness in world trade, and restricted opportunity as we give up the economies of scale created by our continent-wide "common market." We take this common market for granted, but we forget how rare an achievement it is in the fragmented, tribalized march of human history. To preserve this achievement, we must learn to do our "competition" analyses on a much larger scale, recognizing that sometimes we have to sacrifice a measure of competition in one sector (such as transportation) in order to maximize competition in the economy as a whole. Above all, we must steer a course between taking our transport network for granted, on one hand, and capriciously tinkering with the underpinnings that give it stability and predictability on the other hand. What I'm talking about is pretty well summarized by a phrase every schoolchild knows: "one nation indivisible."


229. This letter is reproduced in its entirety:

May 25, 1983

The President
The White House
Washington, D.C. 20050

Dear Mr. President:

As chief executive officers of major coal companies, strong advocates of the free market, and supporters of your economic policies, we are writing to ask that you use your appointive powers to remedy serious shortcomings at the Interstate Commerce Commission. We are gravely concerned about actions and decisions of the Interstate Commerce Commission that have been taken in the name of railroad deregulation, but which are inimical to the interests of coal producers and users and prejudicial to our mutual objective of less regulation by government.

The attached summary document notes the recent ICC decisions and outlines their effects on coal producers, coal users, and consumers of electricity and steel. The 1980 Staggers Rail Act was intended to reduce railroad regulation in order to assist rail carriers in achieving revenue adequacy by allowing them greater flexibility in pricing their services. However, the Act specifically preserved regulatory protection for rail shippers in situations where competitive market forces are inadequate to ensure reasonable transportation charges. With this assurance of captive shipper protection, the coal industry, which is the principal provider of cargo to the major railroads, strongly supported the Act.

Implementation of the law by the ICC has ignored captive shipper protection to such an extent that the desirability of reduced regulation of the railroads is now open to serious question. As strong supporters of economic deregulation, we have reached this conclusion reluctantly, but we have yet to find an acceptable alternative when competition is inadequate to prevent abuses of market power.
and the mineworkers have vigorously supported the promulgation of correc-

One action that you can take to restore balance in these matters is to appoint to vacant position on the Interstate Commerce Commission individuals who will recognize, as Congress did by passing the Staggers Rail Act, that adequate protection for captive shippers must be continued and that reduced regulation of the railroads is feasible only where sufficient competition exists to ensure reasonable rates.

Sincerely,

Robert H. Quenon
President and Chief Executive Officer
Peabody Holding Company, Inc.

Nicholas T. Carnicla
Chairman and Chief Executive Officer
The Pittston Company

Oles Bennett, Jr.
President and Chief Executive Officer
The North American Coal Corporation

S.O. Ogden
President
Sunedco Coal Company

J.L. Marvin
President
Anaconda Minerals Company

C.K. McArthur
Senior Vice President
Utah International Inc.

William G. Kegel
President and Chief Executive Officer
Rochester & Pittsburgh Coal Company

John M. Farley
Vice President — Raw Materials, Purchasing & Traffic
Jones and Laughlin Steel Corporation

Michael K. Reilly
President
Zeigler Coal Company

Herbert E. Jones, Jr.
Chairman of the Board
Amherst Coal Company

Leo C. Smith
President
Coastal States Energy Company

Anthony Digiovanni
Chairman and Chief Executive Officer
Barnes & Tucker Company

Gordon Bonnyman
President
Blue Diamond Coal Company

Robert F. Kropp
President
Midland Coal Company

B.R. Brown
Chairman and Chief Executive Officer
Consolidation Coal Company

Richard M. Hoisten, Jr.
President
The Pittsburg & Midway Coal Mining Company

W.S. White, Jr.
Chairman and Chief Executive Officer
American Electric Power Company, Inc.

James G. Randolph
President
Kerr-McGee Coal Corporation

Garry N. Drummond
Chief Executive Officer
Drummond Coal Company

Hugh W. Evans
President
Old Ben Coal Company

J. L. Jackson
Executive Vice President and President, Coal Unit
Diamond Shamrock Corporation

Ronald E. Sieling
President
Eastern Associated Coal

W.E. Cotter, Jr.
President — Energy Group
National Steel Corporation

Jesse L. Koontz
Vice President Natural Resources Group
W.R. Grace & Co.

Thomas V. Falkie
President
Berwind Natural Resources Company

James R. Thomas II
Chairman
Carbon Industries, Inc.

C. Lynch Christian, Jr.
President
Imperial/Milburn Colliery Company

Enclosure
tive legislation.230 And, in a forcefully worded letter,231 the leaders of the

231. This letter is reproduced in its entirety:

Honorable Bob Packwood, Chairman
Committee on Commerce, Science,
and Transportation
United States Senate
Washington, DC 20510

Dear Senator Packwood:

The undersigned associations and organizations represent a cross-section of trucking companies, trucking employees, owner-operators, and motor carrier lawyers. We are united in our concern for the viability of the national transportation system and those it employs and the bleak prospects for the future absent a dramatic, prompt change in the regulatory policies and practices of the Interstate Commerce Commission.

In our view, the ICC thwarts the will of Congress and violates the law. In so doing, the ICC exacerbates the deteriorating condition of the trucking industry, contributes to unemployment, and fosters volatile, unlawful rate practices. The ICC refuses uniform administration and enforcement of the Motor Carrier Act of 1980. It has no discernible policy towards rates and entry, the two principal areas of its regulatory responsibility. We are convinced Congress must intervene now with strong affirmative action to compel the ICC to administer the statute in accordance with its terms and the intent of Congress.

Each organization signing this letter has its own individual complaints about the ICC's failure to administer the Act. The agency's non-enforcement impacts each group in different ways and in varying degrees. The major areas of dissatisfaction evolve from the following ICC practices, among others:

1. Condoning illegal, discriminatory rates;
2. Failing to adopt a comprehensive ratemaking policy;
3. Allowing virtual free entry without regard to public demand or carrier fitness; and
4. Suspending the common carrier duty to serve.

The ICC justifies its chosen path of administration, declining to exercise its statutory powers, with the facile bureaucratic cop-out: market-place forces are better regulators than Commissioners. We recognize Congress intended to increase competition. It did so, however, in a precise, controlled way. The Motor Carrier Act of 1980 eases entry barriers and adds flexibility to the rate-making freedom of the industry. It does not eliminate all regulation or relieve the ICC of its statutory responsibility to regulate in the interest of the public. The ICC's philosophy of non-regulation may support reductions in its annual operating budget, but it demonstrates a blatant disregard for the will of Congress.

Efforts by private parties in the courts to compel the ICC to carry out the intent of Congress have proven expensive, time-consuming, and therefore impractical solutions. Even when lawsuits are successful, the ICC subverts judicial directives by narrow construction or simple refusal to obey. In recent months, plaintiffs have had to return to court on two occasions to obtain 'writs of mandamus' to compel the ICC to adhere to the terms of the courts' prior orders.

The undersigned organizations individually have complained to Congress about the do-nothing policies of the ICC. Each group has testified before committees of the House and the Senate regarding the ICC's failure to administer the Act. The latest round of testimony occurred during the 1982 Oversight Hearings. Congress has heard our testimony, but present conditions continue unabated. The ICC finds solace if not encouragement in the passivity of Congress. The time has come for Congress to act and to act quickly with force and effectiveness to put the ICC back on track. If the ICC does not terminate its illegal regulatory posture, a viable national motor carrier system will be permanently damaged.

Each of us has a stake in the preservation of a viable national motor carrier system. We focus your attention on the current attitude and practices of the Commission which
American Trucking Associations, the Teamsters Union, the Motor Carrier Lawyers Association, the National Motor Freight Traffic Association, and the Owner-Operators Independent Drivers Association of America, strongly urged Congress "to act and to act quickly with force and effectiveness to put the ICC back on track." Like the tribes of Afghanistan, these organizations may agree on very little, save this: the identity of their common enemy (i.e., the deregulatory zealots who brought them economic chaos out of order), and their determination to drive this occupying army out of the nation's capital.

The time has come to reexamine the grand experiment in the eco-

jeopardize the system's survival in the hopes Congress will recognize the seriousness of the problem. We seek only fair, even-handed enforcement and administration of the Act. Let the chips fall where they may. Congress created the ICC to carry out its mandate as embodied in the Interstate Commerce Act, not to subvert the very statutory directives it is entrusted to enforce. By refusing to administer the Act, the ICC violates the Congressional trust; its expenditure of appropriated federal funds constitutes a fraud on the American public.

We look forward to your response to this letter. We request your advice on what congressional action would aid in compelling the ICC to administer the Act as Congress intended.

Sincerely,

THE AMERICAN TRUCKING ASSOCIATIONS, INC.
By (Bennett C. Whitlock, Jr.)

INTERNATIONAL BROTHERHOOD OF TEAMSTERS, CHAUFFEURS, WAREHOUSEMEN AND HELPERS OF AMERICA
By (Jackie Pressler)

MOTOR CARRIER LAWYERS ASSOCIATION
By (Harold D. Miller, Jr.)

NATIONAL MOTOR FREIGHT TRAFFIC ASSOCIATION, INC.
By (James Harkins)

on behalf of The Eastern
Central Motor Carriers Association, Inc.,
Central & Southern Motor Freight Tariff Association, Inc.,
Central States Motor Freight Bureau, Inc.,
New England Motor Rate Bureau,
Middle Atlantic Conference,
Middlewest Motor Freight Bureau,
Niagara Frontier Tariff Bureau,
Pacific Inland Tariff Bureau,
Rocky Mountain Motor Tariff Bureau, Inc.,
Southern Motor Carriers Rate Conference, Inc.

OWNER-OPERATORS INDEPENDENT DRIVERS ASSOCIATION OF AMERICA
By (Mark Perry)

See Truck Groups Complain to Congress About ICC's Administration of Act, TRAFFIC WORLD, July 4, 1983, at 47.
nomic theory of deregulation, for it seems not to have fulfilled the promises of its proponents. The time has come to compare marketplace performance since deregulation with the strong parallels which existed prior to regulation, lest we repeat an unfortunate history — a history from which our forefathers learned that responsible economic regulation of transportation was and is essential in order to protect the public interest.
Product Liability of the Aviation Component Part Manufacturer: A Proposal To Reduce Transaction Costs

VICTOR E. SCHWARTZ*

PATRICK W. LEE**

ROCHELLE M. GUNNER***

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I. INTRODUCTION

Despite the commonly accepted notion that product manufacturers are intimately involved in all phases of the production process, many products are, in fact, the end result of the discrete contributions of many producers. Modern technology and the development of increasingly complex products has caused specialization in the manufacturing process. It is common for a product to be made up of parts contributed by a number of different component manufacturers.

Aviation products are a prime example. Finished aircraft are made up of altimeters, engines, navigational instruments, electronic and hydraulic systems (in turn, made up of many independently produced components), and a variety of other products, none of which are manufactured by the aircraft manufacturer. While some of these parts are manufactured by part-makers who are engaged exclusively in the business of aviation, many are not.

Aviation component manufacturers have been faced with increasing numbers of product liability claims. In order to fund escalating damage awards, claimants are seeking greater numbers of defendants. The component manufacturer has been the target of this search.

With the exception of injuries caused by manufacturing defects in component parts, however, it is inappropriate for product liability law to treat an aviation component manufacturer as if he designed and produced a finished aircraft. Product liability is based upon the assumption that the manufacturer, as an expert in his field, has greater access to information regarding product safety than does the consumer and, due to this expertise, is in a better position to assess product dangers and to take steps to

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assure safety. Hence, the imposition of liability on product manufacturers is justifiable both as an efficient allocation of society's resources and as a means of deterring the introduction of unsafe products into the marketplace, by placing responsibility for those products upon those who are best able to assure their safety.

In the case of the component part manufacturer, however, these assumptions break down. First, unlike the product assembler, who is familiar with the end-use applications of the finished product, component part manufacturers most often are not experts in the end product. This is particularly true in the case of technologically advanced products such as aircraft. Where large numbers of component part-makers contribute distinct products to the finished aircraft, it is only the aircraft manufacturer who possesses the aviation expertise necessary to insure the production of a safe aircraft. In this situation, it is reasonable for the component part-maker to rely on the greater expertise of the assembler.

Second, component part manufacturers often lack information regarding the interrelationship of the component parts to each other and to the finished product. Manufacturer-assemblers rarely provide information to each component part-maker with respect to the functioning of the system as a whole; moreover, the component part manufacturer frequently is not expert enough in the end-use assembly operations to intelligently use such information effectively. Due to this lack of knowledge, component part manufacturers generally do not have the ability to foresee and assess product risks.

Third, even assuming that the component part manufacturer is able to identify product dangers, he often has no contact with the ultimate user of the product and no means of communicating with him. Unlike the assembler, his product is not distributed to the consumer in his own packaging or with his manual of labeling. Therefore, his opportunity to warn or instruct the ultimate purchaser of the product with respect to hazards and the proper use of the product is limited.

Finally, component manufacturers often manufacture their products to design specifications provided by the assembler or by a third party. Such specifications deprive the component manufacturer of a large measure of control over the design process itself. This serves to insulate him even more from the decision-making function generally performed by the product manufacturer.

The unique position of the component manufacturer renders the prod-

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2. See infra text accompanying notes 56-60 & 93-94.
3. See infra text accompanying notes 68-81 & 85-93.
4. See infra text accompanying notes 95-98.
5. See infra text accompanying notes 55-67.
duct liability system inappropriate for resolving questions of component part manufacturer design or warnings liability in most cases. Because he does not have involvement in or control of product design or marketing, he is usually not causally involved in accidents growing out of design or marketing defects. The principal result of continuing to impose the same standards of product liability on the component part manufacturer as on the assembler of the final product is to increase the costs of compensating injured persons. If the standards of liability are the same, the plaintiff can hardly be expected not to sue the component part manufacturer. In doing so, however, the plaintiff does not broaden the basis of recovery or make recovery more likely. The factual bases for liability — knowledge, control, expertise, ability to foresee and prevent harm—are generally not present, and the courts have recognized the unique position of the component part manufacturer by carving out ad hoc, fact-based exceptions to liability for that class of manufacturers.

In most product liability cases involving component part manufacturers the courts unnecessarily suffer the burden of multi-party litigation and defendant component part manufacturers are unnecessarily put to the cost of defense. This is a waste of legal resources and unreasonably increases the cost of compensating accident victims. The posture of the component part manufacturer is, in this respect, similar to that of wholesaler-distributors and retailers. The Senate Committee on Commerce, Science, and Transportation recommended in its report on S. 2631, a bill to create uniform standards of product liability law throughout the United States, that wholesaler-distributors and retailers be excluded from broad exposure to strict liability and that they be responsible only for harms caused by their own negligent conduct. The Committee recommendation is based on the resource waste and cost burden involved in unnecessarily subjecting wholesaler-distributors and retailers to product liability litigation. Keeping the wholesaler-distributor and the retailer in the product liability system is inefficient and unnecessary to injury compensation in most cases.

A similar adjustment of the product liability system is warranted in the case of component part manufacturers. Their presence in product liability lawsuits is usually not necessary for compensation of injured persons. Component part-maker cases generally involve the allocation of responsibility between the assembler and the component part manufacturer. This issue has little bearing upon the ultimate compensation of the injured victim; rather, it involves the economic allocation of resources between parties of

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6. For every dollar of claims paid an average of 42 cents is spent in defense costs. INSURANCE SERVICES OFFICE, PRODUCT LIABILITY CLOSED CLAIM SURVEY 11 (1977).
7. S. Rep. No. 670, 97th Cong., 2nd Sess. 39 (1982). If the manufacturer is out of business or cannot be reached by judicial process, the wholesaler-distributor and retailer would then have manufacturer liability.
similar, if not equal, bargaining power. Such issues are more properly dealt with by resort to negotiated contracts and insurance, which permits the parties involved in the manufacturing process to assign responsibility among themselves in accordance with the most efficient allocation of resources. Where there is a final assembler of the product subject to suit and able to respond in damages, the component part manufacturer should be removed from the operation of the product liability system except in cases involving its own fault. In suits against component part-makers, the standard by which the part-maker is judged should be a fault-based negligence standard.

In general, the allocation of responsibility between component part manufacturers and final assemblers should be addressed contractually. Where that is not possible and recourse to the courts is necessary, whether in a separate suit or as part of the underlying suit by the injured party, the component part manufacturer’s liability to the final assembler should be determined under negligence principles, not strict liability. The theory of strict liability is premised upon the assumption that the cost of redressing injuries from defective products should more properly lie with the manufacturer, who is better able to spread the risk among those who benefit from the product, than with the injured consumer. Where, however, the issue is not compensation but the allocation of risk between two commercial parties, i.e., the assembler and the component part manufacturer, strict liability is inapplicable because either party is equally able to perform the risk spreading function. Moreover, to the extent that strict liability is based upon the notion that liability serves to deter the manufacture of defective products, that notion is usually inapplicable to the component part manufacturer. He generally lacks the kind of knowledge, control, expertise and ability to foresee and prevent product risks, the essential predicate to the deterrence rationale.

Section II of this article will outline current theories of product liability as they have been applied to the aviation component manufacturer. Section III will review areas of product liability in which the courts have recognized the unique position of component part manufacturers. Finally, section IV will

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8. See Comment, Apportionment Between Partmakers and Assemblers in Strict Liability, 49 U. Chi. L. Rev. 544 (1982); Note, Airline Passenger's Lack of Privity Bars Implied Warranty Action Against Manufacturer of Defective Component Part But Not Against Assembler of Completed Airplane, 63 Colum. L. Rev. 1522 (1963). The former comment argues for the allocation of liability between the assembler and the component manufacturer on the basis of an assessment of who is the "cheapest cost avoider." While this approach is not unreasonable, it will generally be the case that the assembler is the cheapest cost avoider by virtue of his greater ability to learn of the hazardous condition and prevent it from occurring.


10. See infra text accompanying notes 51-54.
suggest proposed revisions to the product liability system which address the burdens on component part manufacturers and on the court system created by the present liability standards.

II. Theories of Liability Applicable to Component Part Manufacturers

Aircraft accident cases generally involve at least three parties: 1) an aircraft owner or operator, which in large commercial litigation is generally an airline; 2) the manufacturer of the aircraft, the assembler of the finished product; and 3) the manufacturer of a component part which is installed into the finished aircraft by the aircraft manufacturer. The liability of the component part manufacturer will, in almost all cases, be intimately related to whether the other parties to the manufacturing and design process performed their functions properly.\textsuperscript{11}

A. Negligence

Aviation component part manufacturers, like other manufacturers, are liable for failure to exercise reasonable care in the production of their products. If a component manufacturer’s lack of due care renders the product, or the finished product in which it is incorporated, unreasonably dangerous for use by consumers, and, if the product is the proximate cause of harm to a product user, the component manufacturer will be liable to the injured party.\textsuperscript{12}

Aviation component part manufacturers may be negligent in one of three ways: (1) they may negligently manufacture a particular product, thus

\textsuperscript{11} An aircraft manufacturer who installs component parts in its aircraft may, of course, be held solely liable for defects in those components. Boeing Airplane Co. v. Brown, 291 F.2d 310 (9th Cir. 1961) (aircraft manufacturer held liable for defects in alternator drive supplied by component manufacturer); King v. Douglas Aircraft Co., 159 So. 2d 108 (Fla. Dist. Ct. App. 1963) (aircraft manufacturer liable in action sounding in negligence and breach of warranty for design defect in engine supplied by component part manufacturer). See generally Ford Motor Co. v. Mathis, 322 F.2d 267, 273-74 (5th Cir. 1963); 1 L. Frumer & M. Friedman, Products Liability § 10.02 (1982) [hereinafter cited as Frumer & Friedman]. This principle has been followed in cases involving strict liability and breach of warranty claims. See, e.g., D’Antona v. Hampton Grinding Wheel Co., 225 Pa. Super. 120, 310 A.2d 307, 309 (1973) (strict liability); King v. Douglas Aircraft Co., 159 So. 2d 108 (Fla. Dist. Ct. App. 1963) (warranty). It is based on the thesis that “an assembler of a product . . . sells the completed product as its own and thereby represents to the public that it is the manufacturer.” King, 159 So. 2d at 110. Since the public does not distinguish between the assembler and the component manufacturer it is considered fair to hold the finished product manufacturer liable for defects in component parts which it incorporates into the final product.

\textsuperscript{12} See generally 1 Frumer & Friedman, supra note 11, at § 9.01; Restatement (Second) of Torts §§ 395, 396 comment m (1965) (“A manufacturer of parts to be incorporated in the product of his buyer or others is subject to liability under the rule stated in this Section, if they are so negligently made as to render the products in which they are incorporated unreasonably dangerous for use.”)
causing harm to the plaintiff;\(^{13}\) (2) they may negligently design an entire product line;\(^{14}\) or (3) they may negligently fail to provide adequate warnings and instructions to accompany their products.\(^ {15}\)

Even though a component part manufacturer has breached a duty of care to product users, no liability will arise where the component manufacturer’s conduct was not the proximate cause of the plaintiff’s injury. Because component products often pass through the hands of a number of parties before reaching the ultimate consumer, the intervening negligence of third parties is frequently an issue in component part cases. Where an accident is caused by the unforeseeable intervening negligence of a third party, the component part manufacturer will be absolved of liability if the intervening negligence is deemed by the trier of fact to be a “superseding cause.”\(^ {16}\)

**Goldsmith v. Martin Marietta Corp.**\(^ {17}\) is a good illustration. In that case Bendix, the designer of a fluxgate caging switch, was sued by survivors of deceased passengers who were killed when the switch was accidentally activated during flight, thus causing the pilot to receive incorrect directional information. Plaintiffs alleged that Bendix was negligent in failing to incorporate a guard in its design of the caging switch. They contended that the installation of a guard would have prevented the inadvertent activation of the switch, and thus would have prevented the ensuing crash. It was undisputed that the actual switch involved in the accident was neither manufactured nor installed by Bendix but rather was manufactured by an unknown party who “pirated” Bendix’s design.

The U.S. District Court for the District of Maryland held that Bendix was

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\(^{13}\) See, e.g., Carter Carburetor Corp. v. Riley, 186 F.2d 148 (8th Cir. 1951) (component part manufacturer’s negligent manufacture of fuel pump was proximate cause of crash).


\(^{15}\) Labelle v. McCauley Indus. Corp., 649 F.2d 46, 49 (1st Cir. 1981) (propeller manufacturer negligently failed to warn users directly of fact that rounding and polishing of propellers had not been performed); Braniff Airways Inc. v. Curtiss-Wright Corp., 411 F.2d 451 (2d Cir. 1969), cert. denied, 396 U.S. 959 (1969) (engine manufacturer negligently failed to warn of incidents of cylinder barrel separation after manufacture); Noel v. United Aircraft Corp., 342 F.2d 232 (3d Cir. 1964) (propeller manufacturer negligently failed to warn users of defects in propeller system).


\(^{17}\) Id. *But see* Fisher v. Bell Helicopter Co., 403 F. Supp. 1165 (D.D.C. 1975), in which a surviving police officer sued Avco, an engine manufacturer, after the helicopter in which he was riding crashed due to the fact that improper bolts were used in the construction of the engine. The helicopter was owned by the District of Columbia. Despite the fact that Avco issued a service bulletin recommending that the improper bolts be removed and replaced with shot-peened bolts, the District of Columbia, which was responsible for maintaining the aircraft, failed to comply with this recommendation. The Court held that the District of Columbia’s negligence was merely a concurring cause of plaintiff’s injury and thus refused to absolve Avco of liability to the plaintiff.
absolved from liability as a result of a number of intervening acts of negligence. The court stated:

First, if it was negligent of Bendix to design the switch without a guard, it was no less negligent for some unknown person to construct it without a guard. . . . Second, if the switch were actuated as the plaintiffs contend, whoever did so or permitted such to be done likewise was negligent. . . . Bendix is to be exonerated, not because it was not negligent, but because its negligence, if any, was superseded by that of the persons who constructed the switch and who actuated it.18

This case, though perhaps not typical, illustrates the relatively unique position in which component part manufacturers often find themselves. Due to the intervening acts of a number of subsequent handlers of the component part, it is often impossible for the part-maker to assure that its product reaches the ultimate user in a non-defective condition. Moreover, due to the part-maker’s lack of knowledge with respect to subsequent steps in the production process, he is frequently forced to rely on the assembler’s greater expertise in the specialized area to which the part relates in order to insure that the product is safe for its intended use.

The courts have gone farthest to expand the manufacturer’s duty of care to the injured consumer in the warnings field. Most time-of-sale warnings to aircraft purchasers are communicated by means of flight or instruction manuals or by cockpit placards. Such warnings, even though they are approved by the Federal Aviation Administration,19 invariably present jury questions as to adequacy of the communication.20 Once the adequacy problem is met, an aircraft user’s failure to follow the procedures specified in the manual is unforeseeable misuse.21

The problem for the component parts manufacturer in the warnings area is that he has no control over the method of conveyance, the words used, or any other element determining the adequacy of a communication. The component part manufacturer has little or no ability to control either the content or the mode of conveying required warnings or instructions. Certainly, an argument can be made that the part supplier should supply essential information to its purchaser, the aircraft manufacturer. In general, however, the law imposes no obligation to warn persons experienced or otherwise expert in a product,22 and the aircraft manufacturer, as an expert, may not be entitled to the warning that an inexpert consumer could expect.

The manufacturer’s duty to warn extends beyond the time of manufac-

22. See note 94 infra.
ture. When a manufacturer acquires new knowledge about the dangers of its product after the product has been manufactured and sold, it is under a continuing duty to warn product users of that danger.23

This has been a particularly significant obligation in aviation tort liability cases. In the aviation field, post-sale warnings from aircraft manufacturers, as opposed to component manufacturers, generally take the form of "service bulletins" or "service letters" to product purchasers informing them of new information acquired by the manufacturer subsequent to sale. In addition, the Federal Air Regulations require manufacturer to promptly report serious failures, malfunctions or defects to the FAA.24 This applies to component manufacturers who hold Parts Manufacturer Approvals and Technical Standard Order authorizations, as well as to aircraft manufacturers themselves. Failure to comply with these regulations can result in a finding of negligence as a matter of law in some jurisdictions.25 If the FAA determines, from a review of information submitted by the manufacturer, that the product defect is sufficiently serious to warrant FAA action, it may issue an "airworthiness directive" requiring modifications to the aircraft which will eliminate the unsafe condition.26

At this time it is frequently difficult, if not impossible, for the manufacturer to discover the identity of the owner of the product.27 This is particularly true for aviation component manufacturers, since aviation parts are frequently removed from one aircraft and transferred to another by the original purchaser without the component manufacturers' knowledge. The aircraft may then be sold to a number of subsequent purchasers, who may also alter or replace component parts.

B. Breach of Warranty

The Uniform Commercial Code is applicable to aircraft sales and has frequently been applied in actions involving component manufacturers. Under the Uniform Commercial Code, component part manufacturers may

25. E.g., Gatenby v. Altoona Aviation Corp., 407 F.2d 443 (3d Cir. 1969); Gas Service Co. v. Helmers, 179 F.2d 101 (8th Cir. 1950). In other jurisdictions such failure is admissible as evidence of negligence at trial. See, e.g., Neiswonger v. Goodyear Tire and Rubber Co., 35 F.2d 761 (6th Cir. 1929).
27. See Comment, supra note 23, at 54-58.
be liable for breach of warranty to their immediate vendees and to injured passengers.

Warranties created by a component manufacturer may be either express or implied. Express warranties arise by reason of a manufacturer's affirmative representations.\(^\text{28}\) No particular words are necessary and it is not essential that the manufacturer intend that its statement have the effect of a warranty.\(^\text{29}\) In the context of the aircraft manufacturing industry, such express warranties may arise from a manufacturer's representations of "airworthiness."\(^\text{30}\) Express warranties may also arise from affirmations contained in advertisements designed to induce someone to buy certain aircraft or component parts.\(^\text{31}\)

Implied warranties on the other hand, arise by operation of law. Under the Uniform Commercial Code, the warranties of merchantability and fitness for a particular purpose are implied in contracts of sale.\(^\text{32}\) The warranty of merchantability arises when the seller is a merchant with respect to the kind of goods sold.\(^\text{33}\) The warranty of fitness arises where a manufacturer has reason to know that the buyer is relying upon its skill and judgment to select or furnish suitable goods.\(^\text{34}\) As with breach of express warranty, a plaintiff must show reliance to recover for a breach of a warranty of fitness; a breach of the warranty of merchantability may arise in the absence of reliance.\(^\text{35}\)

Historically, component manufacturers who sold their products to air-

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28. The Uniform Commercial Code provides:
   (1) Express warranties by the seller are created as follows:
       (a) Any affirmation of fact or promise made by the seller to the buyer which relates to
           the goods and becomes part of the basis of the bargain creates an express warranty that
           the goods shall conform to the affirmation or promise.
       (b) Any description of the goods which is made part of the basis of the bargain creates
           an express warranty that the goods shall conform to the description.
       (c) Any sample or model which is made part of the basis of the bargain creates an
           express warranty that the whole of the goods shall conform to the sample or model.


30. See, e.g., Limited Flying Club v. Wood, 632 F.2d 51 (8th Cir. 1980) (seller's representations
    of airworthiness, based upon entries in logbook which set forth the repair and inspection
    history of the airplane, created an express warranty); Downs v. Shouse, 18 Ariz. App. 225, 501
    P.2d 401 (1972) (seller's description of aircraft maintenance, including a representation that the oil
    had been changed every 50 hours as recommended by the service manual, was an affirmation of
    fact constituting an express warranty).

31. But see Banko v. Continental Motors Corp., 373 F.2d 314 (4th Cir. 1966) (express warranty
    not breached when advertisement warranted freedom from carburetor or vaporization icing
    and accident caused by icing of throttle valve; manufacturer did not warrant freedom from all types
    of engine icing).

32. U.C.C. §§ 2-314 to 2-315.

33. U.C.C. § 2-314.

34. U.C.C. § 2-315.

35. U.C.C. §§ 2-314 to 2-315. See also 2 Frumer & Friedman, supra note 11, at
    § 16.04(2)[d].
craft manufacturers were insulated from liability to injured passengers and to aircraft owners on the theory that neither party was in privity of contract with the component manufacturer. Since the warranty was viewed as an incident of the contract of sale, persons not parties to the contract were not entitled to benefit from the warranties offered or implied thereunder. 36

The privity requirement, however, has been abolished. Since most modern express warranties arise from representations made in advertising and other related promotional material, courts have dispensed with the privity requirement on the theory that such material is, in fact, designed for the ultimate purchaser or user. 37 Similarly, the courts permit breach of implied warranty actions against component manufacturers by remote purchasers and by injured passengers or their representatives on the theory that the manufacturer is better able to distribute the risk than the injured passenger. 38 In addition, courts have frequently cited the difficulty of proving negligence as a basis for abolition of privity in breach of warranty actions. 39

There is still some authority for the proposition that aviation component part manufacturers will not be liable to injured passengers or to remote purchasers for breach of warranty. In Goldberg v. Kollsman Instrument Corp., 40 a wrongful death action was brought by the mother of a deceased passenger after an American Airlines flight crashed near La Guardia airport. Plaintiff named Lockheed Corporation, the manufacturer of the aircraft, and Kollsman Instrument Corporation, the manufacturer of the plane’s altimeter, as defendants. Plaintiff alleged that both manufacturers breached their respective implied warranties of merchantability and fitness. While the New York Court of Appeals had no hesitation in dispensing with the privity re-

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quirement and holding Lockheed liable for breach of implied warranty, the court declined to extend this rule to the manufacturer of the component part. The court found that adequate protection was provided for airline passengers by "casting in liability the airplane manufacturer which put into the market the completed aircraft."41

Even in New York, however, there are instances in which Goldberg does not apply. Where the injured plaintiff cannot recover from the manufacturer or assembler of the finished product, the component manufacturer may still be liable for breach of warranty. In Sevits v. McKiernan-Terry Corp.,42 an injured serviceman brought a claim against McKiernan-Terry Corporation for breach of implied warranty with respect to an engine manufactured by the defendant and sold to the U.S. Navy. Plaintiff was injured when the engine failed during an attempted landing aboard the U.S.S. Constellation. The U.S. District Court for the Southern District of New York, applying New York law, held that the plaintiff could recover against the component part manufacturer despite the holding of the New York Court of Appeals in Goldberg. The court distinguished the case from Goldberg, stating:

[In the instant case] the plaintiff has no right to sue the manufacturer of the entire ship since it is the United States Government, and being a member of the United States Navy, he is not in a position in this particular case to sue the Government on the theory of an implied warranty. Thus, if he is forbidden to sue the manufacturer of the component part . . . the theory of implied warranty which he has a right to assert under admiralty law would become entirely meaningless.43

What Goldberg and Sevits indicate is that when the courts address themselves to the unique position of the component part manufacturer vis-a-vis the assembler of the finished product, they do recognize that position as long as the injured party may recover from the assembler. In the absence of recovery against the assembler, however, the courts will not absolve the component manufacturer of liability to the injured consumer.

In sum, in most jurisdictions a component manufacturer may be sued for breach of warranty by all potential plaintiffs involved in an aviation accident, regardless of whether they are in privity of contract with the manufacturer. In New York, a component manufacturer may be insulated from such suits if the finished product manufacturer is subject to suit.

C. STRICT LIABILITY

At the time of the adoption of section 402A, the drafters of the Re-

41. Id. at 83.
43. Id. at 814.
statement were uncertain as to whether strict liability would apply to component part manufacturers. Comment q to section 402A states:

"In cases of the sale of a component part of a product to be assembled by another . . . the question arises, whether responsibility is shifted to the assembler. It is no doubt to be expected that where there is no change in the component part itself, but it is merely incorporated into something larger, the strict liability will be found to carry through to the ultimate user or consumer. But in the absence of a sufficient number of decisions on the matter to justify a conclusion, the Institute expresses no opinion on the matter."^44

Since the adoption of section 402A, many courts have applied the theory of strict liability to component part manufacturers. ^45 Aviation component manufacturers are no exception to this rule. ^46

It is often the case, however, that the component part undergoes substantial change before it reaches the ultimate consumer. In such cases, the courts have recognized that strict liability is inappropriate due to the fact that the plaintiff cannot prove that the component was defective when it left the control of the component part manufacturer. ^47 This is particularly true with aviation components, such as aircraft engines, which are frequently removed and re-installed in aircraft by airline personnel themselves, either for purposes of repair or replacement in new aircraft. Since the evidence does not establish the component manufacturer’s responsibility for the product defect, it is unfair to impose liability.

This point was made in Rossignol v. Danbury School of Aeronautics Inc. ^48 Plaintiff, the owner of an aircraft which was damaged when he attempted to perform a crash landing after its engines failed, brought an action for property damage to the aircraft. Plaintiff alleged that the accident was caused by a defective exhaust valve in one of the cylinders of the engine. Plaintiff named both Eaton Manufacturing Company, the manufacturer of the exhaust valve, and Avco Corporation, the manufacturer of the motor in which the valve was installed, as party defendants.

The Supreme Court of Connecticut held that plaintiff had failed to state a cause of action in strict liability against the various component manufacturers. Since the product had clearly passed through a number of hands, the court held that it was essential to allege that the product "was expected to and did reach the plaintiff without substantial change in condition in which it was sold." ^49 In the absence of such an allegation the court held

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44. Restatement (Second) of Torts, § 402A comment q (1965).
49. Id., 227 A.2d at 442.
that no cause of action would lie.

A number of rationales have been advanced for the adoption of strict liability. First, strict liability claims insure that the risk of injury from defective products will be borne by those persons who are best able to distribute the risk by insuring against it, rather than by the persons injured by product defects. Second, strict liability is presumed to have a deterrent effect upon product manufacturers by encouraging them to produce safer products. Finally, strict liability claims eliminate the necessity of proving negligence, which is often an insurmountable barrier to injured plaintiffs.50

These rationales do not apply where the issue involves apportionment of liability between an assembler and a component part-maker. Since, in most cases, both are substantial commercial entities, either party is equally able to spread the risk of loss. Moreover, unlike an injured consumer, a large commercial entity does not suffer from the difficulties traditionally associated with proving negligence. Such manufacturers generally have access to expert information which can ease the burden of proof. Finally, the deterrence rationale is equally well served by the law of contracts; component part-makers who are contractually liable to their immediate vendees for their defective products have the same incentive to produce safe products as the product liability system imposes. Insofar as the component part-maker suffers from incomplete knowledge and expertise, the deterrence rationale is improperly applied to him because there is little that he can do to increase the safety of a production process over which he exercises little control.

The courts have recognized these limitations on strict liability.51 In *Scandinavian Airlines System v. United Aircraft Corp.*,52 SAS brought an action against an engine manufacturer when two engines installed in aircraft owned and operated by SAS failed during take-off. One of the engines had been sold by United to McDonnell-Douglas, which installed it in its aircraft and sold it to SAS. The other engine was sold by United directly to SAS. With respect to both engines SAS alleged that United was strictly liable for the product defect.

In passing upon this question the Ninth Circuit held that SAS could not recover against United in strict liability due to the inappropriateness of that


52. 601 F.2d 425 (9th Cir. 1979).
theory to the apportionment of liability between commercial entities. The
court noted that where the two parties to the action are large commercial
entities, it is immaterial "whether the loss is thrust initially upon the manu-
ufacturer [United] or consumer [SAS], [since] it is ultimately passed on as a
cost of doing business included in the price of the products of one or the
other and thus spread over a broad commercial stream."53 Moreover, the
court noted that SAS had the necessary expertise, personnel, and technical
knowledge to identify product defects and to prove negligent design or
manufacture. Since at least one of the engines was sold to SAS directly by
United, SAS did not face problems of privity in bringing a breach of war-
ranty action.

Decisions similar to SAS are common.54 They indicate that the courts
will not mechanically apply strict liability doctrines without fully examining
whether the policy rationale for the doctrine is applicable in each individual
case. They demonstrate that strict liability is inappropriate in design and
warnings cases since they involve apportionment of liability between com-
ponent part manufacturers and assemblers.

III. THE UNIQUE POSITION OF THE COMPONENT PART MANUFACTURER

It is in the design and warnings areas where the inappropriateness of
product liability rules as applied to component part manufacturers is most
apparent. Attempts by the courts to exempt component part manufacturers
from the application of product liability rules by creating limited fact-based
exceptions have unnecessarily complicated product liability law and have
resulted in the piecemeal development of product liability law as it applies
to component part-makers.

A. DESIGN LIABILITY OF COMPONENT MANUFACTURERS

1. COMPLIANCE WITH SPECIFICATIONS

Component part manufacturers frequently manufacture their products
pursuant to specifications provided by the assembler of the finished prod-
uct. This is particularly true of aviation products, which are often designed
to comply with specifications provided by either the aircraft manufacturer in
the case of commercial aircraft, or by the government in the case of military
aircraft. In this context, the question frequently arises whether the compo-
nent manufacturer will be liable to injured persons for aircraft defects
caused by defective design specifications developed by a third party.

The rule is well established that, at least in the commercial context, a
component manufacturer who supplies a product in compliance with speci-

53. Id. at 428 (quoting Kaiser Steel Corp. v. Westinghouse Elec. Corp., 55 Cal. App. 3d 737,
748, 127 Cal. Rptr. 838, 845 (1976)).
54. See cases cited supra note 51.
fications developed by another will be absolved from negligence liability unless the defect in the design was so obvious that the component manufacturer knew or should have known of the defect. This rule is based upon the premise that the party who developed the design specifications is in a much better position than the component part manufacturer to recognize the risks associated with the product design and to incorporate safety features into the product. Not only is the designer familiar with the inter-relationship of the component parts to one another, he is also generally expert in the field to which the specifications relate, perhaps more so than the component part manufacturer. Therefore, it is not unreasonable for the component part-maker to rely on that party's expertise when fabricating the part for eventual incorporation into the finished product.

This premise has been repeatedly recognized by the courts. In Orion Insurance Co. v. United Technologies Corp., a helicopter pilot's estate brought suit against Amtel, the manufacturer of the helicopter's "stationary star," and against the Sikorsky division of United Technologies, which manufactured the helicopter. The plaintiff alleged that the star, which had been manufactured by Amtel to conform to the specifications provided by Sikorsky, was defective because it was too weak for its intended function. This weakness, they contended, ultimately caused the helicopter to crash. Plaintiff asserted that Amtel was liable in negligence and strict liability due to the design defect in the star.

In passing upon this claim, the U.S. District Court for the Eastern District of Pennsylvania noted that Sikorsky was in the business of manufacturing aircraft while Amtel was not. Consequently, absent an obvious defect in the design specifications provided by Sikorsky, it was reasonable for

55. With respect to strict liability, the courts differ as to whether compliance with specifications is a valid defense. Those courts that have upheld the defense in strict liability actions do so on the theory that section 402A of the Restatement requires that the manufacturer be responsible for product defects and, where the specifications have been provided by a third party, the manufacturer is not responsible for such defects. See note 56 infra.

However, some courts have refused to uphold the defense of compliance with specifications in strict liability actions on the theory that, since reasonable care is not an issue in such actions, all parties to the manufacturing and distribution chain should be held responsible for product defects. See, e.g., Lenherr v. NRM Corp., 504 F. Supp. 165 (D. Kan. 1980); Michalko v. Cooke Color & Chem. Corp., 91 N.J. 386, 451 A.2d 179 (1982). These courts will hold component part manufacturers strictly liable for compliance with defective specifications developed by another even where the component part manufacturer has no reason to know of the defect.


57. See note 56 supra.
59. Id. at 177.
Amtel to rely on Sikorsky’s plans. As the court stated, “Amtel was dealing not with specifications submitted by a consumer but by a business entity with superior knowledge in the field of aviation.” Consequently, the court refused to hold Amtel liable in either strict liability or in negligence for the defective design of the star.

Where the design specifications are provided by the government, as in the case of military aircraft, the component manufacturer’s right to rely on those specifications is less clear. Many suppliers doing business with the government have argued that compliance with government specifications should immunize them from tort liability. Most courts have rejected this argument. Thus, in *O’Keeffe v. Boeing Co.*, a New York federal district court decision, the court stated:

> There is no question, and the court so finds, that ultimate responsibility for the design and use of the [product] rests and always has rested with the United States government. The court concludes, however, that this fact, in itself, neither exonerates the defendant, nor has it in any way altered the defendant’s duty as a manufacturer in this case where there has been no showing that the defendant was totally oblivious of and/or aloof from the genesis of the design specifications in the first place or that the specifications represented either something less than the uppermost level of the art or a compromise of safety.

Even where the manufacturer pointed out an error in the government’s specifications and requested that they be changed, the manufacturer has been held liable for injuries caused by the product built to the defective specifications.

Some courts, however, have recognized the government specifications defense, including two recent and significant tort cases involving toxic products. In *In re “Agent Orange” Product Liability Litigation*, the U.S. District Court for the Eastern District of New York indicated that manufacturers who had supplied Agent Orange to the government would be permitted to assert a defense based upon compliance with government specifications provided they could demonstrate: (1) that the government established the specifications for Agent Orange; (2) that the Agent Orange manufactured by the defendant met the government’s specifications in all material re-

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60. *Id.* at 176.
64. 534 F. Supp. 1046 (E.D.N.Y. 1982).
pects; and (3) that the government knew as much or more than the defendants about the hazards associated with Agent Orange. The Court placed great emphasis upon the fact that the product had been supplied to the government for military use. The court indicated, however, that it was unsure "what if any protection a particular defendant’s subcontractor or supplier of component materials may have if that defendant successfully proves the government contract defense." Subsequent to this decision a U.S. district court in Washington permitted eight asbestos manufacturers to assert the government specifications defense despite the fact that the products were not produced for military purposes. The court did not rule upon the question of whether the defense could be asserted by component part manufacturers.

The government specifications defense is even more appropriately applied to component part manufacturers. Component part manufacturers compelled to meet defective government specifications lack even that minimal control over the production process which is associated with the manufacturer of the finished product. The component part-maker is generally several steps farther removed from the vendee of the final product. Therefore, he is in even less of a position to assess the suitability of those specifications than other manufacturers might be. Placing responsibility upon the component part-maker for defective design specifications supplied by the government therefore makes even less sense than placing such responsibility upon a supplier of a finished product.

2. Duty to Install Safety Features

Where the component part manufacturer does design as well as manufacture the component part, the issue of the part-maker’s liability for failure to install safety devices or systems frequently arises. The inquiry in these cases generally focuses on whether the duty to install safety features is more appropriately the function of the component part-maker or of the assembler. It is in this context that the courts have most frequently recog-

65. Id. at 1055.
66. Id. at 1056 (emphasis added).
68. There is some authority for the proposition that the assembler's obligation extends beyond the duty to install safety devices to an affirmative duty to develop safety devices. Noel v. United Aircraft Corp., 342 F.2d 232, 237 (3d Cir. 1964) (United was negligent in "permitting the development of an effective safety device . . . to lag behind similar development for other airplanes"). But see Braniff Airways, Inc. v. Curtiss-Wright, 411 F.2d 451 (2d Cir.), cert. denied, 396 U.S. 959 (1969) (in which the Second Circuit explicitly rejected the Noel holding but implied that the manufacturer may have a duty to remedy product defects which come to his attention after the product is sold). In Bell Helicopter Co. v. Bradshaw, 594 S.W.2d 519 (Tex. Civ. App. 1979) (writ denied), the Texas Court of Civil Appeals expanded upon the obligation to develop product improvements by holding that where a helicopter manufacturer does, in fact, develop safety improvements in its
nized the unique position of the component part-maker vis-a-vis the assembler insofar as his expertise, ability to assess product dangers and limits on foreseeability are concerned.

The leading case in this area is Verge v. Ford Motor Co. A sanitation department employee, who was injured when a fellow employee backed into him with a garbage truck, brought a strict liability action against Ford Motor Company, who manufactured the cab and chassis of the truck, and Elgin Leach Corporation, who modified the chassis by adding a compactor unit to it. The plaintiff contended that Ford had an obligation to include a warning buzzer on the chassis which would sound whenever the truck was put into reverse. In passing upon this claim, the Third Circuit listed three criteria which the court would consider in determining whether such design responsibility would properly be placed upon the part-maker or the manufacturer of the finished product. These criteria were:

1) trade custom — at what stage the device is generally installed;
2) relative expertise — which party is best acquainted with the design problems and safety techniques in question; and
3) practicality — at what stage is installation of the device most feasible.

The court then went on to hold that Ford could not be held strictly liable for failure to include a warning device on the chassis where the evidence revealed that Elgin Leach had much more expertise in the design of garbage trucks than Ford, and that the chassis in question was manufactured by Ford for multiple purposes, only one of which was its use as a component part in the manufacture of garbage trucks.

Following the decision in Verge, a number of courts have reached similar conclusions with respect to the component part-maker’s responsibility for the installation of safety devices. In Shawver v. Roberts Corp., an
employee of the Beloit Corporation suffered amputation of his right foot after it was crushed when a fellow employee mistakenly turned on a conveyor belt on which Mr. Shawver was standing. Shawver sued the Roberts Corporation in negligence and strict liability, alleging that Roberts was liable due to its failure to include a safety device on the conveyor which would have alerted Shawver to the imminent movement of the conveyor.

Despite the fact that the evidence adduced at trial indicated that such safety devices were available in the industry at the time the device was manufactured, the Supreme Court of Wisconsin refused to find Roberts liable. The court stated that the evidence showed that Roberts could not have designed an effective safety system for the conveyor in the absence of knowledge of the noise level, the lighting system, and competing signals on other equipment in the factory. Moreover, the court noted that since the electrical control system which powered the conveyor was not supplied by Roberts, Roberts had no expectation that the conveyor would reach the user without substantial change in condition.

In Shanks v. A.F.E. Industries, the Supreme Court of Indiana reached a similar conclusion. An employee of Grammer Elevator was permanently injured when a grain dryer automatically activated an elevator leg which the employee was repairing. The employee contended that A.F.E. was strictly liable for failure to incorporate a warning device in the dryer which would notify the user of the automatic activation of the machine. In rejecting this claim, the court stated:

Because the dryer could be used as a component in a multifaceted complex . . . to allow a jury to examine, in retrospect, the wisdom of A.F.E.'s incorporating some lights or bells into the dryer is to permit nothing more than speculation. A complex operation such as this one could have taken many forms, depending on the needs of the owner and the imagination of the designer. . . . The need for any warning device, and the circumstances surrounding their use, would, of course depend upon the operation of the whole complex, based upon the features of its design. Thus, because the dryer could be incorporated into a variety of grain handling systems, the desirability or need for such devices could be determined only after any given type of complex had been chosen and created.

Cases such as Shawver and Shanks demonstrate the severe limitations on foreseeability faced by component part-makers. Due to the part-maker's lack of expertise in the operation of the end-use assembly he is frequently unable to make an informed judgment with respect to the installation of appropriate safety devices. Moreover, the component part manufac-

72. 90 Wis. 2d 672, 280 N.W.2d 226 (1979).
73. Id., 280 N.W.2d at 229.
74. Id., 280 N.W.2d at 232.
76. Id. at 838.
urer is hampered by a lack of information with respect to the use to which the component part will be put and the environment in which it will function. This lack of knowledge severely limits his ability to foresee potential product dangers and install appropriate safety systems.

In view of these limitations, the courts have repeatedly refused to impose liability upon component manufacturers for failure to install safety devices. In so doing, they have looked to tort law to justify what are essentially fact-based conclusions. Thus, courts have stated that the part-maker had no duty to provide a safety device; that the part-maker’s duty was not breached; that the product did not reach the user without substantial change in condition; or that the lack of a safety device did not render the product unreasonably dangerous.

The true basis for these court holdings is that, insofar as liability must be apportioned between the component part-maker and the assembler, it makes sense to place liability upon the assembler in view of his greater expertise in end-use assembly applications, his greater familiarity with the environment in which the component part must function, and his consequent better ability to foresee product risks and to prevent them.

3. DESIGN SERVICES

In the area of design services, the courts have been equally reluctant to permit assemblers of finished products to delegate design liability to others. Where the assembler contracts with engineers, architects or other design professionals to prepare design specifications for the finished product or for a component part thereof, the designer may not be held strictly liable for the creation of a defective design.

In this area, the courts have recognized that the assumptions upon which strict liability is predicated are not applicable to the suppliers of design services. Unlike the situation in which products are mass produced

77. See note 71 supra.
81. Id.
and distributed to a multitude of users, design services are performed on an individual basis. Were the sellers of design services to be held strictly liable for defective performance of these services they would, in effect, be required to guarantee the result which they are commissioned to perform. This result would create a disincentive to the development of innovative design techniques and might, in fact, have a negative impact upon the availability of such services. In recognition of this fact, those courts which have addressed the matter have consistently held that those who hire experts can only expect reasonable care. As Justice Traynor stated, "They purchase service, not insurance."

B. WARNINGS

It is in the warnings area that the inappropriateness of strict liability in defining the responsibilities of component part manufacturers is most apparent. The doctrine of strict liability presupposes knowledge, expertise, the ability to foresee product risks and the opportunity to communicate them to the user. The component part-maker's unique position in the distribution chain prevents him, however, from acquiring the information necessary to assess product risks and impedes his access to channels of communication. Consequently, the courts have had difficulty rationalizing warning claims against component manufacturers and have most often absolved them of any warning obligation.

An essential prerequisite to the duty to warn is the knowledge or the ability to acquire knowledge of product hazards. With the exception of the recent decision of the New Jersey Supreme Court in Beshada v. Johns-Manville Products Corp., no court will hold a manufacturer liable for the failure to warn of product defects unless that manufacturer knew or should have known that the product was likely to become dangerous in the ab-

85. One who supplies directly or through a third person a chattel for another to use is subject to liability to those whom the supplier should expect to use the chattel with the consent of the other or to be endangered by its probable use, for physical harm caused by the use of the chattel in the manner for which and by a person for whose use it is supplied, if the supplier
   (a) knows or has reason to know that the chattel is or is likely to be dangerous for the use for which it is supplied, and
   (b) has no reason to believe that those for whose use the chattel is supplied will realize its dangerous condition, and
   (c) fails to exercise reasonable care to inform them of its dangerous condition or of the facts which make it likely to be dangerous.

RESTATEMENT (SECOND) OF TORTS § 388 (1965).

86. 90 N.J. 191, 447 A.2d 539 (1982). In Beshada, the New Jersey Supreme Court ruled that a manufacturer can be held strictly liable for failing to warn of a product hazard, even if the hazard is scientifically undiscoverable at the time of manufacture and sale.
sence of such a warning. 87

Component part manufacturers rarely possess the knowledge necessary to make an informed decision with respect to product hazards. Unlike the assembler, they are generally unfamiliar with the environment in which the component part will be required to function and they are generally unfamiliar with the interrelationship of their component and the other parts of the assembly. Consequently, they cannot foresee risks which may arise from the interrelationship of the component with other component parts in the use environment. Because they are generally not experts in the use to which the product will be put, they have no reason to know that product hazards may arise from the interaction of the component with other parts of the finished product.

The courts have repeatedly recognized these limitations on the component part-maker’s knowledge. 88 In Orion Insurance Co. v. United Technologies Corp., 89 the United States District Court for the Eastern District of Pennsylvania refused to hold Amtel liable for failure to warn United Technologies of defects in design specifications provided by United Technologies' Sikorsky division for a “star” used in the production of helicopters. The court stated that “assuming . . . that the star as constructed per the Sikorsky specification was inadequate for the purpose to which Sikorsky put it, there is no reason why defendant Amtel . . . should have known this.” 90 Sikorsky, not Amtel, the court noted, was an expert in the field of aviation.

In response to the plaintiff's claim that Amtel should have investigated the reason for Sikorsky's change of the alloy from which the star was made prior to the crash of the helicopter, the court held that the law does not impose a duty upon a component manufacturer to undertake an independent safety investigation. To impose such an obligation upon the component part-maker, the court held, would impede the free flow of commerce. The court stated:

[Component part manufacturers] would be forced to retain private experts to review an assemblers plans and to evaluate the soundness of the proposed use of the manufacturer’s parts. The added cost of such a procedure both financially and in terms of stifled innovation outweighs the public benefit of giving plaintiffs an additional pocket to look to for recovery. . . . [T]he better view is to leave the liability for design defects where it belongs and where it now is — with the originator and implementer of the design — the assembler.

50 Ohio St. 2d 317, 364 N.E.2d 267 (1977); Shawver v. Roberts Corp., 90 Wis. 2d 672, 280
N.W.2d 226 (1979).
90. Id. at 177.
of the finished product.91

Similarly, in Temple v. Wean United, Inc.,92 the Supreme Court of Ohio refused to hold a manufacturer of operating buttons, which were installed on a punch press, strictly liable for failure to warn the punch press operator of their danger in the absence of safety guards. The court stated:

In our opinion, the obligation that generates the duty to warn does not extend to the speculative anticipation of how manufactured components, not in and of themselves dangerous or defective, can become potentially dangerous dependent upon the nature of their integration into a unit designed and assembled by another. Because of limited contact with [the assembler of the finished product], there is no indication that [the manufacturer of the components] could have known that its components were to be fashioned or fabricated into the power press in the particular manner that they were here.93

Even where the component manufacturer has knowledge of potential product hazards, he often has no reason to believe that his immediate purchaser does not realize the dangerous condition. Unlike the assembler of the finished product, component manufacturers generally sell to experienced users. If the product assembler has not actually supplied the design specifications for the component part, he is most often experienced in the use to which the component is put in the finished product. Moreover, particularly in the context of highly technical products such as aircraft, the assembler-purchaser is often a large industrial concern with its own engineering department and its own safety programs. In this context, the component part manufacturer's duty to warn never even arises because, as one court stated, "a duty to warn exists only when those to whom the warning is to be communicated can reasonably be assumed to be ignorant of the dangers to which the warning relates. If it is unreasonable to assume they are ignorant of those facts, there is no duty to warn."94

Finally, there are numerous practical problems which arise with respect to warnings given by component part manufacturers. First, it is often difficult to identify to whom the duty to warn runs in a component part-maker case. Unlike the assembler of the finished product, component part-makers frequently sell to intermediate vendees who are often several steps removed from the ultimate user of the product. For this reason the component part-maker should have no responsibility to warn the ultimate

91. Id. at 178.
93. Id., 364 N.E.2d at 272.
user of the finished product.\textsuperscript{95} Aside from the fact that it often has no means of identifying the ultimate user at the time the component is sold to the assembler, it is also generally the case that warnings given to the ultimate user will rarely serve the purpose for which they are intended due to the highly technical nature of the products in which component parts are generally incorporated.

This is particularly true in the aviation area, as is illustrated by \textit{Stevens v. Cessna Aircraft Co.} \textsuperscript{96} The estate of a deceased passenger brought a claim against Cessna, the aircraft manufacturer, alleging that the aircraft was defective due to the failure of the manufacturer to post a warning to passengers with respect to the plane’s load capacity. The aircraft had crashed as a result of the pilot’s inaccurate calculation of the carrying weight. The plaintiff alleged that if the aircraft had contained a sign warning of the aircraft’s load capacity, one of the passengers would have realized the pilot’s error and the accident would have been averted.

In rejecting this claim, the California Court of Appeals indicated that warnings directed to the aircraft passenger would not have performed their intended function. The court stated:

> Whether the plane can fly safely with a given total weight of passengers depends upon too many additional factors for a passenger to make an informed and intelligent judgment from such a notice. . . . . In the airplane situation, the passenger necessarily depends upon the skill and judgment of the pilot to determine the load capacity of the airplane in light of the flying conditions to be encountered. . . . It would be impossible ultimately to provide meaningful information to the passenger, and in the long run a rule requiring the manufacturer to provide such information directly to the passenger would not be in the interests of safety.\textsuperscript{97}

It is equally inappropriate to require component part-makers to warn persons other than their immediate vendee of product hazards. Unlike assemblers of finished products, component part-makers generally have no practical mode of communication with anyone other than their immediate vendee and no means of acquiring access to them. While the assembler’s product is generally distributed in its own “packaging” for which it may supply appropriate labeling, the component manufacturer does not have an equivalent means of communication at his disposal.\textsuperscript{98} In fact, often the

\textsuperscript{95} Basko v. Sterling Drug, Inc., 416 F.2d 417 (2d Cir. 1969); Sterling Drug, Inc. v. Yarrow, 408 F.2d 978 (8th Cir. 1969); Sterling Drug, Inc. v. Cornish, 370 F.2d 82 (8th Cir. 1966). \textit{But} see Labelle v. McCauley Indus. Corp., 649 F.2d 46 (1st Cir. 1981) (a component manufacturer, who notified repair stations of a defect in its propeller blade and revised its service manual accordingly, was negligent because it failed to warn aircraft owners directly of this condition).


\textsuperscript{97} Id., 170 Cal. Rptr. at 926.

\textsuperscript{98} See Jones v. Hittle Serv., Inc., 549 P.2d 1383, 1394 (Kan. 1976) (“[T]he bulk wholesaler has no way of telling who the ultimate purchaser might be, and has no package on which to endorse any warning”); Hill v. Wilmington Chem. Corp., 156 N.W.2d 898 (Minn. 1968).
immediate vendee is the only party who has knowledge that the component part manufacturer has contributed to the finished product. Therefore, it is generally impractical to impose far-reaching warning obligations upon the component manufacturer when the assembler has both the information and the means available to communicate effective warnings to the product user.

IV. A PROPOSED REVISION OF PRODUCT LIABILITY FOR THE COMPONENT PART MANUFACTURER

The foregoing discussion suggests that to the extent the component part manufacturer is subject to the product liability system his liability in design and warnings cases should be determined by a negligence standard. The severe limits placed upon the component part manufacturer by virtue of his place in the distribution chain, in terms of his ability to foresee and assess product hazards and to introduce system safeguards, simply renders the concept of strict liability inappropriate to him. This is particularly true for the component part manufacturer who participates in a highly technical industry, such as aviation, in which he cannot be expected to intelligently assess product dangers associated with the technologically complex final product and exercise the necessary control to avoid them.

Moreover, strict liability is not appropriate when applied to the allocation of responsibility between two commercial parties in relatively equal bargaining positions. Not only is each party equally able to spread the risk of loss through insuring against it, but large commercial parties do not face the same problems of proof in negligence cases as injured consumers face. They generally have access to the expertise required to determine and prove the cause of a product-related accident. Insofar as strict liability is based upon the notion that it will serve to deter the introduction of unsafe products into the marketplace, that notion is inapplicable to the component part manufacturer since he generally lacks the kind of knowledge, control, expertise, and ability to foresee and prevent product risks which is the predicate to the deterrence rationale. Moreover, deterrence is equally well served by negligence liability and the application of principles of contract law to the component manufacturer.

At the present time, due to the uncertainties created by the product liability system, assemblers and component part manufacturers often choose to allocate the risk of loss by contract.99 Devices such as disclaimer clauses,100 limitations on liability, liquidated damages clauses, or

99. It is generally the case that assemblers and part-makers operate under some sort of contractual arrangement with one another. Although the contracts may not always be formalized and strictly negotiated, the exchange of forms that takes place between the parties and the oral promises which are made in the course of commissioning the work become part of the basis of the bargain under which the parties subsequently operate.

100. See generally 2 FRUMER & FREDMAN, supra note 11, at § 16.04[2][e]; Metzger, Disclaim-
hold harmless clauses all serve that purpose. For example, under a hold
harmless clause the component part manufacturer may agree to indemnify
the assembler for all injuries arising out of manufacturing defects in the
component part.

The courts have often recognized that there are significant policy rea-
sons for upholding such devices when they are agreed to by commercial
parties of approximately equal bargaining power. 101 In addition to the fact
that such clauses enable manufacturers to allocate the risk of loss of prod-
uct defects at the outset of a transaction, they also effect a reduction in the
uncertainties associated with product claims and a consequent reduction in
costs. Such cost reductions ultimately inure to the benefit of the consumer.

To the extent that the component manufacturer and the assembler
have not allocated the risk of loss, a system which recognizes the unique
position of component part-makers in the distribution chain by eliminat-
ing strict liability claims against them in design and warnings cases, will contrib-
ute substantially to the reduction of transaction costs caused by the present
complexities and uncertainties in the law. The consequent conservation of
judicial resources will benefit the judicial system, the component part-maker
and, ultimately, the consumer.

101. Airlift Int'l, Inc. v. McDonnell-Douglas Corp., 685 F.2d 267 (9th Cir. 1982) (exculpatory
clause prevented recovery in negligence against aircraft manufacturer and component manufac-
turer); Aeronaves de Mexico, S.A. v. McDonnell-Douglas Corp., 677 F.2d 771 (9th Cir. 1982)
(exculpatory clause upheld to prevent negligence claim against both aircraft and component manu-
facturers); S.A. Empresa (Varig Airlines) v. Boeing Co., 641 F.2d 746 (9th Cir. 1981) (exculpatory
clause prevented airline from recovering for post-delivery negligence of aircraft manufacturer); To-
clause barred both pre- and post-delivery negligence claims by airline against aircraft
manufacturer); Delta Air Lines, Inc. v. McDonnell-Douglas Corp., 503 F.2d 239 (5th Cir. 1974)
(exculpatory clause absolved aircraft manufacturer of liability to airline in strict liability and
negligence); Islamic Republic of Iran v. Boeing Co., 15 Av. Cas. 18,189 (W.D. Wash. June 2, 1980)
(broad disclaimer clause precluded aircraft owner from asserting negligence and strict liability
claims); Scandinavian Airlines Sys. v. United Aircraft Corp., No. CV 74-2609-DWW, slip. op. (C.D.
Cal. Dec. 4, 1975), aff'd, 601 F.2d 425 (9th Cir. 1979) (exculpatory clause barred negligence, strict
liability and breach of warranty claims by airline against aircraft manufacturer); Saturn Air-
clause barred negligence claims by airline against aircraft manufacturer). But see Sterner Aero
AB v. Page Airmotive, Inc., 499 F.2d 709 (10th Cir. 1974) (disclaimer clause would not bar strict
liability action).