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The Ties that Bind: Railroads, Coal, Utilities, the
ICC, and the Public Interest

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I. Introduction

During the past century, a symbiotic relationship has developed be-

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tween coal producers, railroads, and major consumers of coal, principally the steel and electric utility industries. Coal has provided many railroads with a fairly stable base load of traffic which could absorb much railroad overhead. Even if these bulk shipments were not always as profitable to the railroads as some other, more valuable shipments on an individual basis, coal did provide a steady, dependable flow of high volume, easy to handle, fairly remunerative traffic.¹ Traditionally, when coal faced severe competition from other energy sources, the railroads would forego rate increases on coal, minimize increases, or even lower rates in an effort to keep the mines operating (and, of course, minimize erosion of their base load traffic).² Naturally, carriers and producers did not always agree on transportation rates and there have been many complaints over the years from coal producers and others that railroads were charging excessively high rates and thus were stifling attempts by coal companies to expand their production. Concerns about service quality also have been voiced. For the most part, however, the system worked as smoothly as possible in an uncertain world, given the often depressed financial conditions of both the railroads and the coal industry.

The consumers of coal also benefited markedly from this relationship. Fairly low rail rates, reasonably steady and consistent service, and low coal prices brought about by competition from other fuels such as natural gas, oil and, more recently, nuclear energy all combined to encourage the use of coal for the generation of electricity as the most cost efficient method. Into the late 1970's, some electric utilities were using coal to generate practically all of the electricity they produced.³ Although these outside forces combined to keep coal from being a consistently profitable commodity for the producer and a panacea for the financial problems of the railroads, the relationship which evolved did keep the railroads in the coal business and did prevent the destruction of the coal

¹ The Chessie System Railroads, major eastern haulers of coal moved 16,270,000 tons of coal, 2,377,000 tons of coke, and 6,771,000 tons of iron ore in 1981; 12,605,000 tons of coal, 2,146,000 tons of coke and 2,962,000 tons of iron ore in 1982, and 15,257,000 tons of coal; 3,081,000 tons of coke; and 5,711,000 tons of iron ore in 1983 (estimated). Norfolk Southern, another major hauler of coal, had 1983 revenues from coal in excess of $1,300,000,000. Much of this coal moves in easy-to-handle, unit trains, often with utility provided equipment. Increased Rates on Coal—Louisville & N. R.R., 362 I.C.C. 369, 411 (1979).


³ The Southern Electric System, one of the largest-investor owned electric utilities, encompassing parts of Georgia, Alabama, Mississippi and Florida, was 94% dependent on coal for fuel in 1978, with oil and gas supplying peak load energy only. Increased Rates on Coal, supra note 1 (verified statement of James Small).
industry, which aided power companies in their attempts to meet the growing demands of society for more low cost electricity.

During the 1970's, with the advent of the "energy crisis" and the dramatic price increases for competitive fuels, coal prices also rose substantially in compliance with economic law, and many coal producers were able to benefit handsomely, especially those which controlled the relatively "clean" coal demand by many users due to the environmental initiatives of recent times. Many producers and consumers began complaining to the Interstate Commerce Commission (ICC) that their sales and use of coal were constrained by unresponsive, slow rail service and asked for regulatory relief. This increased demand also presented a major opportunity for the railroad industry, still reeling from the Penn Central fiasco and ever growing financial problems, to use coal as a vehicle for regaining reasonable profitability. Loosened regulation by the Commission, coupled with recognition by the Commission and Congress that the entire rail system could follow the northeastern railroads into bankruptcy if steps were not taken to increase revenues, gave the railroads a golden opportunity to increase coal rates by much higher percentages than the rate increases for most other commodities. Coal rate increases of up to forty percent were filed by various railroads, and were justified to the ICC as being necessary to improve carrier profitability, to make coal pay its "fair share," and to enable the carriers to make improvements in service (new track, extra engines, etc.) necessary to meet the growing demand for coal transportation. The recognition of railroad revenue needs, the strengthening market for coal, and the often "boom or bust" nature of the coal industry made these arguments attractive to the Commission, which began justifying coal rate increases on the grounds of overall railroad revenue needs and as being necessary to upgrade railroad operations to meet the increased demands of coal producers and users.

Not surprisingly, this turn of events brought howls of protest from the coal industry, which had grown accustomed to stable coal transportation rates, or even rates that had been falling in real, inflation adjusted terms. As the transportation costs of some coal (especially that produced in the West) began exceeding the price paid the producer and as escalating

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4. See, e.g., Assigned Cars for Bituminous Coal Mines, 346 I.C.C. 327 (1974). In other instances, the ICC has ordered such equitable remedies as transferring locomotives from one carrier to an affiliated carrier in order to alleviate coal transportation problems.

5. See, e.g., Increased Rates on Coal, supra note 1, (an unusually large, but pathbreaking case in which the railroad requested a 38% rate increase on all originated coal shipments).


7. Increased Rates on Coal, supra note 1, at 412-17.
transportation costs continued pushing up the delivered cost of coal, electric utilities and others with large fixed investments in coal burning generating facilities and access to only one source of transportation became very concerned about the high costs they were being forced to pass on to their customers and the possibility of seemingly endless future increases with no competitive checks in place. In effect, electric utilities, which price their product on the basis of cost plus reasonable return on investment, expected the same consideration from the regulated railroads and the ICC in their approach to railroad costs and rates. This traditional pricing policy eroded rapidly, much to the dismay of the power companies. Long-term coal supply constraints, coupled with the ICC’s traditional refusal to allow users or producers to make binding long-term contract agreements with railroads (now reversed\(^8\)), left the electric utilities without immediate weapons to combat the increases. They were locked into expensive plant sites and long-term coal supply agreements, with one mine contracted to produce coal for the facility. Their transportation alternatives were often inadequate or non-existent, but the sole transportation provider—the railroad—had power to alter rates, seemingly at will and unchecked by regulatory constraints.

For producers, the results were much the same, with those companies having access to only one railroad (and no alternatives, such as barges) often finding their competitive position weakened vis-a-vis their competitors who had access to transportation alternatives. No longer could a producer mine coal with the assurance that railroad rates would not put a particular mine or company at a competitive disadvantage in this very competitive market. Transportation had to be factored into the equation, but it was too late to do anything about contracts, agreements and investments that had been entered into before the railroads were given increased flexibility concerning coal rate increases. Clearly, the symbiotic relationship that existed for so long had fallen apart. Each element—user, producer, and transporter—still was dependent on the others, which muted much open hostility, but the degree of animosity and antagonism, not to mention law suits and other actions, appeared to reach new highs.\(^9\)

In effect, the railroads, producers, and users had dramatically differing views of the role of a railroad in the coal business. For the producers and users, the railroad’s role was seen as primarily passive. It should set its rates at a level which allowed for a reasonable return on its coal related investment and recoupment of all its coal related costs, including pro rata

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9. In the early 1970’s, the Southern Electric System participated in only two transportation-related law suits involving railroad rate levels. By the end of the 1970’s, the average had become three per year by this author’s estimate.
shares of overhead and so on. Once supply and demand for the overall market in question determined an equilibrium selling price for coal, individual producers were free to choose to provide coal at that price, based on whether production costs plus the set railroad rates were equal to or less than the delivered price at which the coal could be sold. While competitive economic theory suggests that, in the long run, all existing companies will end up at a position in which production costs plus transportation costs equal the equilibrium price of the commodity, the long run infrequently occurs.

In the short run, differences often exist between various companies. This could occur due to the company's location, the quality of its coal, its bargaining ability with labor or landowners, or any number of factors which lower its production costs in the short run below those of its competitors. This fortunate company would make an above average profit or economic surplus. Likewise, some coal companies will have higher production costs and will be able to participate in the coal market only if they are willing to accept a loss. Transportation costs remain basically the same for all similar companies, even though this means that some will choose not to ship coal and that others will make a substantial profit on their shipments. In this passive role, transportation costs represent a relatively fixed and constant component of the delivered price of coal. The railroad operates effectively risk-free, making a reasonable return (based on what is common for other industries) on all the coal it transports while the producer, which is not guaranteed a positive return, is free to benefit handsomely if it has been shrewd or to lose substantially if it has not been. The producer is the risk-taker and the recipient of "excess" profits if it could keep its costs below those of its competitors or produce a better product, while the railroad would receive a certain, but limited, profit on each haul.

The railroads, however, have now placed themselves in a much more active role. While their profit may be assured on individual movements, they argue that they still are harmed somewhat by the "bust" phase in a coal cycle and should benefit more from the "boom" phase, even though much coal now moves pursuant to minimum annual volumes in unit trains (which are immune from the "bust" cycle).\textsuperscript{10} They have occasionally lowered rates in the past in an effort to keep the mines operating, and claim that they generally have kept coal rates at low levels.\textsuperscript{11}

\textsuperscript{10} A "unit train" is a regularly scheduled movement in which the same cars continually shuttle between one destination and one origin carrying only one commodity. Often the cars are owned by the shipper rather than the railroad. A typical unit train might consist of 100 hopper cars, each carrying 100 tons of coal.

\textsuperscript{11} See supra note 2. Many railroads often note that in the past, coal rates have been raised by lower percentages than rates on other commodities during general increase proceed-
They have a larger stake in the coal industry than they do for most other commodities they haul, accept the risk of standing ready with massive investments in track and equipment to move whatever coal they are asked to transport, and therefore make less money when coal is economically unattractive and fails to meet expectations.\(^{12}\) Thus, the railroads argue, it is only reasonable that they should share in the increased profits that accrue to the industry when times are good, and not be limited to a fixed, fairly modest rate of return on coal movements, especially as they believe that higher returns are necessary for coal traffic in order to compensate them for revenue shortfalls from other traffic which does not pay its full cost. To accomplish this, the railroads desire to charge profitable coal producers a higher than normal rate, thus absorbing some or all of the extra profit these producers would have been able to earn due to their above average efficiencies. The increased economic return that would have accrued to the owner of company due to its business acumen, or luck, would now belong to the railroad, leaving the company with a lower return, but still enough to stay in business.

Expressed slightly differently, this is market segmentation or the consumer surplus problem.\(^{13}\) Referring to the graph below, let \(P_1\), represent the price of any given commodity such as railroad services traditionally sold at a fixed price. Some users would be willing and able to pay more than is asked of them (D and E). Some others would not use the service if the charge were increased (F). Still others do not use it at all (G) because of its cost. In other words, various customers derive different benefits from the same service. They will use the service only so long as its benefits exceed its costs. If the price of rail services were increased from \(P_1\) to \(P_2\), D would still utilize the services, while E, F, and G would now find it unprofitable to do so. If the railroad were to lower its price to \(P_3\), E and D would use its services, but the railroad would be giving up the right to charge D the higher price (\(P_2\)) that it would be willing to pay. In so doing,

\(^{12}\) This begs the question whether the costs associated with transporting coal have gone up less than for other commodities (due to unit trains, customer provided equipment, and other innovations) during the same time period.

\(^{13}\) More formally, the railroad uses the consumer's surplus to engage in second-degree price discrimination. See, e.g., F. SCHERER, INDUSTRIAL MARKET STRUCTURE AND ECONOMIC PERFORMANCE (2d ed. 1980).
the railroad would be giving up the revenue it could receive if it could tailor its prices to approximate the maximum each customer would pay. The total potential revenue the railroad is giving up when it charges $P_1$ is represented by the triangle $P_1P_2F$, and is often called the consumer surplus, or benefit that consumers receive from a service above what they are required to pay for that service. Businesses often try to capture that surplus for themselves by resorting to market segmentation—i.e., offering reduced fees to targeted persons and higher fees to other segments (business travelers versus tourists on airplanes) or by status symbols (polo ponies and alligators on shirt pockets versus plain pocket shirts made of precisely the same material).

When seen in the context of consumer surplus, the question confronting policy makers is whether railroads are passive entities which should accept a fairly fixed return on coal operations, or whether railroads should be able to attempt to capture some or all of the consumer surplus (the benefit that the railroad confers on the producer of coal beyond what the railroad routinely charges) when it exists. If railroads are allowed to capture some of this consumer surplus and, in effect, share in the good fortune or business skill of the coal producer or receiver, should the railroads also be required or expected to lower rates and return on investment from the producers and receivers when the consumer surplus no longer exists (i.e., coal prices are near production costs), as is currently the case?

Congress and the ICC have been grappling with these issues, although typically they have been expressed somewhat differently. For the most part, the arguments have focused on the amount of freedom
from regulation which should be given to railroads, especially when "captive" traffic is involved, and the definition of what traffic is actually captive to the railroads. The unstated assumption has been that additional rate freedom would give the railroads the ability to capture part of the consumer surplus, and that the railroads would act accordingly, thus eliminating many of their financial problems. In the remainder of this article, the decisions of Congress and the Commission relating to these issues will be analyzed and the implications of these decisions discussed.

While both Congress and the ICC have taken many actions during the past decade or so in an attempt to restore financial health to the ailing railroad industry, this article will focus solely on the principal actions that affect the carriers' ability to set rates in a flexible manner and potentially capture some or all of the available consumer surplus. Furthermore, this article will examine how these efforts have altered and may continue to alter the fortunes of industries that rely heavily on railroad transportation and are precluded, for a variety of reasons, from shifting to a competitive alternative. While several industries could fit into this category, large segments of the coal industry clearly do. As Congress and the ICC have singled out coal for special attention because of the possibility of abuse of railroad monopoly power due to the "captive" nature of this freight, the effects of the new legislative and regulatory policies on coal and coal transportation will be the centerpiece of this article.

II. LEGISLATIVE AND REGULATORY ACTIONS

In response to the new railroad provisions of the Railroad Revitalization and Regulatory Reform Act of 1976 \textsuperscript{14} (4R Act) and the Staggers Rail Act of 1980,\textsuperscript{15} the ICC began allowing railroads much greater freedom to increase all of their potential revenues, but much of the controversy arising from these actions has centered around coal policy, specifically because of the captive shipper problem. While there have been many individual cases involving particular railroads, utility facilities, and coal producers, the ICC, in several recent major policy pronouncements, has set the course for coal transportation in this country for the foreseeable future—Ex Parte No. 353, \textit{Adequacy of Railroad Revenue (1978 Determination)};\textsuperscript{16} Ex Parte No. 393, \textit{Standards for Railroad Revenue Adequacy};\textsuperscript{17} Ex Parte No. 338, \textit{Standards and Procedures for the Establishment of

\textsuperscript{16} 362 I.C.C. 199 (1979).
Adequate Railroad Revenue Levels;¹⁸ Ex Parte No. 320 (Sub-No. 2), Market Dominance Determinations and Consideration of Product Competition;¹⁹ Ex Parte No. 347 (Sub-No. 1), Coal Rate Guidelines—Nationwide;²⁰ Ex Parte No. 346 (Sub-No. 7), Railroad Exemption—Export Coal;²¹ and Docket No. 38754, Arkansas Power & Light Co., Petition to Institute Rulemaking Proceeding—Implementation of Long-Cannon Amendment to the Staggers Rail Act.²² In this section, the treatment of coal under these decisions and their underlying legislative provisions will be discussed.

A. REVENUE ADEQUACY

1. DETERMINING REVENUE ADEQUACY

   With passenger service and the Penn Central already burdening the taxpayers, and with it becoming increasingly clear that overregulation by the ICC had hamstrung railroad efforts to improve profitability and lower costs, Congress passed the 4R Act, a somewhat indecisive sounding measure, which appeared to loosen a few regulatory constraints on the railroads. For purposes of this paper, the Act’s most important provision directed the ICC to aid the railroads in achieving revenue adequacy, which was defined as revenue:

   adequate, under honest, economical, and efficient management, to cover total operating expenses. . . . plus a fair, reasonable, and economic profit or return (or both) on capital in the business, (with such revenue levels to) provide 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, . . . cover the efforts of inflation in amounts adequate to provide a sound transportation system in the United States.²³

   From this, it was clear that the revenue needs of railroads would take on increased prominence in ICC deliberations. This provision was tempered, however, by Congress’s expressed concern that carriers not use the need for revenue adequacy as an excuse or rationale for obtaining monopoly profits from shippers and receivers which had no competitive transportation alternatives. One provision which showed this concern was the “market dominance” section of the Act, which maintained ICC jurisdiction over the reasonableness of rates in the “absence of effective

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²⁰ Coal Rate Guidelines—Nationwide (I.C.C. served Feb. 24, 1983) [hereinafter cited as Ex Parte No. 347].
²² 365 I.C.C. 983 (1982).
competition from other carriers or modes of transportation." In effect, this provision was analogous to what an economist would call "inelastic demand for transportation services" and recognized that some shippers simply have no choice but to pay whatever price a carrier chooses to charge when there are no available competitive transportation sources and no products which can be substituted for the one that comes via rail. A wheat farmer in North Dakota, a coal mine, or an electric utility generating plant could be examples of "market dominant" traffic or "captive" shippers as defined by the Act. A nearby navigable river, trucking feasibility, or many other factors could, of course, vitiate the seemingly captive position of a given shipper.

The other crucial change espoused by the 4R Act was its reliance on competition, rather than ICC fiat, to set transportation policy whenever possible. Given the record of the ICC, this change was understandable. Section 207 gave the ICC authority to exempt railroad transportation or services from regulation if regulation would:

1. not be necessary to carry out transportation policy;
2. be an unreasonable burden on the railroads; and
3. serve little or no public purpose.

Four years later, the Staggers Act amended this section by removing the requirement that the regulation serve little or no public purpose and that it be an unreasonable burden on a petitioner or on interstate or foreign commerce. The ICC could then exempt railroads from any regulation, rule, practice, or policy which is found not to be necessary to carry out national transportation policy, as expressed by the Staggers Act. The legislative history of the Act singled out this exemption provision as the "cornerstone" of the Staggers Act. Furthermore, the ICC was given the

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26. See, e.g., Grain in Multiple-Car Shipments—River Crossings to the South, 318 I.C.C. 641 (1963); Grain in Multiple-Car Shipments—River Crossings to the South, 321 I.C.C. 582 (1963), remanded sub nom., Cincinnati, N.O. & T.P. Ry. v. United States, 379 U.S. 642 (1965) (in which an interminable battle took place concerning whether railroads should be able to attract new business by using larger "Big John" covered hopper cars and offering lower rates than competing rail and barge lines. The lower rates were finally approved.)

27. Grain in Multiple-Car Shipments—River Crossings to the South, supra note 26.


responsible of "actively pursuing exemptions"\textsuperscript{30} and Congress stated that "as many as possible of the Commission's restrictions on changes in prices and services by rail carriers will be removed" through the use of the provision.\textsuperscript{31} Still, this language was tempered with the requirement for the ICC to "adopt a policy of reviewing carrier action after the fact to correct abuses of market power."\textsuperscript{32} Coal was singled out as needing protection during the debate, and was the only commodity so discussed.\textsuperscript{33} Language was included in the record that the power to exempt traffic from regulation should not be used "at the expense of captive shippers who have no reasonable transportation alternatives"\textsuperscript{34} and that coal should not be unduly burdened by ICC action, bearing only its fair share of railroad costs.\textsuperscript{35}

Once Congress mandated the ICC to strive toward bringing the railroads to a state of revenue adequacy, it was incumbent on the Commission to determine what railroad revenue adequacy consisted of, and several proceedings did just that. The Commission concluded that the railroads should have an opportunity to earn a return on investment equal to the current cost of capital, and has then proceeded yearly in a very straightforward manner to determine the cost of capital for various railroads, now using the current, rather than embedded, before tax debt cost of each, and estimating the equity return that would be necessary for the railroads to attract needed new capital.\textsuperscript{36} Comparisons of the equity return earned in other industries and by other regulated utilities were among the evidence introduced and relied on by the ICC.\textsuperscript{37} In effect, the Commission determined the return required for the composite railroad to reach revenue adequacy in a manner very similar to that used by most state regulatory bodies to determine the revenue needs of an electric utility. While the Commission's determination in each proceeding varied somewhat based on the vagaries of changing economic conditions, ICC estimates of revenue adequacy initially determined the before tax debt cost of railroads to be in the 7\% range and the equity cost to be 12-13\%, with a weighting of between 35-40\% debt and 60-65\% equity.\textsuperscript{38} These

\textsuperscript{30} Id.
\textsuperscript{32} Id.
\textsuperscript{34} Id. at 17.
\textsuperscript{35} Id.
\textsuperscript{37} Id.
figures appear to be relatively modest and certainly are not out of touch with the economic realities of the late 1970's, the time frame on which these first estimated were based, except for the fact that not a single major railroad is "revenue adequate" pursuant to the present standard.\textsuperscript{39}

Perhaps the most controversial methodological element is the use of current, rather than embedded, debt cost. This practice yields a windfall to the railroads. In times of rising interest rates, the determination would tend to overstate the cost of debt to the railroads because they owe many long term fixed obligations (bonds) which pay interest much lower than current levels. In effect, the railroads are allowed to earn a return on their debt obligations over and above the cost of servicing those instruments. This is contrary to the thinking of most regulatory bodies which reimburse only for actual, embedded debt costs, and under current economic conditions tends to work against the interests of consumers and shippers. In the future, however, if interest rates begin falling below current levels, the policy could disfavor the railroads. This would occur if the embedded debt cost exceeds current market yields, an outcome that is not likely to happen in the near future, but one which certainly is not improbable.

The findings also were attacked by shippers on many other grounds, the most prominent being that the required revenue levels and returns on investment were higher than necessary to allow the railroads to attract capital and to be financially viable, that railroad earnings were understated due to ICC accounting practices, and that the rate base (or investment) of the railroads was overvalued due to large amounts of sunk investments that are obsolete, inefficient, and no longer revenue producing or needed, but which are still carried on railroad books.\textsuperscript{40} In effect, the argument was that book value exceeds market value on quite a large percentage of railroad assets. As regulatory principles require that a company earn its capital return only on those assets that are "used and useful" (productive), large amounts of obsolete property reflected on railroad books could lead to an inflated rate base and the overstatement of railroad revenue needs.

The ICC rejected the inflated rate base argument on the ground that obsolete investment was less than one percent of the railroad rate base.\textsuperscript{41} The Commission also pointed out the impracticality of the undertaking suggested by shippers in culling out unneeded railroad investments and noted that such second guessing of prior investment decisions could increase the risk of future railroad investments, thus leading to a higher

\textsuperscript{39} See supra note 36.

\textsuperscript{40} Ex Parte No. 347, supra note 20, at 15 n.43. See also Standards for Railroad Revenue Adequacy, supra note 36, at 830.

\textsuperscript{41} Ex Parte No. 347, supra note 20, at 15 n.43.
required return on capital.\textsuperscript{42} The ICC suggested that such a policy could cause greater future rate increases if this increased regulatory investment risk offset revenue savings from the reduced rate base.\textsuperscript{43} The final, rather vague point made by the ICC was that phasing in major rate increases for captive traffic would provide carriers with an incentive to eliminate unneeded facilities, although how this would occur remains unclear.\textsuperscript{44}

For the most part, the general arguments of the shippers are not as persuasive as those of the ICC. First of all, many of the electric utilities which would bear the brunt of higher coal freight rates also are regulated, and routinely ask for large rate increases due to low return on equity, inflation, new construction, and so on, and are constantly in the position of arguing that their return on equity is not high enough to attract new capital. Electric utilities, for the most part, have in fact not been allowed to earn a sufficient return on equity, and neither have most railroads for quite a long period. It is somewhat unseemly, and perhaps inconsistent, for electric utilities to attack a finding that focuses on return on equity. After all, their regulatory bodies do precisely the same thing, although in a somewhat different manner, one less beneficial to the regulated entity. Certainly, the ICC left itself open to criticism and legal challenge because previous policies had considered these other factors,\textsuperscript{45} but, in principle, a finding by a regulatory body that finally recognizes the need for the industry to earn a competitive yield on its investment is certainly not bad economics, even if adopted in a less than procedurally perfect manner and even if the consequences of such a finding have serious ramifications for coal burning utilities due to certain other ICC actions. Short-term procedural victories may appear desirable; but rather than complaining about the good fortune of the railroads in finally getting the ICC (and Congress) to recognize the financial realities and weaknesses of the national transportation system due to the fiscal plight of some railroads, perhaps the utilities would be well advised to expend their efforts by trying to restrain other ICC practices which cause financial distress to utilities and their rate payers and by getting state commissions to adopt an equally realistic approach. There are quite a few other issues on which the railroads and coal rate policy can legitimately be attacked without becoming bogged down in this one.

The issue of inflated rate base is a troubling one because it does

\textsuperscript{42} Id.
\textsuperscript{43} Id.
\textsuperscript{44} Id.
\textsuperscript{45} See generally Standards and Procedures for the Establishment of Adequate Railroad Revenue Levels, 358 I.C.C. 844 (1978). Standards for revenue adequacy found at 49 C.F.R. § 1109.25 (1980) were repealed, so that now the ICC will consider only the current cost of capital in its deliberations.
appear likely that the railroads control quite a few obsolete assets; then again, so do most large, capital intensive corporations. Technology, customer needs, population shifts, environmental concerns, and many other factors can quickly render obsolete or disfunctional investments that were properly made at an earlier time. Absent gross malefeasance in railroad investment policies, it would be inappropriate for the ICC to disallow railroads the ability to recoup their investment costs and a reasonable return on the basis of second-guessing or ex parte rationales about the desirability of certain prior decisions. Again, most electric utilities would expect (or hope for) the same policy from their regulatory agencies, especially given the problems facing the owners of nuclear power plants. Also, another reason why current market values may be less than book value, thus leading to an inflated railroad rate base, is the ICC regulatory policies which have kept some railroads on the brink of financial insolvency. Perhaps in a more enlightened regulatory environment, the market value of these assets would rise to or above book value as they become more productive, free from governmental interference in railroad decision-making. Thus, the decline in value may not be the sole responsibility of the railroads themselves, and they should not bear the financial brunt of earlier regulatory policies. Finally, as a practical matter, it is very difficult to ascertain those investments which are obsolete and for which a return should not be earned, with the only obvious candidates being that very small amount of railroad investment which is targeted by the railroads for abandonment each year.

It is not surprising that the utilities object to rulings such as those involving the use of current debt costs, which allow the railroads a much more favorable potential return than traditional regulatory principles would allow.\(^{46}\) Certainly this practice is not necessary to allow the railroads a reasonable return on their fixed investment and should be tempered by the ICC or the railroads will be able to exceed true revenue adequacy at the expense of captive shippers, an outcome contrary to Congressional intent. The utilities only want railroads treated in a manner designed to

\(^{46}\) Other ICC proceedings which have also raised the ire of utilities and which do tend to overstate railroad revenue needs beyond accepted regulatory principles include Cost Standards for Railroad Rates, 364 I.C.C. 898 (1981) (which severely limited the number of railroad rates that could be found noncompensatory); Standards for Railroad Revenue Adequacy, supra note 36 (which suggested the use of current or replacement cost accounting in railroad revenue adequacy determinations, a move that would markedly increase railroad revenue needs); Alternative Methods of Accounting for Railroad Track Structures, 48 Fed. Reg. 7182 (codified at 49 C.F.R. pt. 1201) (inflation based accounting for all railroad property except land). An appeal of this decision is pending before the United States Court of Appeals for the District of Columbia. Other federal offices also seemed concerned that the ICC had gone too far in aiding the railroads. See U.S. GENERAL ACCOUNTING OFFICE, INFORMATION ON REGULATORY REFORM UNDER THE STAGGERS RAIL ACT OF 1980, at 7-10 (1983).
yield solely a reasonable return, and for this they certainly cannot be faulted. Still, however, on an overall basis, current ICC practices appear more likely to allow the railroads to systematically approach revenue adequacy than prior regulatory practices and in principle seem preferable. The problem is not with the procedures themselves, but rather with the ICC positions which short-circuit the Congressional safeguards concerning captive shippers.

2. **Achieving Revenue Adequacy**

The other major determination to come out of the revenue adequacy proceedings was the strong reaffirmation of differential pricing as a mechanism for allowing the railroads to reach revenue adequacy. Traditionally, regulatory policy requires that each customer pay rates equal to the costs associated with its service plus a fair return on equity to the carrier and that all customers pay roughly equivalent rates for roughly equivalent services. In the railroad area, this policy has led to the development of an archaic, highly intricate costing scheme which allows any interested parties to develop the variable costs (operating expenses) associated with an individual freight movement.\(^{47}\) Variable cost plus an arbitrary Commission approved allowance for fixed (constant) costs or overhead was referred to as "fully allocated cost."\(^{48}\) This number, expressed on a per ton basis, has often been the focal point for determining the reasonableness of a challenged rate. In effect, then, all rates were set as a function of fully allocated cost.

In theory, if each movement yields to the railroads’ fully allocated cost plus a reasonable return, revenue adequacy would be reached. In practice, however, some traffic has competitive alternatives which are priced lower than railroads’ fully allocated cost. The railroads must then reduce their rates or lose the business. If the competitive rate is below railroads’ variable cost, economic theory suggests that the freight should not move via rail because it would be carried at an out-of-pocket loss to the railroad; if the freight can be hauled at a rate between fully allocated cost and variable cost, the railroad should compete for the freight. In this zone, the freight would pay all its associated out-of-pocket expenses, plus some (but not enough) of the overhead that the railroad needs to operate, leaving less overhead that must be provided by the remaining shippers. Assuming that all freight moves at above variable cost, but also assuming that some freight moves at below fully allocated cost plus a fair return, the

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policy question is what shippers will have to make up the difference, and in what proportion.

In its efforts to end this shortfall, the ICC scrapped its usual comparable rates and fully allocated cost plus a reasonable return scheme in recognition that this method was unlikely ever to yield revenue adequacy to the railroads due to the massive amounts of freight that moved at below fully allocated cost because of competitive conditions. Any method of arbitrarily assigning overhead to all freight would drive off the freight for which competitive alternative existed, thus increasing the woes of the carriers and the amount of fixed costs that the remaining shippers would eventually be forced to shoulder. The answer to this quandary seized on by the Commission was deceptively simple and, in reality, was the only available to it—differential pricing, a concept that Congress had already included in the Staggers Act for setting certain jurisdictional levels.

Differential pricing is simply another slightly less onerous name for "value of service" or "what the market will bear," and allows railroads to capture as much of the consumer surplus as possible. Rather than basing rates on cost to the railroad plus a reasonable return, railroad rates should now be based, according to the ICC, on what the shipper would be willing to pay for the service, i.e., a rate up to, but not more than, the value or benefit the shipper receives from the transportation provided by the railroad. For shippers with transportation alternatives, the rate would be relatively low (below fully allocated cost), and for shippers which have a need for transportation that can be accomplished only via rail (coal users), the value of service provided may be very high. The regulatory dilemma is how to allocate the railroad fixed costs to shippers of commodities such as coal and wheat, for which even the shippers would admit the benefits derived from good rail service are substantial, without allowing the railroads to set the rates unreasonably high through the use of their monopoly or market dominant position. This dilemma led to the need for a proceeding to examine the entire issue of the share of fixed costs to be shouldered by coal, and how that share should be determined. Ex Parte No. 347 (Sub-No. 1), Coal Rate Guidelines—Nationwide became that proceeding.

B. Market Dominance

For the most part, the 4R Act and the Staggers Act removed from the ICC authority to find a rail rate unreasonably high if the forces of free and open competition could ensure that the railroads could not exercise mo-
poly power over the shipper.\textsuperscript{51} On the competitive traffic, the removal
of ICC control over maximum rate levels meant that carriers were free "to
set rates in response to their perception of market conditions."\textsuperscript{52} For
shippers of commodities that could be transported via truck, or for ship-
ners having access to barge lines or multiple railroads, competition was
expected to suffice to control potential railroad abuses. For the captive
shipper of bulk commodities, such as a coal producer which has access
to only one railroad, the "market dominance" provisions were supposed
to offer access to regulation as a substitute for competition. In order to
more specially protect these captive shippers, the Long-Cannon Amend-
ment\textsuperscript{53} to the Staggers Act was designed to limit the ability of carriers to
force their market dominant traffic to subsidize competitive freight and to
allocate fairly any unavoidable railroad revenue shortfalls. Differential
pricing was still an acceptable ICC technique for encouraging revenue
adequacy, but the Amendment's function was to ensure that captive ship-
ners did not bear a "disproportionate share of responsibility" for impro-
ving railroads' financial position or did not "subsidize the continuation of
antiquated and inefficient railroad practices."\textsuperscript{54}

Even to be a candidate for market dominance, however, the traffic in
question must move at a rate greater than or equal to 175% of variable
cost.\textsuperscript{55} In the event this test is satisfied, the Commission still does not
have to temper the rate, or even investigate it. Its decision to investigate a
rate over which it has jurisdiction is based on:

i. The amount of traffic which is transported at revenues which do not con-
tribute to going concern value and efforts made to minimize such traffic

ii. The amount of traffic which contributes only marginally to fixed costs
and the extent to which, if any, rates on such traffic can be changed to
maximize the revenues from such traffic; and

iii. The impact of the proposed rate or rate increase on the attainment of the
national energy goals and the rail transportation policy under section
10101(a) [National Transportation Policy] of this title, taking into account
the railroad's role as a primary source of energy transportation and the
need for a sound rail transportation system in accordance with the reve-

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\textsuperscript{51} 49 U.S.C. § 10709(c) (1982).

\textsuperscript{52} Blessemer, 691 F.2d at 1108. \textit{See also Ford Motor Co.,} 714 F.2d at 1158-59.


\textsuperscript{54} Arkansas Power & Light Co., Petition to Institute Rulemaking Proceeding—In-

plement of Long-Cannon Amendment to the Staggers Rail Act, 365 I.C.C. 983, 988 (1982). \textit{See also}

125 CONG. REC. 36,421-22 (1979); 126 CONG. REC. 7264-67 (1980) (remarks of Sens. Long,

Cannon, Baucus and Bentsen).


shipper, chooses to examine the rate, it should base its judgment on factors (i) and (ii) above—railroad efforts to minimize traffic moving at below variable cost and to maximize revenues from traffic moving at less than fully allocated cost. Furthermore, the ICC must consider whether the commodity subject to the rate is paying an unreasonable share of the railroad’s overall revenues. If the ICC acts pursuant to a complaint, the shippers bear the burden of proof. No burden is specified concerning the proceedings involving the ICC’s decision to institute an investigation.

While this procedure appears straightforward, if somewhat convoluted, the ICC does not appear to have taken its obligations concerning market dominance, captive traffic, and the purposes of the Long-Cannon Amendment very seriously. Rather than institute a rulemaking proceeding to determine those factors and other evidence necessary to conduct a Long-Cannon inquiry, the Commission decided to consider the issue on a case by case basis. It did set forth its burden of proof guidelines for Long-Cannon proceedings, however, with the burden being placed on shippers to demonstrate railroad inefficiencies and that the removal of these inefficiencies alone would lead to railroad revenue adequacy. In its ad hoc Long-Cannon efforts, the ICC has been surprisingly unwilling to require railroads to systematically produce evidence concerning elasticities of demand for various traffic, a necessary prerequisite to determining what more the railroads could do to maximize revenues from non-captive traffic. The Commission has also been very unsupportive of discovery efforts by shippers, an especially large problem when only the railroads have cost data for all their freight, which are a necessity if comparisons are to be made; therefore, only railroads have data to show their own efficiencies and inefficiencies.

Refusal to allow adequate discovery, short timetables to analyze the data, and failure to require the railroads to provide data on costs of serving various commodities (some captive, some not), coupled with the burden of proof on the shippers, yields an impossible task for a company trying to avail itself of the Long-Cannon protections. ICC decisions have set up a perfect “‘stonewall’” situation for the railroads. Their failure to provide adequate costing data or elasticity studies precludes a shipper

58. Id.
59. 49 U.S.C. § 10701a(b)(2)(A) (1982). If the ICC institutes an investigation on its own motion into the reasonableness of a rate, the carrier bears the burdens of proof. 49 U.S.C. § 10701a(b)(2)(B) (1982). The statute does not impose a burden of proof or production concerning ICC determinations of whether to investigate a proposed rate.
61. Id.
62. Id. at 997.
63. Id.
from proving its case, and this lack of data cannot even be used to show that the railroads are operating inefficiently. In effect, the ICC has set up a system where a railroad benefits from its failure to know its costs, from its lack of procedures to maximize revenues from non-profitable freight and to minimize inefficiencies, and from its lack of a systemtic approach for treating captive traffic in a manner which minimizes the burden on the traffic consistent with moving toward revenue adequacy. Most modern companies would be said to be mismanaged and inefficient per se if they did not have such systems in place, but ICC policies actually encourage such tendencies, even in the face of substantially expressed Congressional intent that railroads should be free to move toward revenue adequacy at the expense of captive traffic only if they are attempting to ferret out inefficiencies and revenue shortfalls to the extent possible from their other operations.

C. Coal Rate Guidelines

As its attempt to deal with situations in which railroads exercise market dominance over coal traffic and to develop a formula for prescribing maximum reasonable rates on such traffic, the ICC issued Ex Parte No. 347 (Sub-No. 1), Coal Rate Guidelines—Nationwide,64 a series of non-binding proposals. Not surprisingly, the Commission placed great emphasis on the goal of aiding the railroads in achieving revenue adequacy while paying very little attention to the other regulatory goal of not allowing railroads the unfettered opportunity to trample on the rights of shippers with captive traffic. In effect, the question was how the ICC could allocate excess railroad fixed costs among those shippers which have no competitive alternatives at the rate currently assessed by the carriers. When grappling with the issue, the ICC decided that any arbitrary method of allocating or attributing costs to the various shipper classes left the railroads with a revenue shortfall. Neither the ICC nor the railroads could possibly come up with a system to allocate the excess costs in an equitable manner that would not have the effect of driving some freight to competing modes, thus perpetuating the shortfall. The ICC, therefore, was left with some form of demand based on differential pricing as the only viable alternative. The question, then, became one of setting an upper limit on those rates which "are set in an essentially non-competitive environment,"65 i.e., market dominant freight.

The railroads' position was that the only way to allow them to reach revenue adequacy and to minimize regulatory intrusions into their industry was "Ramsey Pricing," a theoretical system which uses demand elasti-

64. Ex Parte No. 347, supra note 20.
65. Id. at 9.
ties to determine what the market will bear for a particular movement and to charge accordingly. Ramsey Pricing is a perfectly acceptable pricing method for the situation in which marginal costs are less than average costs, the typical railroad position, but it has no equitable component which takes monopoly power or captive freight into account as Congress has required. In effect, pure Ramsey Pricing would allow, and expect, unlimited rates to be charged to captive shippers, with the only upward constraint being a point where the shippers were forced out of business due to high rates or when the rates became so burdensome that another alternative mode became cost effective. This failure to set a maximum upper bound for captive traffic is the failure of theoretical Ramsey Pricing for use as a public policy tool when the carrier does not face competition from another railroad or another transportation mode. In effect, the Ramsey Pricing model assumes that competition is available for all freight or that there is nothing undesirable about charging limitlessly high rates to those without competitive alternatives. This is a position that may lead to theoretical economic efficiency but which was rejected by Congress.

Most shippers, on the other hand, recognized that some form of differential pricing, coupled with aggressive pricing of competitive traffic, was necessary to nudge the railroads toward revenue adequacy, and that solely cost based pricing was no longer an adequate regulatory tool. These shippers proposed a variety of plans, some of which would allocate the railroad revenue shortfall among the various classes of shippers which could bear an additional burden without defecting to other transportation modes. These allocations, of course, were very difficult to define properly and could lead to unexpected defections of some freight and revenue shortfalls, if improperly implemented. Other proposals suggested setting ceiling rate levels at a percentage of variable cost, unless the carriers could prove the freight should bear an additional burden; some shippers proposed that the maximum allowable rate should be based on return on investment. For instance, railroads would be allowed to earn twice the rate of return found necessary by the Commission to achieve revenue adequacy, but rates beyond that would be constrained by the Congressional principles relating to captive shippers and market dominance. The shippers' proposals differed, but all had one goal in common—put some sort of cap on railroad rates that retained some semblance of cost based pricing (plus a profit additive). The maximum rate might yield revenue well in excess of fully allocated cost, but at

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66. Id. at 9-10, 26.
67. Id. at 20-27.
68. Id.
69. Id. at 24-25.
70. Id.
least the railroads' ability to demand greater revenues from captive coal would not be unlimited.

The Commission rejected the shipper proposals as being arbitrary allocations (which they were, although they may also have been reasonable), impractical, likely to stifle innovation (an amazing statement to make in the context of railroads), or not likely to induce railroad revenue adequacy.\textsuperscript{71} The ICC also rejected Ramsey Pricing, not in theory but on the practical grounds that large amounts of theoretical data of arguable validity (demand elasticities and marginal costs) would be needed to properly Ramsey Price and that requiring such data would not be in keeping with the Congressional mandate to trim the regulatory burden on railroads whenever possible.\textsuperscript{72} Instead, the Commission accepted "stand alone" pricing and made it the centerpiece of a concept dubbed "Constrained Market Pricing."\textsuperscript{73} Stand alone pricing had been advocated by some railroads and was consistent with the principles of Ramsey Pricing. The maximum allowable rate levels under the two systems were, for all practical purposes, likely to be little different.

1. \textit{Constrained Market Pricing}

a. \textit{Stand Alone Cost}

The ICC set forth four principles of Constrained Market Pricing, with the provision that a carrier violating any of the four could be found to be charging an unreasonably high rate.\textsuperscript{74} Stand Alone Cost, the centerpiece of this scheme, was defined as the cost to the railroad of providing service solely to that single shipper.\textsuperscript{75} In other words, the Stand Alone Rate was that rate at which a shipper could provide itself with a transportation alternative to the monopoly railroad at current prices. As the ICC correctly and rather obviously pointed out, "no shipper would reasonably agree to pay more to a railroad for transportation than it would cost to produce in isolation itself, or more than it would cost a competitor of the railroad to provide the service for it."\textsuperscript{76} The ICC also stated that "no shipper could be said to be cross-subsidizing other shippers if it pays no more than the cost to the railroad of providing service dedicated solely to it."\textsuperscript{77} In effect, then, Stand Alone Pricing stated that a rate was reasonable so long as it was less than the next most cost effective hypothetical alternative avail-

\textsuperscript{71} id. at 20-27.
\textsuperscript{72} id. at 9-10, 26.
\textsuperscript{73} id. at 10-19.
\textsuperscript{74} id. at 11.
\textsuperscript{75} id.
\textsuperscript{76} id.
\textsuperscript{77} id.
able to the captive shipper, or was no more than the rate at which the railroad would lose its monopoly position over the traffic.

The problem with this position is clear. It is using a competitive economic model in a non-competitive situation. Transportation alternatives, if they exist, keep the cost to shippers at efficient, reasonable levels, and that is the rationale for deregulating those commodities and routes for which competition exists. Where competition does not exist, it is unreasonable to define maximum rate levels on the basis that nonexistent competition will keep them reasonable. Despite the mandate of Congress for the ICC to offer some protection for captive shippers, the Commission has in effect adopted the same test for both captive and non-captive shippers—an unrestrained "what the market will bear." The only limit on captive coal shippers set by the ICC under this test would be that railroads may not charge more than the best available potential alternative (such as building a new railroad or a coal slurry pipeline to serve that one shipper). In reality, the railroad could never charge more than the Stand Alone Rate regardless of ICC sanctions, because that is the rate level which would force the shippers to another carrier or transportation mode. Congress meant to provide some protection for captive shippers beyond what the market for captive freight will bear and clearly this test provides no such protection. It is inconceivable that Congress meant that the common carrier could charge a captive shipper any rate equal to or less than that at which it would be cheaper for the shipper to build its own private railroad for its exclusive use, but that is the interpretation of Congress's intent adopted by the ICC. The amount of protection is negligible to non-existent. The ICC's own administrative law judges have recognized the absurdity of this approach and in one case, a Judge pointed out that since passage of the Staggers Act the ICC has never found a rate to be above a maximum reasonable level.

It probably never will, for the level set by the ICC as possibly unreasonable (i.e., above Stand Alone Cost) is so high that no railroad could ever charge such a rate. Thus, this factor will never come into play.

b. **Railroad Management**

The second principle of Constrained Market Pricing focuses on management factors. In keeping with the Long-Cannon mandates, the ICC states that it will consider the amount of traffic which does not contribute to the going concern value of the railroad and efforts to minimize this traffic, the amount that only marginally contributes toward fixed costs and the extent to which such rates can be raised, and, finally, whether one com-

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modity is paying an unreasonable share of the carrier’s overall revenues.\textsuperscript{79} The ICC further vows to take action if carriers are “consciously carrying freight at a loss or at a suboptimal level,”\textsuperscript{80} but in reality the lack of cost data and the lack of concern by the ICC for the lack of cost data make it highly unlikely that a shipper could demonstrate that a railroad is “consciously” carrying freight at a loss. The ICC simply believes that its system will automatically “induce railroad management to continue efforts to maximize revenues on all traffic,”\textsuperscript{81} a highly dubious assumption given the paucity of regulatory incentives, the railroads’ performance to date with non-captive traffic, and evidence in other cases that railroads do in fact carry large amounts of freight at an out-of-pocket loss.\textsuperscript{82} Finally, the ICC states that any carrier failing “to conform to generally accepted standards of economic, economic, and efficient management' must bear the cost of the inefficiencies, not the captive shippers.\textsuperscript{83} Again, the lack of data, the unavailability of discovery, and the short procedural time periods involved, coupled with the ICC’s stated reliance on Constrained Market Pricing to force the railroads to act properly, suggest that only in the most egregious, almost fraudulent type situation could a shipper expect a carrier or the ICC to lower captive coal rates in response to management factors, or even to consider them, despite Congressional intent to the contrary.

\textbf{C. Revenue Adequacy}

The third part of the Commission’s Constrained Market Pricing system has to do with changes in the system once railroads attain revenue adequacy. Although the ICC states that captive coal revenues which allow a railroad to attain or exceed revenue adequacy, as defined by the Commission, would not be unreasonable per se, these rates must be scrutinized more closely.\textsuperscript{84} The ICC, however, takes a long-run perspective, so that rates will not have to be continuously adjusted if revenues slightly exceed or temporarily drop below revenue adequacy levels.\textsuperscript{85} Because of the possible disincentive on carrier attempts to maximize profitability and improve efficiency, the Commission is not likely to lower

\textsuperscript{79} Ex Parte No. 347, supra note 20, at 15 n.43.
\textsuperscript{80} Id. at 14.
\textsuperscript{81} Id.
\textsuperscript{83} Ex Parte No. 347, supra note 20, at 14.
\textsuperscript{84} Id. at 14, 15.
\textsuperscript{85} Id. at 15, 16.
captive coal rates if revenue adequacy is exceeded due to improved profitability on competitive traffic or better operational efficiency.\textsuperscript{86} Only in the instance in which "a consistent pattern of return substantially in excess of carrier's revenue needs has been established . . . would [the ICC] . . . consider the reasonableness of rates on captive coal traffic and prescribe lower rates in appropriate circumstances."\textsuperscript{87} The Commission further states, however, that this will be done only upon filing of a complaint, thus putting the burden of proof on the shippers, not on the carrier which has exceeded revenue adequacy by charging "stand alone" rates to captive shippers of coal.\textsuperscript{88}

While this provision seems to offer some slight hope to the captive shippers that Stand Alone Pricing will not endure indefinitely, the practicalities associated with the provision are much more revealing and much less optimistic. First of all, revenue adequacy has been defined so that no major railroad currently can be said to have adequate revenues, and it appears unlikely that any will achieve this ICC nirvana in the near future. The Commission figured that if 1981 net investment and expenses remain constant, as do non-coal revenues, and coal rates grow at a uniform rate compounded annually, 17 of 21 major coal hauling railroads could reach revenue adequacy within 7 years if coal revenue grows 15\% per year.\textsuperscript{89} This represents a highly unlikely scenario, given the ups and downs of the coal industry, and the heroic assertions that net investment base and expenses will remain constant at 1981 levels. Furthermore, each year the ICC seems to increase the return needed for the railroads to reach revenue adequacy.\textsuperscript{90} In all likelihood, revenue adequacy is going to be a very long-run proposition.

Even if such a state is reached, the captive shipper still has to show that the phenomenon of railroad adequacy is permanent in duration and is not due to railroad improvements in efficiency.\textsuperscript{91} Again, it appears doubtful that much relief will be available to the captive shippers from this provision. Another problem is that revenue adequacy is based on return for book investment, a concept which is often meaningless in financial markets, which value a railroad on its earnings per share. To the extent that railroads can keep their return on book investment below revenue adequacy levels by keeping unused assets on the books, rather than aban-

\begin{footnotes}
\footnotetext[86]{Id. at 16.}
\footnotetext[87]{Id.}
\footnotetext[88]{Id.}
\footnotetext[89]{Id. at 17-18 and app. D.}
\footnotetext[90]{The railroads figured their composite cost of capital at 15.7\%, with equity costing 17.4\%, and debt 11.3\% for 1983. In 1978, the ICC found a 10.6\% overall cost of capital to be reasonable. Adequacy of Railroad Revenue (1978 Determination), 361 I.C.C. 79, 108 (1978).}
\footnotetext[91]{Ex Parte No. 347, supra note 20, at 15, 16.}
\end{footnotes}
d. Phasing of Rate Increases

Because of the ICC's concern that "dramatic" changes could disrupt coal markets, it proposed to phase in rate increases by generally not allowing rates to increase by more than fifteen percent per year plus an allowance for inflationary effects.92 Thus, the real increase in coal rates could not exceed fifteen percent per year, except in unusual circumstances such as imminent bankruptcy or inability to meet debt service. The rates on coal would be presumed reasonable so long as the cumulative increase did not exceed fifteen percent, thus allowing an increase to be deferred for several years and then added on to the increase for a later

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92. Id. at 16-18.
year without violating guidelines. Rates on new traffic would be presumed reasonable if they do not exceed those for comparable movements, including the cumulative fifteen percent increase. This allowable fifteen percent increase was to be inclusive of the zone of rate flexibility allowed by the Staggers Act for all traffic.

The ICC based this requirement on the grounds that severe dislocations could occur if dramatic transportation cost increases were allowed. Fears were expressed of precipitous rises in rates paid by consumers of electricity and of possible hasty conversions of coal burning power plants to alternative fuels, an occurrence that could be contrary to national energy policy. Concern about forcing the railroads to attain the maximum possible contribution from all non-market dominant traffic also led to this provision, as did the rationale of allowing captive shippers time to evaluate their transportation alternatives and attempt to use this transition period to limit potential rate increases in any manner still available to them. The Commission also suggested that, for a variety of reasons, electric utilities would be less captive to a single railroad and have greater market strength starting about 1986. Finally, the Commission believed that most railroads were close enough to revenue adequacy that it could be reached within a reasonably short time, so that the transition period to total Stand Alone Pricing should not unduly affect their attempts to achieve financial strength. The transition period, then, should allow for a smoother, less disruptive change to market oriented pricing, at least in the Commission’s view, and should not excessively prolong railroad attempts at achieving revenue adequacy.

Clearly, this is the only one of the four components of Constrained Market Pricing that offers any immediate protection to captive shippers. This protection is relatively modest, and may often be nonexistent in practice because even if the Commission’s rosy scenario concerning revenue adequacy is true, it will still be eight years before most of the nation’s coal haulers will have achieved revenue adequacy. In that time, coal rates may have tripled, in real terms. The effects of inflation, new investment, and so on will have driven up the potential rates charged to captive shippers even more. A tripling of real rates in eight years for captive shippers

93. Id. at 16 n.46.
94. Id. at 16.
95. Id. at 16 n.46.
96. Id. at 16, 17.
97. Id. at 17.
98. Id.
99. Id.
100. Id. at 17-18.
101. Id. at 16-18.
hardly seems indicative of any concern on the part of the ICC about protecting these users from the monopoly power of the railroads.

D. EXPORT COAL

In Ex Parte No. 346 (Sub-No. 7), Railroad Exemption—Export Coal,102 the Commission exempted all export coal from any ICC rate regulation. In order to do this, the ICC first had to determine that regulation of export coal was not necessary to carry out national transportation policy. The analysis of this issue was extensive, but not really revealing or interesting.103 The salient part of the order dealt with another criterion for exemption—whether the transaction was of limited scope or whether regulation was not necessary to protect shippers from abuse of railroads' market power.104 In this proceeding, the Commission clearly and unequivocally stated its premise that the railroads should be allowed to capture as much of a shipper's consumer surplus as possible, and the railroads were actually in competition with the shippers to control as much of this excess or economic rent as possible. In other words, the ICC's regulatory position was that a railroad should no longer seek to earn a reasonable profit on each shipment and act as a common carrier, treating all shippers equitably and fairly; rather, the carrier was encouraged to take an active role, charging one customer more than a similarly situated competing shipper if the first shipper, by means of its efficiency, ingenuity or luck has managed to produce its coal for a price that yields to it a higher than average profit.

While opponents of this exemption argued that the railroads would price their services excessively high so that United States coal would not be competitive worldwide on a delivered basis,105 the ICC and the railroads noted that this eventually would not be in the best interest of the railroads because of the large amount of capital the railroads have invested in export coal facilities, which would be unused, and thus unproductive, if American coal was priced too high for the world market.106 Also, they believed that coal exporters have bargaining leverage with the railroads which could act as a check to keep rates reasonable, thus preventing the railroads from capturing all the consumer surplus associated with the coal transportation.107 One reason for this would be that coal exporters tend to be larger producers and often own several mines,

103. Id. at 584-92.
104. Id. at 592-96.
105. Id. at 592.
106. Id. at 593-94.
107. Id.
located on more than one railroad, and are able to play one railroad against the other by threatening simply to shift production to another mine, thereby depriving that railroad of all revenues, unless a mutually acceptable transportation price is reached. 108 The ICC further noted that the exemption would terminate all antitrust immunity and that the railroads would not abuse their market position, even if able to, because the Commission might revoke its exemption decision and restore regulation of export coal. 109 The ICC concluded by arguing that:

the exemption of export coal will place the parties involved in exporting coal on equal footing, and will leave the producer and carrier free to negotiate a division of available profit or economic rent. We expect that, following exemption, the railroads will differentiate among the mines they serve and set their rates in an area between an individual mine's long run marginal cost of extraction at the current cost of capital and the world market price. The railroads have long differentiated their rates among the mines they serve and are fully equipped to do so once regulation ends. Although, under exemption, the railroads sometimes may obtain more of the available profit than they currently do, it is in the carriers' long range self interest to encourage the shippers to expand production. Both they and the shippers have a common interest in bringing to market as much coal as the market will absorb. Regional and world competition and shipper transportation and marketing alternatives, as well as the carriers' rational self interest, will all constrain the railroads from abusing such market power as they may possess. . . . 110

The revealing statement makes perfectly clear the ICC's perception of how railroads should react toward both captive and non-captive traffic. Basically, the ICC hopes for an economic tug-of-war, with the railroads and shippers utilizing their long-run marginal cost curves in an effort to arrive at a mutually agreeable location. If, for instance, the delivered price of coal (set by the market) is $5.50 per ton, barge and transloading costs are fixed at $10.00 per ton, railroad variable costs are $8.00 per ton, and marginal coal production costs are $30.00 per ton, the ICC foresees railroads and producers haggling and negotiating over the economic surplus inherent in this transaction—$7.00 per ton. The producer would shut down before paying the railroad more than $15.00 per ton; the railroad would not consider hauling the coal for less than $8.00 per ton, but within those parameters, the ICC desires that economic leverage, bargaining power, negotiating skills or threats, and other similar factors should set the transportation rate. A $15.00 per ton rate would allow the railroad to capture the entire consumer surplus associated with the haul;

108. Id. at 594.
109. Id. at 595.
110. Id. at 596. But see S. REP. NO. 470, 96th Cong., 1st Sess. 43 (1979) and H.R. REP. NO. 1430, 96th Cong., 2d Sess. 88 reprinted in 1980 U.S. CODE CONG. & AD. NEWS 4110 (1980) (indications that the exemption power should not be used at the expense of captive shippers, whether domestic or export shipments are involved).
an $8.00 rate would leave the entire surplus for the producer and keep the railroad in a state of revenue inadequacy. The only unanswered question is where within this range will the transportation rate ultimately be set, once the economic shootout has ended and the dust has settled. In the absence of meaningful competition, however, the ultimate result is starkly clear—if the shippers have no transportation alternatives, the transportation rate will hover close to $15.00, with the only variable being the accuracy of railroad cost estimates for producers and their perception of the strength of the coal market. Quite simply, the consumer surplus is theirs for the asking.

III. ANALYSIS AND CONCLUSIONS

Certainly, the ICC’s unfettered non-passive, price differentiating (or discriminating), quasi-monopolistic role for the railroads is one view of the way to promote railroad revenue adequacy and allegedly protect the interests of captive shippers—and, as it has been advanced by the ICC and the railroads, it is a very important interpretation of their role. The policy question, however, is whether the ICC is on the right track. Most people involved with the issue recognize the railroads’ need for greater freedom and applaud any reasonable regulatory policy that moves in the direction of fewer regulatory constraints. The remaining issue is simply whether the ICC has or has not given enough protection to shippers of a limited number of generally captive commodities. Even looking at a relatively captive commodity such as coal, only about half the shipments have no competitive alternatives.\footnote{111} The number of captive shipments may be relatively few, but the amounts of money they involve can be staggering.\footnote{112} Do these captive shippers need some protection from the railroads in order for equity to prevail and has the ICC met this need within the context of accomplishing other regulatory goals such as pushing the railroads toward a position of revenue adequacy?

While the ICC may have engaged in good long-run economic theory in developing its Constrained Market Pricing system for the purpose of achieving revenue adequacy, efficient economics do not always make good public policy. In this instance, they appear to be colliding. The ICC

\footnote{111. Ex Parte No. 347, supra note 20, at app. B. A consulting firm for the ICC found that 53% of the utilities surveyed only have access to a single terminating carrier and are presently constrained from shifting to alternative coal sources. Utility-related sources suggest that the amount of captive coal is much higher than 53%. \textit{id}.}

\footnote{112. Twenty-one railroads received more than 10% of their revenues from hauling coal in 1981; ten exceeded $100,000,000 in coal revenues; and one exceeded $1,000,000,000. Ex Parte No. 347, \textit{supra} note 20, at app. D. One utility, Arkansas Power & Light, recently estimated that the threat of competition saved consumers $16.5 billion over the life of a contract when compared to current ICC approval rates. \textit{id}.}
simply seems to have ignored Congressional policy concerns about captive coal traffic while focusing solely on railroad revenue adequacy needs. The ability of the ICC to take its fairly one-sided position may not last long. Cases are pending which attack almost every position the ICC has adopted with respect to captive traffic pricing, and it appears that substantial judicial sentiment exists against some ICC views and policies.\(^1\)\(^1\)\(^3\) This certainly should not be surprising, because Congress clearly intended to offer some regulatory protection for captive coal traffic beyond those afforded by competitive conditions, and the ICC just as clearly has not taken these Congressional concerns very seriously. As discussed earlier, since the Staggers Act no coal rate has ever been found too high by the ICC.\(^1\)\(^4\) The policies adopted by the ICC with respect to captive coal are based on the supposition that competitive forces will keep transportation rates at reasonable levels, even in areas for which the ICC admits no transportation alternatives exist. Congress clearly rejected this viewpoint and the ICC's position is untenable in the short-run.

It is true that shippers of captive commodities will have to be harmed at least somewhat if railroads are to attain revenue adequacy. There is no other way to meet this desirable goal. This does not mean, however, that increases based on Ramsey Pricing, restrained only by a maximum cap in real terms of fifteen percent compounded annually, are an equitable solution to the problem of how a common carrier should be allowed to price differentially its services. Congress directed the ICC to afford some protection to captive commodities, and under current ICC policy those regulatory protections are nonexistent.

In *Arkansas Power & Light Company v. ICC*,\(^1\)\(^5\) the court did not directly review ICC captive shipper policy because the case before it did not arise in the context of a specific factual issue, but it did offer some interesting observations about ICC policy which may well presage trouble for the ICC when its policies are reviewed on their merits in future cases. The court recognized the obvious Congressional interest, as expressed in the Long-Cannon Amendment, to offer some protections to captive shippers due to the fact that "carriers might use their monopoly traffic to subsidize other traffic that faced effective competition."\(^1\)\(^6\) It noted that the Long-Cannon Amendment limited ICC discretion to ignore the issue by "requiring" that the Commission consider certain factors when reviewing rates on captive traffic.\(^1\)\(^7\) Furthermore, the court voiced some concern about

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\(^1\)\(^3\) See *Arkansas Power & Light Co. v. ICC*, 725 F.2d 716 (D.C. Cir. 1984).
\(^1\)\(^5\) 725 F.2d 716 (D.C. Cir. 1984).
\(^1\)\(^6\) Id. at 719.
\(^1\)\(^7\) Id. at 720.
discovery and burden of proof problems currently placed on protesting shippers, found some aspects of ICC policy "disturbing" and others "that arguably stand in contradiction to the relevant statutory mandates."\textsuperscript{118} The court chose not to review the issues at that time because the ICC’s Coal Rate Guidelines had not yet been tested in a concrete case and were only a "non-binding statement of future intent."\textsuperscript{119} But this case, as well as \textit{Farmers Union Central Exchange v. Federal Energy Regulatory Commission},\textsuperscript{120} a proceeding which examined the Interstate Commerce Act’s reasonableness standard, clearly evince judicial concern about unduly favorable rate of return standards for certain traffic and the total absence of cost-based pricing as an underlying basis for ratemaking. While there is no doubt that courts recognize the need for some restrained type of differential pricing, the ICC’s current standards may not pass muster because of their unrealistic rationales and lack of concern about maximum reasonable rates for captive shippers.\textsuperscript{121}

Bad law can still be good public policy, and, in the long-run, the ICC’s position is defensible, and may even be desirable. In the long-run (that time frame beyond which utilities have the ability to choose where their power plants are located and producers the ability to open new mines freely), a shipper may be able to protect itself by contracting in advance with a railroad. Before a plant site is selected, an electric company may be able to play one railroad against another, or threaten to use barges or mine mouth generation, and, in general, promote free and open competition among all feasible transportation sources. As is the case now that ICC policy has changed, a long-term contract which guarantees the utility a set transportation rate (plus escalator provisions) for the expected useful life of the facility and guarantees the railroad a minimum annual volume of traffic for an extended period could be signed with a railroad before the plant site was selected. This relationship, again, is symbiotic in nature, with greater efficiency and lower capital costs accruing to the railroad because of the long-term certainty and continuous nature of the movement.

\textsuperscript{118} \textit{Id.} at 723-24.
\textsuperscript{119} \textit{Id.} at 724 (emphasis in original).
\textsuperscript{120} 584 F.2d 408 (D.C. Cir. 1978). The court held that abusive or gouging rates are of themselves not just and reasonable, and largely undocumented evidence on competition cannot be the principal means of ratemaking. Departures from cost-based rates should be made only when non-cost factors are identified clearly and these factors justify the resulting rate levels.
\textsuperscript{121} Commissioner Sterrett, who is normally in agreement with most ICC actions, also recognizes the unfairness of some captive shipper decisions. He is concerned about the mechanical formula which has been substituted for ICC discretion in coal rate cases and that the guidelines are too heavily weighted against captive shippers. 48 Fed. Reg. 19,421 (1984). Support for this viewpoint could come from Chairman Taylor, and, with impetus from a few court decisions could cause somewhat of a shift in ICC policy. It is still far too early, however, to state that a shift in policy has occurred or is even being contemplated.
Possibly in the long-run, true competition will prevail and a position financially attractive to both sides will occur because shippers and carriers both have viable negotiating positions and alternatives. In recent cases, electric utilities publicly announced that they had saved the public hundreds of millions of dollars in transportation costs over the life of generating facilities, solely because their plants had access to two railroads from the source of coal rather than a single carrier as had previously been the case. 122 That sole carrier had been able to exercise monopoly pricing and capture a large portion of the consumer surplus associated with the utility’s coal supply; but when the bargaining involved another carrier, the first railroad was forced to share its excess profit with the electric utility and the consumers in order to retain the freight. This is a classic example of the tug-of-war and interaction among utilities’ and railroads’ revenue and cost curves that was depicted in ICC coal decisions. In the long-run, this result may occur in some or all dealings between carriers and shippers. Competitive alternatives should be available for much traffic and economically efficient pricing will occur without the need for regulation, even for formerly captive traffic such as coal.

The point is that, in the long-run, coal is no longer captive. Competitive alternatives may exist for producers—to mine another site—and utilities—to choose another transportation alternative without sacrificing a large fixed investment. The problem with the ICC’s position is that it has not significantly differentiated between the long-term and the short-term, despite the fact that, in the short-term, much coal remains captive. The ICC has simply adopted a short-run strategy for efficiently pricing coal transportation, but based it on considerations that are true only in the long-run or in those current situations in which a utility or producer happens to have access to alternative transportation. 123

While it is true that long-run competition should end most coal industry concern about ICC policy, certain other trends are apparent that may cause problems because they substantially lessen available competition for freight. Mergers among major coal hauling roads have substantially reduced the number of possible carriers for coal. 124 Also, a major railroad presently has an application pending before the ICC to purchase

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123. Typically, this consists of the utility building its own short-line railroad to connect its plant with another carrier, or pairing two or more plants together, some of which have transportation alternatives and some which do not. The utility then offers to give a railroad the traffic for which competition exists only if that carrier lowers its rates on the monopoly traffic. Arkansas Power & Light believes that the threat of building a coal slurry pipeline or a competitive alternative to an existing monopoly railroad saved it and its consumers approximately $16.5 billion. Id.
America's largest barge company, which occupies an important competitive niche in that railroad's territory.\textsuperscript{125} Finally, railroad refusals to sell right-of-way access and railroad lobbying have doomed current efforts to build several coal slurry pipelines, the most promising source of competition for captive coal. The anticompetitive implications of these moves could be staggering. The ICC's coal strategy presumes competition, but other ICC policy negates competition by reducing the number of viable carriers, putting various competing transportation modes under railroad control, and giving the railroads an effective veto power over competing technologies.

One final area of long-run concern, and one that the ICC has treated cavalierly or not at all, is the environment. In its export coal exemption decision, no environmental impact statement was found necessary by the ICC and in \textit{Coal Rate Guidelines—Nationwide}, the ICC gave notice of intent to consider the effects of its actions on the environment and on energy consumption after it had reached its decision.\textsuperscript{126} While the Commission's notice stressed that the guidelines were merely proposals, not binding policy pronouncements, it is apparent the environmental issues are not likely to play an important role in ICC policy. In fact, it appears likely that they have been ignored, except for a perfunctory, after the fact analysis. For instance, the ICC stated in its notice of intent that certain models estimating the environmental impact were likely to overstate the problems of the proposal.\textsuperscript{127} Apparently the ICC was already making its case for ignoring negative data even before it saw the evidence. While the notice stressed the usual factors such as likelihood of modal shifts, commodity shifts, deferral of generating facilities, and shifts to foreign coal and comparisons of the environmental desirability of nuclear energy and coal, one of the most serious problems of the ICC policy was unmentioned—how it will affect future siting decisions of producers and electric utilities.\textsuperscript{128}

When railroads were closely regulated, both producers and utilities could locate their facilities solely on the basis of site desirability, with the knowledge that they would not have to worry about railroad monopoly profits on their traffic. The ICC would make sure that they were treated equally with other shippers and receivers. Under the deregulated envi-

\textsuperscript{125} At the present time, the parent company of the American Commercial Barge Lines may be taken over by the CSX Corporation, a large railroad conglomerate with substantial coal-hauling facilities in the eastern and southern United States, the same territory in which American Commercial Barge Lines operates. See CSX Corp.—Control—American Commercial Lines, Inc., Finance Docket No. 30300 (I.C.C. decided Aug. 27, 1984).
\textsuperscript{127} \textit{Id.}
\textsuperscript{128} \textit{Id.}
environment, this is no longer the case. Each mine and power plant must be sited so as to have access to two or more carriers, or modes, in order to maintain a competitive edge. A plant site on a navigable river or between two railroads may not be the most environmentally sound location, but it may be the most economically sound location. Furthermore, a plant may not be sited most efficiently for the needs of consumers in its service area due to the necessity of availing itself to two competing transportation modes. This could lead to additional energy consumption and wasted electricity because of excessively long transmission requirements and to additional environmental degradation resulting from extra coal being burned. When confronted with rising consumer protests from electric users and the possibility of billions of dollars in savings over the life of a project, many utilities may choose an environmentally or otherwise economically inferior site which has competitive transportation alternatives. At a minimum, utilities now have to factor transportation accessibility into their siting decision, a constraint which previously was unnecessary. The same arguments also hold for producers, which also may find it necessary to switch mine locations in order to preserve transportation competition. Furthermore, the railroads, which own much coal property, may choose to price transportation such that their lands are developed to the exclusion, or at least detriment, of non-railroad owned coal. This may have antitrust implications, but also environmental ones if the coal so favored causes more severe environmental problems due to its location and so on than non-railroad controlled coal.

It is unlikely that this argument will be publicly brought forth by the electric or coal industries, for two reasons. Given the small likelihood of change by the ICC, the utilities would not want to admit that any site they select is environmentally inferior, thus having to face the wrath of environmental groups and other regulatory agencies. Furthermore, electric utilities and coal companies often fight environmental regulations and litigation tooth and nail and may well find it hard to resort to these laws for help when they are so used to getting clubbed over the head by them in other proceedings.

Even if the arguments are unlikely to be raised by electric utilities, the issue should be reviewed. The ICC has a duty to consider foreseeable, but secondary impacts resulting from its actions that are likely to have environmental effects. The Commission admits, however, that it knows

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129. While 49 U.S.C. § 10746 (1982) prohibits railroads which own coal from also transporting it, railroads are now free to move their own coal for export, thus giving them a complete vertical monopoly position should they choose to exercise it. Furthermore, even for domestic consumption, they remain free to market their coal and affect competing coal production companies; they merely cannot transport the coal they own.

very little about the effect on energy utilization and environmental impact arising from some of its coal decisions.\textsuperscript{131} Additionally, the ICC has looked only at environmental concerns likely to arise from increased rates and has ignored other shifts such as the relationship between domestic and exported coal and other possibilities that might adversely affect the environment.\textsuperscript{132} Chairman Taylor, in his dissent in the \textit{Export Coal} decision, articulated most of the non-siting concerns very well.\textsuperscript{133} Some heed should be paid to these issues before the ICC acts precipitously.

While the long-run implications of ICC coal policy may actually yield a balanced economic environment in which railroads, producers, and users compete equitably (although certain other problems may arise), the short-run picture is much less rosy for those who believe that the need for revenue adequacy should not be the sole determinant of railroad ratemaking. ICC policy is predicated on competition existing for traffic that has been determined to be captive or market dominant. Meaningful competition simply does not exist for this traffic in the short-run, and to base policy on that assumption is folly. The only recognition to date by the ICC of the needs of captive traffic is to defer unlimited railroad rate setting ability for a few years by limiting the \textit{real} rate increases to fifteen percent compounded annually. This procedure gives captive shippers a few years before the full brunt of the policy is felt, but rates can still triple in eight years on this captive traffic, without even the possibility of ICC intervention and rate relief.

The ICC wants shippers and carriers to act as if competition exists and to engage in the aforementioned long-run marginal cost curve tug-of-war, but this policy is not satisfactory because many shippers have no short-run ability to withstand railroad attempts at extracting monopoly profits. This problem occurs for a variety of reasons. First of all, the railroads themselves control much coal land in the east and west. They could juggle transportation rates to favor their land, or they could lease their land to developers at favorable rates in order to determine what economic shifts in the market occur. Furthermore, their determination of whether to enter various markets and at what levels of output, would cause competitive harm to existing producers, thus making it less likely

\textsuperscript{131} See Railroad Exemption—Export Coal, supra note 102 at 608-10 (Taylor, A.L.J., dissenting).


\textsuperscript{133} See Railroad Exemption—Export Coal, supra note 102, at 605-07, 608-10.
that these producers can stand up to the railroads in a bargaining situation. Even if the railroads do not act in such a manner concerning their lands, the realities of their power over transportation and over coal could give pause to any producer trying to buck them.

ICC arguments that shippers can protect themselves by signing contracts with carriers are equally fallacious.\(^{134}\) While true in the long-run, the short-run picture is different. If shippers have no bargaining power, railroads will only sign contracts on terms most favorable to them, or will simply wait out the shippers by publishing tariffs as they see fit. As shippers have no possibility of stopping these rate increases, the railroads have no incentive to limit them by signing contracts, unless a competitive alternative exists for the shipper. Unequal bargaining power is not conducive to contract negotiation.

The ICC further suggests that railroads will have to be reasonable in their demands because many producers have separate mines operating on other rail lines, and may simply shift production from one to the other if one railroad's rates are not reasonable.\(^{135}\) The problems with this viewpoint are many. First of all, coal from one mine may not match the sulfur, ash, etc., content of another mine, and may not be compatible, even when blended, with a particular power plant which the company must supply. Secondly, a multiple mine owner which closes some or all of its mines to force the railroads to lower rates loses a substantial part of its volume; the railroad, on the other hand, would lose an infinitesimally small share of its market by refusing to lower that mine's transportation rate and consequently losing its freight. Clearly, only in the most exceptional case would a mine owner, even with facilities on different carriers, be able to withstand the economic might of a railroad if the railroad refused to lower its rates. Furthermore, in many other circumstances, even the existence of apparent competition will not preclude the railroad from capturing all the excess profits. For instance, railroads now may refuse to offer a shippers reasonable rates on a short movement from the mine to a competing barge line, or a short movement to a competing railroad. Thus, the alternative movement posited by the ICC as promoting competition must take place solely via competing carriers because the ICC no longer is in position to require that interline rates or rates to barge facilities be non-discriminatory, fair, and reasonable. By the same token, for this carrier shift to work in most circumstances, the receiver, as well as the shipper, would also have to be served by two carriers. If only the original carrier serves the receiver, it could refuse to participate in a joint line movement, except at an exorbitant rate. In effect, only in those circumstances in which two

\(^{134}\) Id. at 588. See also Ex Parte No. 347, supra note 20, at 17.

\(^{135}\) See Railroad Exemption—Export Coal, supra note 102, at 593-94.
fully independent transportation alternatives exist can the railroad be prevented from capturing the entire consumer surplus associated with the coal.

The ICC also suggests that the railroads benefit from high volume coal shipments and will exercise voluntary restraint so as not to kill the goose that lays the golden egg, thus giving shippers some bargaining leverage.\(^{136}\) When a monopoly exists, economic theory suggests that the monopolist does not maximize volume but rather maximizes revenues and profits. The principal economic problem with monopolies is that they cause higher prices and lower volume than would occur in a competitive situation. The railroads certainly would act as rational monopolists, and despite expressions of faith by the ICC, coal prices can only rise and volume fall so long as railroads possess market dominance over traffic.\(^{137}\)

Much of the ICC’s analysis of this problem has been based on railroads’ need for revenue adequacy, which they cannot reach otherwise because competitive conditions force them to haul some freight at less than full cost, but more than variable cost. As the railroads typically have a downward sloping marginal cost curve, says the ICC, pricing their services at marginal cost leaves them with a permanent revenue shortfall, which cannot be made up so long as competition exists for some traffic unless other, captive traffic is charged higher rates. By coupling the railroads’ monopoly power with pricing freedom, the ICC has put the coal industry in the same position of short-run subservience from which it has just rescued the railroads. The railroads, if they are smart enough and gather enough knowledge about market conditions, can capture all of the consumer surplus associated with coal and force shifts in the producers’ marginal cost curves until they are just on the verge of shutting down. As coal producers also have downward sloping marginal cost curves, total producer revenues will now tend to fall short of total producer costs where marginal revenue equals marginal cost, thus leaving producers with a revenue shortfall equivalent to that formerly experienced by the railroads. The coal industry’s revenue problems have not been solved, but only shifted from the railroad to the producer, and ultimately to the users of steel and electricity. Assuming perfect knowledge of market conditions by the railroads and producers, the above represents the rational short-run outcome in the absence of meaningful competition.

Assuming perfect knowledge by the railroads, producers and shippers is also a heroic assumption by the ICC. Railroads certainly do not have a history of quick reaction times to market shifts, and may well mis-

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136. Id.
137. Whether volume will fall can be argued indefinitely. However, evidence does exist that such an occurrence could happen and that the issue does deserve serious consideration by the ICC in light of statutory requirements.
judge market conditions. Giving the railroads monopoly power and pricing freedom allows them to capture as much of the consumer surplus as their skills allow, but it also gives them the power to destroy a particular market through spite or simply miscalculation. If they incorrectly estimate the amount of consumer surplus or changes in market condition and price their services too dearly, a contract may well be lost and a mine closed. Railroads tend to be ponderous entities with a 100 year tradition of not competing, and it would be almost miraculous to expect their bureaucracies to be at the forefront of innovative and accurate marketing.

When the ICC shifted from fair, just, and reasonable pricing on captive traffic to what the market will bear, the effect was to increase costs to the principal consumers of coal—electricity consumers. In effect, all customers of coal burning utilities pay a tax to the railroads to make up for their revenue shortfalls from other commodities. This is a relatively painless way for the ICC to meet its revenue adequacy obligations to the railroads. Railroads and electric utilities are both regulated, and both typically pass through costs to their customers. The electric utilities are hurt somewhat by these transportation cost increases and do fight them vigorously, but consumers are the class ultimately hurt the most by captive market pricing. Coal, transportation, energy, consumer and environmental issues should be combined with concerns of equity for all affected groups when setting coal transportation policy, but the ICC has focused almost exclusively on one facet of the problem—railroad revenue adequacy—and almost totally ignored the others. The ICC’s concern has been to prevent future railroad failures, and at least in the short-run, it has succeeded with a vengeance. Competing considerations mandated by Congress and suggested by non-railroad sources have been repeatedly overlooked. Unless the courts overturn some ICC policies, the short-run ability of the railroads to capture the consumer surplus, if any, which exists for a captive coal producer is limited only by the skill and imagination of the railroads. The long-run implications of the policy may be more competitively balanced, but given the long life of existing facilities built before ICC policy shifts, the captive shipper problems will be facing Congress and regulatory officials for many years.
Motor Carrier Bankruptcy in an Uncertain Environment

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I. INTRODUCTION

Since passage of the Motor Carrier Act of 1980,1 numerous motor carriers have discontinued operations. The American Trucking Associa-

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tion (ATA) indicates "250 known carriers have gone out of business, reduced service or declared bankruptcy since the act and that these carriers generated revenues in excess of $2.3 billion." There is substantial controversy over the impact of deregulation on motor carrier insolvency. Some lay the blame squarely on either deregulation or the economy. But most analysts see the poor economy and the increased competition spurred by less regulation as the primary forces behind the current flood of carrier closures. Concerns for further insolvencies persist as the Motor Carrier Act of 1980, with its open entry policy and relaxed rate controls, has increased competition significantly.

Financial analysts have long sought accurate methods of measuring financial health and forecasting bankruptcy. Research attempts have centered on the use of predictive models which combine financial ratio

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3. The financial condition of the motor carrier industry has been addressed in every oversight hearing held by the House or Senate. See Motor Carrier Act of 1980, Pub. L. No. 96-296, § 3(b), 94 Stat. 793, 793 (requiring such hearings to be held for five years after enactment).


6. Many financial analysts conclude that:

Any companies which might prefer to liquidate or sell out cannot do so due to the Multiemployer Pension Plan Amendments Act (MEPPAA). Most such companies sign multiemployer collective bargaining agreements which call for fixed amounts of contributions per employee. Prior to passage of the MEPPAA, the pension funds established and maintained under the labor agreement were considered to be "defined-contribution" plans. The liability of participating carriers was restricted to the amount of contribution defined by the labor agreement. MEPPAA created a new concept called withdrawal liability which requires a withdrawing company to pay a share of the pension plans' total unfunded vested benefits. Current unfunded vested liabilities are estimated to be over $4 billion for the motor carrier industry and, in many cases, the liability of individual carriers is greater than their total equity. A number of the carriers affected by this ruling are in precarious financial conditions. Because this $4 billion liability is the shared responsibility of all carriers who have signed the industry's labor agreement, the surviving carriers will have to bear an increased share of the liability if a carrier declares bankruptcy and cannot cover its share of liability. Trucking companies whose management and stockholders agree that remaining in the trucking business would not provide rates of return satisfactory to them and therefore might seek to liquidate their investment or find a suitable merger partner, could be dissuaded from making this logical business decision because of the requirements of MEPPAA as presently stated. This withdrawal liability is on par with unsecured debt in the event of a liquidation. Therefore, the financial community faces increased risk due to the large pension claims that would occur with liquidation.

analysis with statistical techniques. The purpose of this article is to assess the changing financial state of the motor carrier industry and to forecast bankruptcy trends. The methodology employed is one of the most widely accepted statistical bankruptcy classification models, the Altman Model. The paper will first describe the General Freight segment of the trucking industry upon which the empirical analysis is focused. Then the model will be applied to a sample of bankrupt and non-bankrupt motor carriers to test its validity to the trucking industry. Once validated, it will be used on a random sample of carriers to measure the overall financial health of the industry and to test two hypotheses advanced by industry analysts. The first asserts that deregulation has been the direct cause of increased bankruptcy problems in the industry. The second holds that larger carriers are benefiting at the expense of the smaller.

II. THE GENERAL FREIGHT SEGMENT OF THE TRUCKING INDUSTRY

The motor carrier industry can be segmented into groups that share common economic and operating characteristics. A generalized view of this structure is shown in Figure 1. The intercity general freight carrier segment is the subject of frequent study because of its size, the number and range of customers served, and unique operating requirements (frequent rehandling at terminals). This study concentrates on motor carriers which derived an average of seventy-five percent or more of their revenues from the intercity transportation of general freight. This includes the regular and irregular route general freight carriers shown in Figure 1. These carriers are frequently referred to as Instruction 27 (I-27) carriers by the Interstate Commerce Commission (ICC) for reporting purposes. A breakdown of revenues earned by these carriers is shown in Figure 2.

Figure 1: Legal Structure of the Motor Carrier Industry

III. THE ALTMAN MODEL

Historically, analysts have used balance sheet and income statement ratios to assess financial performance. These ratio measures can be grouped into several categories, each of which measures a particular aspect of financial health.\(^\text{12}\) Rations can measure liquidity (the ability to pay current obligations promptly), leverage (the extent to which a firm uses debt finance), turnover (the efficiency of asset use), and profitability. Until recently, there was a lack of empirical evidence linking these ratios to the successful prediction of corporate bankruptcy. Research by William Beaver in the mid-1960's attempted to statistically correlate financial ratios to bankruptcy using single variable models.\(^\text{13}\) Edward Altman refined the analysis by combining groups of ratios into a multivariate model with greater predictive ability.\(^\text{14}\) His model, often referred to as the Z Score


\(^{14}\) Altman has published dozens of journal articles and several books on the prediction of corporate bankruptcy. See, e.g., Altman, Financial Ratios, Discriminant Analysis, and the Prediction of Corporate Bankruptcy, 23 J. Fin 589 (1968); Altman, Predicting Railroad Bankruptcies in America, 4 Bell J. Econ. & Mgmt Sci. 184 (1974); Altman, Haldeman & Narayanan, Zeta Analysis: A New Model to Identify Bankruptcy Risk of Corporations, 1 J. Banking & Fin. 29 (1977); Altman & McGough, Evaluation of a Company as a Going Concern, J. Acct., Dec. 1974, at 50; E.
Model, remains today as the most widely quoted and generally accepted model in both industry and academia.\textsuperscript{15} The methodology of this paper will utilize one of several variants of this popular model. That variant is the Z" Score.\textsuperscript{16}

Altman’s Z" model isolated four important ratios demonstrated to be consistent predictors in several studies of corporate bankruptcy.\textsuperscript{17} These four ratios are:

1. The ratio of working capital to total assets (WC/TA), a liquidity measure. Working capital is defined as current assets minus current liabilities. The higher this ratio, the more liquid is the firm, and therefore the probability of insolvency is lower.

2. The retained earnings to total asset ratio (RE/TA), an accumulated past profitability measure. As an indicator of “staying power,” high ratios indicate a lower likelihood of insolvency.

3. The ratio of earnings before interest and taxes, or net carrier operating income as it is referred to in the motor carrier industry, to total assets (NCOI/TA), a profitability measure known as the return on assets. High ratios are correlated with decreased risk of bankruptcy.

4. The ratio of the book value of equity to the book value of debt

\textsuperscript{15} Altman’s model has not been without its critics. Some have argued that the model does not perform well under all circumstances and that simpler models may do well in some cases. See Moyer, \textit{Forecasting Financial Failures: A Re-Examination}, \textit{FIN. MGMT.}, Spring 1977, at 11. Others have attacked its statistical validity. See Joy & Tollefson, \textit{On the Financial Applications of Discriminant Analysis}, 10 J. FIN. & QUANTITATIVE ANALYSIS 723 (1975). Altman, however, has countered the criticism of his model and defended its application. See Altman, \textit{Examining Moyer’s Re-examination of Forecasting Financial Failure}, \textit{FIN. MGMT.}, Winter 1978, at 76; Altman & Eisenbeis, \textit{Financial Applications of Discriminant Analysis: A Clarification}, 13 J. FIN. & QUANTITATIVE ANALYSIS 185 (1978). In any case, as the authors will demonstrate later in this paper, the Altman Model does work well when applied to the motor carrier industry, and it still remains the most widely used model in predicting corporate bankruptcy. See, e.g., E. Solomon & J. Pringle, \textit{An Introduction to Financial Management} 122 (2d ed. 1980); J. Van Horne, \textit{Financial Management and Policy} 691-94 (5th ed. 1980); J. Weston & E. Brigham, \textit{supra} note 12, at 192-94.

\textsuperscript{16} Altman has refined his original Z Score model and he uses several variants as general models depending on certain circumstances. The two variations on the Z Score are the Z and Z" Score models. The authors tested these two alternatives and found Z" to be superior to both the Z and Z' Score models in the case of the motor carriers. See generally E. Altman, \textit{Corporate Financial Distress} 120-24 (1983).

\textsuperscript{17} The Z" Score model is a reduced form of Altman’s original Z Score. The latter includes a fifth variable, a turnover ratio (or Sales/Total Assets). Altman suggests, however, that in some industries this variable should be deleted to minimize “a potential industry effect which is more likely to take place when such an industry sensitive variable as asset turnover is included.” \textit{Id.} at 124. The authors' tests on the different models bore out Altman’s suggestion. We obtained much more significant results with the turnover ratio deleted.
(BVE/BVD), a gauge of financial leverage.\textsuperscript{18} High ratios measure low risk.

Altman combined these four ratios via an applied regression technique known as multiple discriminant analysis\textsuperscript{19} into the following predictive model:

\[ Z'' = 6.56X_1 + 3.26X_2 + 6.72X_3 + 1.05X_4, \]

where \( X_1 \) through \( X_4 \) are the respective financial ratios. The \( Z'' \) Score is an index which Altman maintains is of considerable use in both forecasting bankruptcy several years in advance and in assessing overall financial performance.\textsuperscript{20} The critical value of \( Z'' \) are 1.10 and 2.60. A \( Z'' \) of less than 1.10 indicates severe financial stress, a likely bankruptcy candidate. A value of 2.60 or more signals a stronger financial position. Scores between these two barriers form the "zone of ignorance," where classification is more difficult.\textsuperscript{21}

IV. VALIDATION OF THE MODEL TO MOTOR CARRIERS

In order to validate the model as applicable to the motor carrier industry, 47 bankrupt and 47 non-bankrupt carriers over the years 1979-1983 were selected.\textsuperscript{22} Appendix I lists those carriers. Altman's \( Z'' \) Score was then used to test the model's ability to discriminate between the two groups. Appendix II presents the results for the bankrupt carriers; Appendix III, for the non-bankrupt. Table I summarizes some salient information from the study.

\textsuperscript{18} This ratio is an inverted variation of the traditional debt to equity ratio so widely used by bankers and security analysts. Altman found that this version better fit the model. \textit{Id.} at 107.

\textsuperscript{19} Multiple discriminant analysis (or MDA) is a statistical technique involving the correlation of key variables (called independent variables) with a variable to be predicted (the dependent variable). The dependent variable is an index that allows classification of an observation into one of several \textit{a priori} groups—in this case failed versus successful firms. The MDA technique derives a linear combination of the characteristics that best discriminate between the groups (that is, those discriminations that minimize the probability of misclassifications). Altman tested twenty-two financial ratios, four of which were found to contribute most to the predictive model. The slope terms (e.g., 6.56, etc.) are the results of the best "fit" of the data. \textit{Id.} at 102-05.

\textsuperscript{20} \textit{Id.} at 124. While the derivation of the model is quite complex, its application is quite simple as will become evident from the exhibits to follow.

\textsuperscript{21} Not one firm with a \( Z'' \) score of 1.10 or less survived, while no firm with a \( Z'' \) of 2.60 or more failed. \textit{Id.}

\textsuperscript{22} Bankrupt carriers were identified in I. Silberman, \textit{Analysis of the Financial Performance of the General Freight Motor Common Carrier Industry}, attachments II, III (1982). Non-bankrupt carriers were selected by sequential sampling of carriers listed in various \textit{Motor Carrier Annual Reports}. The number of non-bankrupt carriers were to match the number of bankrupt carriers in the sample for that year.
TABLE I

<table>
<thead>
<tr>
<th></th>
<th>BANKRUPT</th>
<th>NON-BANKRUPT</th>
</tr>
</thead>
<tbody>
<tr>
<td>Computed Average Z' Score</td>
<td>-3.98</td>
<td>3.87</td>
</tr>
<tr>
<td>Number of Carriers With Scores:</td>
<td></td>
<td></td>
</tr>
<tr>
<td>2.60&gt;</td>
<td>6</td>
<td>28</td>
</tr>
<tr>
<td>1.10-2.60</td>
<td>7</td>
<td>11</td>
</tr>
<tr>
<td>&lt;1.10</td>
<td>34</td>
<td>8</td>
</tr>
<tr>
<td>Number Classified: 2.6&gt; / &lt;1.1</td>
<td>40</td>
<td>36</td>
</tr>
<tr>
<td>Error Rate: Type I Error</td>
<td>15%</td>
<td></td>
</tr>
<tr>
<td>Type II Error</td>
<td></td>
<td>22%</td>
</tr>
<tr>
<td>Percent Successfully Predicted</td>
<td>85%</td>
<td>78%</td>
</tr>
</tbody>
</table>

The power of the model is evident from this summary. It clearly separates the two classes of motor carriers with a high degree of accuracy. Note especially the Type I and Type II error rates. A Type I error results when a bankrupt carrier is classified as non-bankrupt. In this case, the model classified 6 carriers as solvent when they in fact went bankrupt. Out of the total of 40 carriers classified, this is an error rate of only 15% (or 6/40). The model was therefore 85% accurate in classifying the carriers that were to fail. A Type II error, on the other hand, is the classification of a non-bankrupt carrier as bankrupt. Eight carriers scored less than 1.10 and were still solvent one year after the test period. This resulted in an error rate of 22% (8/36). It is worthy to note here, however, that two of these carriers did ultimately go bankrupt several years later, thus decreasing the actual error rate to 16.7% (6.36).23

In sum, the validation tests show the model works relatively well in the motor carrier industry. Although the model is not perfect in its forecasting ability, it does allow an analyst to make sound judgements about the overall financial strength of this industry.

V. FINANCIAL CONDITION OF GENERAL FREIGHT CARRIERS BEFORE AND AFTER Deregulation

An evaluation of the effects of deregulation and the post-deregulation...
economy on the financial well being of the trucking industry is made by comparing the Z'' scores of carriers before and after deregulation. The year 1976 was chosen as the "before" period in order to avoid the effects of administrative deregulation that began in 1977.\textsuperscript{24} The latest year after deregulation for which uniform and consistent data was available was 1982. Two population types were chosen for the "before" and "after" deregulation comparison.

These samples are henceforth referred to as the industry samples and are listed in Appendix IV.\textsuperscript{25} A carrier is not necessarily represented in both years although the random selection procedure may have led to this result. A second group of carriers was chosen to compare the financial condition of carriers which have survived from 1976 to 1982. Carriers in the 1976 sample which also reported in 1982 were chosen for this sample. These thirty-six carriers are referred to as the "panel sample" and are identified in the 1976 column.

The intercity general freight carriers segment may be further classified according to size of carrier and type of service. For reporting and statistical purposes, the ICC classifies motor carriers into Class I, II or III categories. Only the large Class I and medium-size Class II carriers are included in this study.\textsuperscript{26} Intercity carriers are further subclassified as either regular route, operating predominately over designated highways,

\begin{footnotesize}
\textsuperscript{24} This is cogently revealed in Kahn, \textit{Motor Carrier Regulatory Reform—Fait Accompli}, 19 Transp. J. 5 (1979).

\textsuperscript{25} A sequential sampling technique of Class I and II general freight motor carriers was used. All financial data was from the 1976 and 1982 data compiled in the \textit{Motor Carrier Annual Report}. These publications contain useful income and balance sheet statistics as well as operating details taken from the annual reports submitted by individual motor carriers to the Interstate Commerce Commission. A uniform system of reporting is prescribed in 49 C.F.R. pt. 207 (1984).

\textsuperscript{26} From 1974 through 1979 the following revenue criteria were used to classify motor carriers by size: CLASS I carriers are those receiving annual gross operating revenues (including interstate and intrastate) of $3 million or more from property motor carrier operations; CLASS II carriers are those receiving annual gross operating revenues (including interstate and intrastate) of $500,000 to $2,999,999 from property motor carrier operations; CLASS III carriers are those receiving annual gross operating revenues (including interstate and intrastate) of less than $500,000 from property motor carrier operations. Class III carriers are not included in this study. \textit{AMERICAN TRUCKING ASSOCIATION, MOTOR CARRIER ANNUAL REPORT} iv (1979).

Beginning in 1980, the revenue classification was revised to: CLASS I carriers are those receiving annual gross operating revenues (including interstate and intrastate) of $5 million or more; CLASS II carriers are those receiving annual gross operating revenues (including interstate and intrastate) of $1 million to $4,999,999 from property motor carrier operations; CLASS III carriers are those receiving annual gross operating revenues (including interstate and intrastate) of less than $1 million from property motor carrier operations. Class III carriers are not included in this study. \textit{AMERICAN TRUCKING ASSOCIATION, MOTOR CARRIER ANNUAL REPORT} iv (1981). These changes recognize the impact of inflation on the revenue criteria.
\end{footnotesize}
or irregular route, authorized to serve an area over any appropriate route.\textsuperscript{27} Separate analysis of the financial position of each group will be performed to identify the differential impact of the economy and deregulation on different types of carriers.

\textbf{A. INDUSTRY SAMPLE}

The effects of deregulation and the economy (represented by 1976 and 1982 periods), and carrier size (Class I versus Class II), on the financial condition of the carriers was analyzed using Analysis of Variance (ANOVA).\textsuperscript{28} The ANOVA indicated that only the deregulation/economy factor and carrier size had a statistically significant effect on the Z" Score. This is illustrated by comparing the mean Z" Scores for carriers cross-classified by these two variables as shown below.

<table>
<thead>
<tr>
<th></th>
<th>Class I</th>
<th>Class II</th>
<th>Total</th>
</tr>
</thead>
<tbody>
<tr>
<td>1976</td>
<td>2.91(34)</td>
<td>4.83(28)</td>
<td>3.78(62)</td>
</tr>
<tr>
<td>1982</td>
<td>2.80(23)</td>
<td>.30(15)</td>
<td>1.81(38)</td>
</tr>
<tr>
<td>Total</td>
<td>2.87(57)</td>
<td>3.25(43)</td>
<td>3.03(100)</td>
</tr>
</tbody>
</table>

Clearly, the average Z" Score has dropped from well above the minimum score that signals a strong financial position (Z" = 2.6) to a Z" Score that is well within the gray area or "zone of ignorance." Most of this drop, however, can be attributed to the deteriorating position of the smaller Class II as opposed to the Class I carriers. On the average, the Class I carriers fell from a superior financial position relative to Class I carriers in 1976 to one of severe financial stress in 1982.

\textbf{B. PANEL SAMPLE}

As one would expect, the average financial performance of the panel sample is superior to that of the industry sample because the former consists only of carriers which have survived from 1976 to 1982. However,

\textsuperscript{27} For a complete description, see C. Taff, COMMERCIAL MOTOR TRANSPORTATION 111-13, 446-48 (1980).

\textsuperscript{28} Analysis of Variance (ANOVA) is a statistical technique for ascertaining from sample data whether one factor really influences another factor or whether the observed association was probably the result of sampling fluctuations. In our case, we are interested in knowing whether the financial position of general freight carriers is influenced by the combined effects of deregulation and the economy, independent of the effect of carrier size and service type. A basic description of the technique is found in R. Ferber & P. Verdoorn, RESEARCH METHODS IN ECONOMICS AND BUSINESS 80-82 (1962). A technical description can be found in W. Mendenhall & F. Reimnuth, STATISTICS FOR MANAGEMENT AND ECONOMICS 465-502 (1978). Because of the detailed nature of the statistical tests involved here, the results are not reported. The interested reader may obtain the tests from either of the authors.
the financial performance of the panel sample behaved in a pattern similar to the industry sample, as shown below.

<table>
<thead>
<tr>
<th></th>
<th>Class I</th>
<th>Class II</th>
<th>Total</th>
</tr>
</thead>
<tbody>
<tr>
<td>1976</td>
<td>4.47(21)</td>
<td>5.01(15)</td>
<td>4.69(36)</td>
</tr>
<tr>
<td>1982</td>
<td>3.69(20)</td>
<td>2.18(16)</td>
<td>3.02(36)</td>
</tr>
<tr>
<td>Total</td>
<td>4.09(41)</td>
<td>3.55(31)</td>
<td>3.86(72)</td>
</tr>
</tbody>
</table>

The Class I carriers again outperformed the Class II carriers. Their Z'' Score dropped from 4.47 to 3.69, while the Class II carriers’ Z'' Score dropped from 5.01 to 2.18. The panel sample is consistent with the industry sample and confirms the view that there has been substantial deterioration in the financial position of motor carriers, particularly that of the smaller carriers.

C. ANALYSIS OF FINANCIAL PERFORMANCE

Given the deterioration of the Z'' Scores, particularly of the Class II carriers, the causes of the decline need to be considered. The trend in the underlying financial ratios used in the Z'' model are displayed in Table IV. Comparison of the financial ratios in 1976 and 1982 for the industry sample indicate that Class II profitability declined much more than Class I profitability (NCOI/TA). The reduced profitability had two causes. As the economy declined, fixed costs could not be reduced as sales volume decreased, leaving the burden of those costs on the remaining business.\(^{29}\)

At the same time, price discounting allowed under the relaxed regulation brought down the rates and subsequently the profit margins. The Class II carriers were especially affected by these lower rates and higher costs. These carriers tend to be localized in a small geographic area and dependent on a narrow traffic base. Consequently, they have fewer opportunities than their larger competitors to differentiate their service and price among customers to minimize the impact of rate discounting. Negative profitability in turn drains retained earnings, i.e., equity, thus reducing the RE/TA and BVE/BVD ratios. (See Table IV.) At the same time, the working capital positions of the Class I and Class II carriers also reversed positions. In a recessionary period, motor carriers typically improve their liquidity as their cash position increases due to a reduction in capital ex-

\(^{29}\) The majority of economists have argued that these fixed costs are very small in the short run and insignificant over a very short span of years in trucking. This is attributed to the short life and mobility of trucking assets and the ability of a motor carrier to increase its capacity in small increments. See 2 A. Kahn, THE ECONOMICS OF REGULATION 179 (1971). A minority, but growing, viewpoint is that cost fixities do exist for motor carriers, such as the general freight type, because they are heavily dependent on terminal facilities to efficiently produce transportation service. See G. Chow, supra note 10, at 245-47.
penditurers, as evidenced by the improvement of the Class I carriers' WC/TA ratio. Unfortunately, the trucking industry has faced two economic recessions since 1979\textsuperscript{30} and sustained losses have caused significant deterioration in the working capital position of the Class II carriers.

<table>
<thead>
<tr>
<th>Financial Indicator</th>
<th>Class I 1976</th>
<th>Class I 1982</th>
<th>Class II 1976</th>
<th>Class II 1982</th>
</tr>
</thead>
<tbody>
<tr>
<td>$X_1$ WC/TA</td>
<td>-.002</td>
<td>.137</td>
<td>.124</td>
<td>-.029</td>
</tr>
<tr>
<td>$X_2$ RE/TA</td>
<td>.298</td>
<td>.321</td>
<td>.434</td>
<td>.104</td>
</tr>
<tr>
<td>$X_3$ NCOI/TA</td>
<td>.107</td>
<td>-.043</td>
<td>.110</td>
<td>-.127</td>
</tr>
<tr>
<td>$X_4$ BVE/BVD</td>
<td>1.178</td>
<td>1.089</td>
<td>1.773</td>
<td>.954</td>
</tr>
<tr>
<td>$Z''$ Score</td>
<td>2.914</td>
<td>2.797</td>
<td>4.828</td>
<td>.298</td>
</tr>
</tbody>
</table>

VI. CONCLUSION

The motor carrier industry enjoyed sustained traffic growth and stable regulatory environment through most of the 1970's. Relaxation of regulation by the ICC in 1977 was followed by total deregulation upon the enactment of the Motor Carrier Act of 1980. Meanwhile, traffic growth has slowed and even declined since 1979. Motor carriers have been thrust into a new and uncertain environment to which they must adapt.

Many motor carriers have been unable to deal with these changes and have gone out of business. This paper has summarized the financial position of the general freight motor carrier in 1982 relative to the financial position in 1976. An overall deterioration in the financial position of this carrier group was observed, but it was the smaller Class II carriers that suffered the most. This was evident in both the industry and the panel samples. The smaller carriers incurred relatively large losses compared to their larger counterparts and have been unable to sustain an adequate liquidity position. We are thus led to conclude that there are benefits to being large.

We also observed that reduced profitability was due in large part to sustained price competition reflected in discounting and lower rates. There is little doubt that this would have been minimized if the ICC had maintained strict control of rate competition and entry into the industry as in previous years. If deregulation means increased competition, the natural result is increased turnover via bankruptcy of competitors. Competition is, by its very nature, destructive. It is the responsibility of

\textsuperscript{30} Truck tonnage is highly correlated with the Federal Reserve Board Industrial Production Index. That index declined 3.6% in 1980, grew by 2.7% in 1981 and declined 3.8% in the first 8 months of 1982. G. Morris, supra note 5, at 40.
transportation policymakers to decide whether the current level of instability and the industry's precarious financial position are acceptable prices to pay for the lower rates offered to the public.
<table>
<thead>
<tr>
<th>BANKRUPT MOTOR CARRIERS</th>
<th>NON-BANKRUPT MOTOR CARRIERS</th>
</tr>
</thead>
<tbody>
<tr>
<td>1. Fowler &amp; Williams</td>
<td>1. H.C. Gabler Inc.</td>
</tr>
<tr>
<td>2. Fox &amp; Ginn</td>
<td>2. Harns Motor Express, Inc.</td>
</tr>
<tr>
<td>4. Baxter Transport, Inc.</td>
<td>4. Smiser Freight Service</td>
</tr>
<tr>
<td>5. Courier-Newson</td>
<td>5. Gator Freighways, Inc.</td>
</tr>
<tr>
<td>7. Eazor Express, Inc.</td>
<td>7. Murfreesboro Freight Line Company</td>
</tr>
<tr>
<td>10. Time D.C.</td>
<td>10. Inter-City Trucking Service, Inc.</td>
</tr>
<tr>
<td>17. Hemingway Transport</td>
<td>17. Pacific Inter Mountain Express</td>
</tr>
<tr>
<td>23. CHFL - Chief Freight Lines</td>
<td>23. Advance Transportation Co.</td>
</tr>
<tr>
<td>27. Arrow Transportation</td>
<td>27. North Penn Transfer Inc.</td>
</tr>
<tr>
<td>29. Cape Cod Overland Express</td>
<td>29. Campbell Sixty-Six Express Inc.</td>
</tr>
<tr>
<td>31. Long Transportation Co.</td>
<td>31. McNamara Motor Express Inc.</td>
</tr>
<tr>
<td>32. Monahan Transportation Inc.</td>
<td>32. Pilot Freight Carriers Inc.</td>
</tr>
<tr>
<td>33. North Shore &amp; Central</td>
<td>33. Estes Express Lines</td>
</tr>
<tr>
<td>34. Perkins Trucking Co.</td>
<td>34. Hunt Truck. Lines Inc.</td>
</tr>
<tr>
<td>35. Stand Transportation Inc.</td>
<td>35. AAA Trucking Corp.</td>
</tr>
<tr>
<td>36. Transport Motor Express</td>
<td>36. Lehman Cartage Inc.</td>
</tr>
<tr>
<td>40. Dodds Truck Line</td>
<td>40. Dearborn Motor Express Inc.</td>
</tr>
<tr>
<td>41. Highway Express Co.</td>
<td>41. E. W. Fraser inc.</td>
</tr>
<tr>
<td>42. Motor Transport Co.</td>
<td>42. Consolidated Mountain Freight Inc.</td>
</tr>
<tr>
<td>43. Western Transportation</td>
<td>43. Burnett Truck Line Co.</td>
</tr>
<tr>
<td>44. Atlas Freight Lines</td>
<td>44. LaPorte Transit Co. Inc.</td>
</tr>
<tr>
<td>45. Browning Freight Lines</td>
<td>45. Bee Line Motor Freight Inc.</td>
</tr>
<tr>
<td>46. IML</td>
<td>46. Wooster Express Inc.</td>
</tr>
<tr>
<td>47. Orscheln Bros. Trucking</td>
<td>47. S &amp; W Freight Lines Inc.</td>
</tr>
</tbody>
</table>

### APPENDIX II—BANKRUPT CARRIERS

<table>
<thead>
<tr>
<th>CODE #</th>
<th>Z&quot; SCORE</th>
<th>( X_1 ) (WC/TA)</th>
<th>( X_2 ) (RE/TA)</th>
<th>( X_3 ) (NCOI/TA)</th>
<th>( X_4 ) (BVE/BVD)</th>
</tr>
</thead>
<tbody>
<tr>
<td>35</td>
<td>11.67</td>
<td>.43</td>
<td>.84</td>
<td>.05</td>
<td>5.50</td>
</tr>
<tr>
<td>26</td>
<td>7.98</td>
<td>.32</td>
<td>.75</td>
<td>-.01</td>
<td>3.31</td>
</tr>
<tr>
<td>31</td>
<td>5.63</td>
<td>.33</td>
<td>.56</td>
<td>.01</td>
<td>1.52</td>
</tr>
<tr>
<td>42</td>
<td>4.56</td>
<td>.16</td>
<td>.51</td>
<td>.05</td>
<td>1.42</td>
</tr>
<tr>
<td>29</td>
<td>4.03</td>
<td>.16</td>
<td>.59</td>
<td>-.11</td>
<td>1.75</td>
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<tr>
<td>39</td>
<td>2.81</td>
<td>.01</td>
<td>.40</td>
<td>.00</td>
<td>1.34</td>
</tr>
<tr>
<td>33</td>
<td>2.58</td>
<td>.00</td>
<td>.73</td>
<td>-.06</td>
<td>.57</td>
</tr>
<tr>
<td>36</td>
<td>2.10</td>
<td>.12</td>
<td>.05</td>
<td>.00</td>
<td>1.11</td>
</tr>
<tr>
<td>30</td>
<td>2.03</td>
<td>.04</td>
<td>.41</td>
<td>-.05</td>
<td>.71</td>
</tr>
<tr>
<td>44</td>
<td>1.91</td>
<td>.09</td>
<td>.22</td>
<td>.04</td>
<td>.33</td>
</tr>
<tr>
<td>27</td>
<td>1.51</td>
<td>.00</td>
<td>.73</td>
<td>-.23</td>
<td>.69</td>
</tr>
<tr>
<td>25</td>
<td>1.44</td>
<td>-.03</td>
<td>.28</td>
<td>.00</td>
<td>.72</td>
</tr>
<tr>
<td>14</td>
<td>1.13</td>
<td>.01</td>
<td>.37</td>
<td>-.27</td>
<td>1.62</td>
</tr>
<tr>
<td>37</td>
<td>.98</td>
<td>.08</td>
<td>.23</td>
<td>-.11</td>
<td>.38</td>
</tr>
<tr>
<td>17</td>
<td>.87</td>
<td>-.02</td>
<td>.16</td>
<td>.02</td>
<td>.30</td>
</tr>
<tr>
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\[ Z" = 0.43(6.56) + 0.84(3.26) + 0.05(6.72) + 0.55(1.05) = 11.67. \]

Manual results may differ from listed Z" score due to rounding.

Source: All ratios are computed from basic income statement and balance sheet data contained in American Trucking Association, Motor Carrier Annual Report (various years).

### APPENDIX III—NON-BANKRUPT CARRIERS

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### APPENDIX IV

**CARRIERS IN INDUSTRY AND PANEL SAMPLE**

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44. Potter Freight Lines Inc.
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46. George Rimes Trkg Co. (27)
47. Rockford Milwaukee Disp (28)
48. Safeway Trucking Corp.
49. G & L Scheffler Trpt Inc. (29)
50. Shawmut Trptu Co. Inc.
51. M C Slater Inc. (30)
52. South Bend Frt Line Inc (31)
53. Standard Motor Frt Inc.
54. Strickland Trptu Co Inc.
55. TIME-DC Inc.
56. Tobler Transfer Inc. (32)
57. Turner Trucking Co. (33)
58. Valleries Trptu Serv Inc. (34)
59. Ward Transfer Inc.
60. Western Gillette Inc.
61. Willig Freight Lines (35)
62. Yellow Freight System Inc. (36)
FAA Punitive Certificate Sanctions: The Emperor Wears No Clothes; Or, How Do You Punish A Propeller?

LAWRENCE B. SMITH

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* Mr. Smith practices law in Tucson, Arizona. J.D., Stanford University; B.A. in Political Science, University of Virginia. In 1967-68, he worked in the Federal Aviation Administration's Office of General Counsel, in the branch that had oversight of the Agency's enforcement program. In 1980, he was a consultant to the U.S. General Accounting Office on the legal aspects of FAA enforcement. Mr. Smith holds commercial pilot and flight instructor certificates with multi-engine and instrument ratings.
I. INTRODUCTION

Overlooked in the mass of information continually produced by the Federal Aviation Administration (FAA) is a set of statistics published by the Office of Chief Counsel that should be of special concern to pilots and mechanics.1 These numbers tell us that of 4,000 safety enforcement cases closed by legal action each year, in about 2,400, or 60%, licensees have their FAA certificates suspended or revoked for violation of a safety rule.2 The balance result in civil money penalties.3 For private and student pilots (i.e., non-professionals), the proportion of suspensions and revocations rises to an astonishing 87%, the balance resulting in civil money fines.4 These sanctions are imposed through the use of two entirely separate and independent systems of justice, one administrative, the other judicial. Every year as many as 700 men and women who hold commercial pilot, air transport pilot or mechanic licenses (certificates mandatory for their employment) are suspended for periods up to one year.5 Aside from the severe monetary loss, suspensions often cause the person to lose his job and substantial inconvenience for employers, particularly the smaller operator who must replace him.

Since 99% of all FAA enforcement cases are first offenses,6 and generally involve inadvertent violations of traffic and other technical safety regulations7 which have no criminality attached,8 the question arises: why is it that such a large proportion of these cases are routinely resolved by means of a punishment far too severe for the offense, rather than the traditional money fine? The answer is that Congress has never authorized use of license suspensions and revocations as punishment for violations of air-safety regulations, nor their imposition in an administrative forum.

In support of this theme are the following propositions: 1) The only

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1. FEDERAL AVIATION ADMINISTRATION, CHIEF COUNSEL’S OFFICE ENFORCEMENT REPORT (1979) [hereinafter cited as ENFORCEMENT REPORT].
2. Id. at 1, 6.
3. Id.
4. Id. at 10.
5. Id. at 3, 8.
6. See FEDERAL AVIATION ADMINISTRATION, SURVEY OF THE ENFORCEMENT PROGRAM, 1971, at app. B (1972) (internal FAA General Counsel document) ("The number of repeat violators are small, probably less than one percent ....")
time Congress considered what kind of enforcement system to provide for air-safety violations, it chose a civil money penalty scheme with the right to a jury trial; 2) The few cases that have upheld the legality of FAA’s punitive certificate sanction system are all based upon a fundamental error concerning legislative authorization; 3) This error has been perpetuated by government aviation officials who are violating the public trust by refusing to correct it; 4) This behavior is part of an ongoing effort to cover up lack of legislative authority for certificate penalties; 5) A major part of this coverup is the FAA’s failure to promulgate as formal regulations basic enforcement policies that affect civil rights of airmen, resulting in many serious violations of the Administrative Procedure Act.9

Several salient facts underscore the legitimacy of the issues raised. Since 1926, the seminal year for federal regulation of aviation,10 50,000 American citizens have had their pilot, navigator, flight engineer or mechanic licenses suspended or revoked for the sole purpose of punishing them for violating an air-safety regulation.11 Never has the policy of using such penalties, or imposing them through an administrative rather than a judicial system, been debated in Congress or committee. There is not now, nor has there ever been, any statute that authorizes their use. There is no regulation that does so, nor has there been for forty-five years, since the sole governing rule12 was repealed by government aviation officials.13 Since that event they have avoided instituting rulemaking procedures through which airmen could challenge the system and force public debate.

The FAA’s punitive certificate sanction system is entirely the creation of zealous public officials who in 1926 refused to accept the enforcement system that Congress had just enacted. Ever since, they and their successors, by all manner of devices, have shielded that fact from scrutiny.

II. HOW ENFORCEMENT WORKS

A. BACKGROUND

The vast majority of air-safety cases involve pilots, mechanics, air carriers and air-taxi operators who are charged with violations of air-traf-

10. See infra text accompanying notes 53-56.
11. Author estimate based mainly on sampling count of FAA enforcement docket index cards, and other sources.
12. Department of Commerce, Air Commerce Regulations § 74(a), (f) (1926). ("Pilots’ and mechanics’ licenses will be suspended or revoked for (A) Violating any provision of the air commerce act of 1926 or these regulations. . . . (F) Violating air traffic rules.") [hereinafter cited as 1926 Rule].
13. For discussion of how and when this rule was eliminated, see infra text accompanying notes 138-44.
fic, record-keeping, maintenance and operations regulations. These are
prosecuted by either a certificate action pursuant to the claimed authority
of section 609 of the Federal Aviation Act,\textsuperscript{14} where punishment is by sus-
pension or revocation of a given certificate (license), or by a civil penalty
action under section 901 of that Act,\textsuperscript{15} which may lead to payment of a
money fine by compromise or judicial action.

These two avenues for air-safety enforcement should be distin-
guished from qualifications actions by the FAA. For example, if an airman
applies for a particular type of certificate (pursuant to section 602 of the
Federal Aviation Act), and is then denied its issuance on grounds he does
not meet "pertinent rules, regulations, or standards," he may appeal that
denial to the National Transportation Safety Board (NTSB), which may
overrule the FAA and direct that the certificate be issued.\textsuperscript{16} After having
been issued a certificate, developments may occur which indicate that the
holder no longer meets the qualifications set down for it. For instance a
pilot may land short and wreck his aircraft, or the FAA may learn that he
has a medical problem that he didn't report. He may be asked to take a
flight test, or undergo a medical exam by specialists. Should he refuse,
the agency will institute an action under section 609 (also appealable to
the NTSB) to suspend the certificate or rating in question until he does so,
and passes.\textsuperscript{17} Should he flunk, the FAA will revoke.\textsuperscript{18} These qualifi-
cations matters account for only a small minority of section 609 cases ap-
pealed to the NTSB.\textsuperscript{19} Rather than risk delay, expense and an adverse
decision (basically, only the reasonableness of the FAA request can be
contested), it is usually far more practical for the airman to take the flight
test or exam promptly and resolve the matter.

These cases highlight a key point—section 609 is used for two dis-

\textsuperscript{14} 49 U.S.C. app. § 1429(a) (1982).
\textsuperscript{15} 49 U.S.C. app. § 1471(a)(1) (1982). For other discussions of FAA enforcement which
mention other safety duties, see generally Kovarik, Procedures Before the Federal Aviation Ad-
mistration, 42 J. Air L. & Com. 11 (1976); Hamilton, Administrative Practice Before the NTSB:
Problems, Trends and Developments, 46 J. Air L. & Com. 615 (1981); Pangia, Handling FAA
Enforcement Proceedings: A View From the Inside, 46 J. Air L. & Com. 573 (1981). None of
these articles address the issues raised here.
\textsuperscript{16} 49 U.S.C. app. § 1422(b) (1982).
\textsuperscript{17} See Compliance and Enforcement Program, FAA Order 2150.3, ¶ 203.c(1)(c), at 13
\textsuperscript{18} Id.
\textsuperscript{19} The NTSB docket staff has advised the author that the Board receives 700 adminis-
trative appeals a year from the FAA (all numbers approximate): 200 are appeals from a denial of an
application for a certificate under section 602; 500 are appeals from section 609 actions. Of
these 500, 10 cases will involve an airman who refuses to be reexamined for skill purposes, or
no more than 2% of section 609 cases; 15 cases, or 3%, involve medical certificates already
issued, but a new disability is discovered; the balance, or 475, will be strictly to impose a sus-
pension or revocation as punishment for the violation of a safety rule.
tinct and mutually exclusive purposes—a dichotomy which cannot be discerned from any language in the section itself. One branch involves cases that charge a violation of a safety regulation, the other a failure to satisfy license qualifications.²⁰ The statute clearly speaks to the latter, but says nothing of the former.²¹

Since certificate sanctions will literally shut down the operation, put people out of work, and disrupt service to the public, they are normally not used against a business entity like an airline, air-taxi operator, or repair shop. Rather, FAA imposes civil penalties which it can be fairly certain will be paid.²² This is ensured by the cost of legal defense and the need to avoid strained relations with inspectors who may soon return to the certificate holder's shop. The ratio of certificate to civil penalty actions in airline cases, most of which originate with their pilots or mechanics, is about 20/80.²³ In general aviation, this trend is reversed, 67/33, while the overall ratio is 60/40.²⁴ It is likely because of FAA sensitivity to the great salary loss occasioned by a suspension that airline captains pay a far higher ratio of civil penalties than the commuter pilot or private pilot. Civil penalties for private pilots generally run between $100 and $200; for commercial pilots, $200-$300; and for airline pilots, $300-$1,000.²⁵ A civil-money fine is, of course, almost always a far less drastic solution to a violation case than a certificate action.

Violation cases are investigated at the local level, then screened at regional headquarters and turned over to regional counsel for prosecution. An enforcement handbook provides overall guidance.²⁶ Most violations, FAA concedes, are inadvertent²⁷ and 99% of them are first offenses.²⁸ If it is minor and a first offense, the inspector may take administrative action by a warning letter.²⁹

B. THE BASIC PROBLEM

The key problem with FAA enforcement is that it consists of two unrelated systems, or tracks, of justice, either of which may be invoked by FAA officials in prosecuting a given offense: 1) Section 901 civil money

²¹ See infra text accompanying notes 47-57.
²³ ENFORCEMENT REPORT, supra note 1, at 4.
²⁴ Id.
²⁵ See OFFICE OF CHIEF COUNSEL, FEDERAL AVIATION ADMINISTRATION, BRIEFING BOOK FOR TESTIMONY BEFORE ANDERSON AVIATION SUBCOMMITTEE, H.R. 7488, July 1 & 2, 1980 [hereinafter cited as BRIEFING BOOK].
²⁸ See supra note 6.
penalty actions; 2) Section 609 punitive certificate actions. Subject only to handbook guidelines, rather than any statute or regulation, FAA regional counsel can initiate a given violation case on whichever track he chooses.\textsuperscript{30} In one case, the certificate track may be used and the action initiated with a form letter called a Notice of Proposed Certificate Action.\textsuperscript{31} It would propose, for example, to suspend the pilot’s license for a period of up to one year (the FAA has no fixed penalties), usually in increments of 30, 60, 90 days, and so forth. In another case, which might involve an identical violation, the agency may well impose a civil penalty. This, too, would be initiated by a form letter, informing the accused that the FAA will accept so many dollars in compromise.\textsuperscript{32} Regardless of which form letter is used, the allegations of the acts complained of and regulations violated will remain the same.

On the civil penalty track, should the pilot ignore the letter and take the initiative and wish to contest the matter, the FAA must turn the case over to a United States Attorney for action in the United States District Court.\textsuperscript{33} There the airman (or government) may “demand trial by jury of any issue of fact.”\textsuperscript{34} Should he lose and the judge impose a fine, the maximum is $1,000 per violation.\textsuperscript{35}

On the certificate track, should the accused ignore the notice, the FAA will issue an order in the name of the Administrator that commands the suspension or revocation of his license.\textsuperscript{36} The limit on either is one year.\textsuperscript{37} On this track, the burden falls on the airman to appeal to the NTSB, during which appeal, absent an FAA declaration of emergency, the order is stayed.\textsuperscript{38} There he will have a trial de novo before an administrative law judge (ALJ).\textsuperscript{39} Either side may appeal the ALJ’s decision to the full board, which acts in a similar capacity to a court of appeals; from there only the airman may appeal to a United States court of appeals.\textsuperscript{40}

Should the NTSB find the airman guilty of a violation and deserving of punishment, it will affirm the FAA order, or modify it by reducing the term

\textsuperscript{31} Id. at ¶ 1203.a, at 168-70, and fig. 12-8, at 214-18; see also 14 C.F.R. § 13.19(c) (1984).
\textsuperscript{32} Id. at ¶ 1202.b, at 164, and figs. 12-1 to 12-5, at 201-09; see also 14 C.F.R. § 13.15(b) (1984).
\textsuperscript{33} 49 U.S.C. app. § 1473 (1982).
\textsuperscript{34} 49 U.S.C. app. §§ 1422(b) (1982).
\textsuperscript{35} 49 U.S.C. app. §§ 1429(a) (1982).
\textsuperscript{37} See 49 U.S.C. app. § 1422(b) (1982).
\textsuperscript{38} 49 U.S.C. app. § 1441(a) (1982).
\textsuperscript{39} Id.
\textsuperscript{40} 49 U.S.C. app. §§ 1429(a), 1486 (1982).
of suspension or revocation, but it cannot under any circumstances switch to a money penalty. Likewise, the district court judge cannot switch from a pecuniary fine to a certificate suspension or revocation. The two enforcement systems are wholly independent of one another.

Logically, then, the FAA’s position must be that it can operate its enforcement program with two separate yet unequal systems (one administrative, the other judicial), and choose either in its sole discretion. Yet Congress guaranteed airmen the right to jury trial for violation of “any rule, regulation, or order.” Section 901 also states that airmen “shall be” subject to a civil money penalty. It is improbable that Congress would authorize an executive branch official to deny licensees their statutory privileges by the simple expedient of sending out a form letter that puts the case on the certificate-administrative law track.

To underscore the contradictions of logic and common sense the two-track enforcement program engenders, consider, for example, the pilot against whom FAA has proposed a sixty-day suspension. Suppose he is an airline captain, who then asks FAA regional counsel if he can pay a civil penalty instead, because the suspension will cost him, at $90,000 per year, $15,000. Assume also that he is sincere, has no prior record, and has just accomplished a good checkride. The FAA lawyer can relent and agree to accept a certified check for $500, simultaneously drop the certificate case, and close out the file with a civil penalty letter of receipt.

In the letter of receipt he prepares, the FAA official will flip-flop from citing section 609 as authority for the legal action to section 901, which carries with it a right to jury trial. But this procedure precludes any chance for the airman to ever demand that right! And, as we have just seen, this same lawyer could have started the case off, in the first instance, on the civil penalty track. In short, by claiming it can operate the two tracks in parallel and choose between them at will, FAA takes away the airman’s right to jury trial.

III. ENFORCEMENT PERSPECTIVE

The core issue is whether Congress has ever authorized a system of administrative enforcement to decide issues of guilt or innocence, with certificate suspension or revocation as the penalty. If Congress has not

45. Id.
so authorized the FAA, how have federal officials been able to continue operating in such a manner for more than half a century?

A. THE ACT AND LEGISLATIVE HISTORY

In looking at FAA enforcement history, the stark contrast in statutory language between sections 901 and 609 is apparent. Section 901 of the Act is written in clear, precise and unequivocal terms:

Any person who violates . . . any provision of . . . [this Act], or any rule, regulation, or order issued thereunder . . . shall be subject to a civil penalty of not to exceed $1,000 for each such violation. . . .

Any civil penalty may be compromised by the [Administrator] . . .

The trial of any offense under this [Act] shall be in the district in which such offense is committed. . . .

This language is exclusive; nowhere does it even hint of a parallel or alternative enforcement system with a different penalty.

In contrast, section 609 provides in pertinent part:

The [Administrator] may, from time to time, reinspect any civil aircraft, aircraft engine, propeller, appliance, air navigation facility, or air agency, or may reexamine any civil airman. If, as a result of any such reinspection or reexamination, 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 type certificate . . . airman certificate . . .

The provision contains no language concerning offenses, regulations, violations, sanctions or penalties; this section has remained unchanged in this regard since 1938, and section 901 has been essentially the same since 1926. Yet the FAA claims that the punitive certificate sanction system is authorized by the vague language in section 609, "[if the Administrator] determines that safety in air commerce or air transportation and the public interest requires."

In order to resolve the issue of the extent of legislative authorization,

49. 49 U.S.C. app. § 1473(a) (1982). See also id. § 1473(b)(1), which provides:
   Any civil penalty imposed or assessed under this chapter may be collected by proceedings in personam against the person subject to the penalty. . . . Such proceedings shall conform as near as may be to civil suits in admiralty, except that . . .
   either party may demand trial by jury of any issue of fact, if the value in controversy exceeds $20, and the facts so tried shall not be reexamined other than in accordance with the rules of the common law.
52. Air Commerce Act of 1926, ch. 344, § 11(b), 44 Stat. 568, 574.
one must examine Congressional activity in the seminal year of 1926. On May 20, 1926, the same day that it enacted the Air Commerce Act, Congress adopted an official history of that legislation, which proclaimed:

The enforcement of the provisions of the Air Commerce Act of 1926 and regulations thereunder is for the most part by means of a system of civil administrative penalties similar to those by which the customs and navigation laws have always been enforced. A flat penalty prescribed by the statute is imposed by subordinate Federal administrative officers for the violation. The offender then has the right of appeal to the proper Secretary [Commerce, War and Post Office]—the Secretary of Commerce, for instance, in the case of air traffic rules. The Secretary may mitigate or remit the penalty so as to fit the offense, and his action is final. The penalty as thus finally determined may be collected by proceedings in personam against the person subject to the penalty . . . . These proceedings will conform as nearly as may be to civil proceedings in admiralty, save that trial by jury may be had . . . .

In providing for federal regulation of aviation, Congress wisely gave careful consideration to the kind of enforcement system needed to back up those regulations. It looked at alternatives: the House approved a bill that provided for "[a] criminal penalty of a fine not exceeding $500 or imprisonment not exceeding 90 days." The Senate bill provided for the enforcement of the provisions of the act and regulations thereunder through a system of flat civil penalties . . . ." In conference committee the Senate scheme prevailed.

The 1926 history reflects that Congress never considered using suspensions or revocations as a form of punishment for rules violations (much less trying them by administrative justice). In creating its enforcement system, Congress asked and answered at least six basic questions: 1) Who would be prosecutor? (United States attorney); 2) How would the case be initiated? (like a civil case in admiralty); 3) In what court? (United States district court); 4) In what venue? (district where offense committed); 5) Right to jury? (yes); 6) What kind of penalty? (money fine).

53. Id.
54. CIVIL AERONAUTICS, LEGISLATIVE HISTORY OF THE AIR COMMERCE ACT OF 1926, at 59 (1928) [hereinafter cited as 1926 History].
55. Id. at 45. Also relevant is a comparison of the provisions of the Air Commerce Act of 1926 as passed by the Senate and as passed by the House (S. 41, 69th Cong., as passed by the Senate December 16, 1925, and S. 41, 69th Cong., as passed by the House of Representatives April 12, 1926). The House amendment was in the nature of a substitute for the Senate provisions and struck out all after the enacting clause of the Senate bill. Id. at 9.

The criminal penalties were set forth in section 13(a) of the House version of S. 41. Id. at 20. Section 13(d) of that version provided that the states as well as the United States may prosecute the offenses prescribed by the act or regulations thereunder, and may also prescribe penalties or forfeitures, civil or criminal, to be imposed for such offenses in lieu of the federal penalties under subdivision (a). Id. at 47.
56. Id. at 51.
It is indisputable that the sole enforcement system provided by Congress in 1926 was civil money penalties with right to jury trial in regular federal courts. The salient question then becomes: Did Congress thereafter authorize use of a punitive certificate sanction as an additional or alternative method of punishment, and the substitution, in the sole discretion of an official of the executive branch, of a one-man administrative hearing for the right to trial by jury? The FAA lawyers' position has always been that the Civil Aeronautics Act of 1938 established the punitive suspension/revocation system. Yet close scrutiny of regulatory and legislative history reveals that this is manifestly not the case.\textsuperscript{57}

\textbf{B. \textit{Cases Challenging the Punitive Certificate Sanction Authority}}

The use of punitive certificate sanctions has been directly challenged in three reported cases. Remarkably, each holding in these cases is premised on the misconception that punitive suspensions and revocations began in 1938 with the enactment of the Civil Aeronautics Act. Yet, the first rulebook in 1926 told pilots and mechanics their certificates would be suspended or revoked for "[v]iolating any provision of the Air Commerce Act of 1926 or these regulations [or for] violating air traffic rules."\textsuperscript{58} Thus, the court in \textit{Wilson v. Civil Aeronautics Board}\textsuperscript{59} misconstrued the question by phrasing the key issue as: "Whether, in circumstances in which the Civil Aeronautics Board does not find the pilot to be unqualified to fly, the Board is empowered under section 609 of the Civil Aeronautics Act [of 1938] to suspend his airman certificate as a deterrent sanction."\textsuperscript{60}

Similarly, the court in \textit{Hard v. Civil Aeronautics Board}\textsuperscript{61} was quite definite in expressing it's belief that the system started with the Act of 1938. The court held: "A protocol statement, part of the Congressional declaration of policy in section 2 of the Civil Aeronautics Act of 1938 is the main prop for Board action under section 609 of the Act . . . ."\textsuperscript{62} Finally, \textit{Pangburn v. Civil Aeronautics Board}\textsuperscript{63} held:

Under the provisions of the 1938 Act suspensions were frequently im-

\textsuperscript{57} See 1926 Rule, supra note 12; see also Brief for Respondent at 21, Wilson v. CAB, 244 F.2d 773 (D.C. Cir.), cert. denied, 355 U.S. 870 (1957).
\textsuperscript{58} See 1926 Rule, supra note 12.
\textsuperscript{59} 244 F.2d 773 (D.C. Cir.), cert. denied, 355 U.S. 870 (1957). The briefs in this case may be found at Vol. 1163, Records and Briefs, United States Court of Appeals, D.C., of the D.C. Bar Association.
\textsuperscript{60} 244 F.2d at 773-74.
\textsuperscript{61} 248 F.2d 761 (7th Cir.), cert. denied, 355 U.S. 960 (1957).
\textsuperscript{62} 248 F.2d at 761-62. Section 2 instructed the Civil Aeronautics Authority (later CAB) that it should consider "as being in the public interest . . . . the regulation of air transportation in such manner as to . . . assure the highest degree of safety . . . ."
\textsuperscript{63} 311 F.2d 349 (1st Cir. 1962).
posed as a deterrent sanction notwithstanding the apparent technical qualifications of the pilot. The imposition of a suspension as a sanction was challenged under the 1938 Act in Wilson v. Civil Aeronautics Board . . . . Relying on the consistent administrative practice of over 4,000 such suspensions during the course of administering the [1938] Act . . . . the [Wilson] court held that the administrative practice should be sustained . . . ."64

In these cases, the courts’ focus was on the 1938 Act; the decisions make no mention of the more relevant 1926 Act. Both the courts and the challengers were unaware both that the Civil Aeronautics Board (CAB) and earlier government aviation officials actually relied on the 1926 Act as their legislative authority for the suspension system65 and of the existence of the 1926 Rule. The challengers’ basic argument was that section 609, because it said nothing about violations, offenses, regulations or sanctions, could not possibly have been meant to authorize punitive suspensions.66 The CAB took advantage of the focus on the 1938 Act, although in their brief in Wilson they had acknowledged that the system started earlier67 and that the 1938 legislation was not determinative.68

The decisions in Wilson, Hard and Pangburn rest upon a false premise; this is fundamental to understanding how the punitive certificate sanction system has survived attack. Since the system actually started in 1926 and the government really claimed Congress had authorized it in that year, the only possible relevancy that the 1938 Act could have had was if it modified or clarified the system in some manner, which the government impliedly conceded it did not. Despite their knowledge that the 1938 Act has no relevance to the origins of the punitive certificate sanction system, FAA officials continue to defend section 609 actions by citing Wilson, Hard and Pangburn.69 Ironically, while they continue to do this, the Agency’s own official history relates:

The familiarization period over, the Aeronautics Branch began meting out other forms of punishment in addition to reprimands—fines, suspensions and revocation. . . . 22 percent had their licenses suspended. The usual fine was $25.

When Young succeeded MacCracken as Assistant Secretary [of Commerce] in October 1929, the Branch gradually began to deal more severely with violators. . . . the Aeronautics branch turned to suspensions as a primary enforcement tool. At the same time revocations were being handed out . . . .

64. Id. at 354; see also Specht v. CAB, 254 F.2d 905 (8th Cir. 1958).
65. See Brief for Respondent at 8, 17 n.14, 20, 21, 22, 27, Wilson.
66. See Brief for petitioner at 13-16 and Reply Brief for Petitioner at 1-11, Wilson.
67. See Brief for Respondent at 21, Wilson.
68. See infra notes 98 and 99 and accompanying text.
69. See infra note 73 and accompanying text. See also Barnum v. National Transp. Safety Bd., 595 F.2d 859 (D.C. Cir. 1979); Haines v. Department of Transp., 449 F.2d 1073 (D.C. Cir. 1971); Walker v. CAB, 251 F.2d 954 (2nd Cir. 1958).
with greater frequency. . .

We can see from this history and the existence of the 1926 Rule on the subject that CAB lawyers deliberately led the court in Wilson to believe 1938 to be the key year, then cited that case as authority in Hard, which came down later the same year. By the time of Pangburn in 1962, FAA officials merely needed to cite Wilson for authority in order to sustain their certificate actions. This same approach was repeated as late as 1977 in McGee v. Secretary of Transportation, the latest challenge to section 609. Nothing in these case decisions or in the public record indicates that FAA officials have ever made any effort to correct this judicial misunderstanding about the 1938 Act. Such government agency failure to correct a gross error upon which the rights of so many citizens depend is an unconscionable breach of public duty. The evidence is compelling that this conduct has been a part of a deliberate effort to cover up the lack of legislative authority for the punitive suspension system. FAA lawyers know full well that the only enforcement system Congress authorized in 1926 was the civil money fine with right to jury.

This history explains why no request to Congress has been made by any government agency for authorization of punitive certificate sanction power and why committee hearings, which would have allowed public input into this major policy, have never been held. It explains why FAA officials, in particular, have never asked Congress to amend section 609 so that it plainly authorizes the current system. Such public action would risk exposing the inconsistencies and paradoxes of the FAA’s two-track enforcement program, including the following:

1) Congress, after careful consideration in 1926, clearly stated that in the case of a rules violation, pilots and mechanics had the right to pay a money fine and “demand” a jury trial. Congress has never rescinded that right, yet executive branch officials now deny this right by the simple expedient of sending out a form letter. Neither the FAA nor the courts have ever focused on this blatant inconsistency.

71. See infra notes 93 and 94 and accompanying text.
72. See 248 F.2d at 764.
73. No. 76-1092 (D.C. Cir. 1977). See Brief for Respondent; the briefs in this case may be found at Vol. 2910, Records and Briefs, United States Court of Appeals, D.C., of the D.C. Bar Association.
74. See infra sec. VI for details and discussion of this coverup.
75. It has been my experience that if you ask an FAA or NTSB lawyer what year Congress authorized punitive certificate sanctions, he will answer 1938, and cite the Wilson, Hard and Pangburn cases; he will also agree that the only enforcement system Congress authorized in 1926 was the civil money penalty with right to jury trial.
2) Suspension and revocation of any license has always been seen as a harsh form of punishment reserved for flagrant offenses (money fines are the norm). On what basis would Congress, leaving no legislative history to support such a drastic measure, single out aviation and approve this extraordinary use of certificate sanctions rather than money fines?

3) Congress specifically focused in 1926 on the issue of penalties, and ultimately set a limit of $500 per violation ($1,000 after 1938). There is no indication in the 1938 Act that Congress was dissatisfied with this basic system—that Congress increased the maximum fine in 1938 shows that it considered the question of penalties and determined that an increased ceiling, not a suspension system, was appropriate. License suspension is totally inconsistent with this increased ceiling, since it often means the loss of thousands of dollars in wages and possibly even the pilot or mechanic’s job.

4) Why would Congress authorize a two-track enforcement program that prohibits an ALJ from switching from an extreme form of penalty, suspension or revocation, to the customary money fine, then turn around and give that purely discretionary power to an executive branch lawyer? No such intent is expressed in any of the statutes.

Once one understands that these paradoxes accurately reflect the state of the FAA’s two-track program, it can be seen that any agency claim that Congress has ever authorized punitive administrative certificate sanctions is illogical and fails upon careful scrutiny of the public record. In light of these shortcomings in the government’s position, it is alarming that this program has been able to endure without being successfully challenged.

IV. THE HEART OF THE CONUNDRUM—THE WILSON CASE

It took thirty years after 1926 before anyone mounted a serious legal challenge to punitive certificate sanctions. This time lag was probably due to the cost of litigation, the small size of the aviation community in the 1920’s, the Great Depression, World War II, and the past unwillingness of most citizens to believe that their government could be less than honest. That challenge had to await the growth and financial muscle of the Air Line Pilots Association (ALPA) in the 1950’s. ALPA launched its first attack in Wilson v. Civil Aeronautics Board76 in 1957; Hard v. Civil Aeronautics Board77 was decided in that same year. Pangburn v. CAB78 followed

76. 244 F.2d 773; see supra text accompanying notes 59-60.
77. 248 F.2d 761; see supra text accompanying notes 61-62.
in 1962. After a long hiatus, ALPA tried again in 1977 with McGee v. Secretary of Transportation. In each case the unsuccessful challenger was an airline captain.

The Wilson case became the touchstone for the other rulings. Captain Wilson's lawyers based their challenge on section 609 of the Civil Aeronautics Act of 1938. The reasons they did so and the arguments they used are obvious: the section says nothing of violations, regulations, offenses or punishment. Since Congress so precisely described these procedures in section 901, the lawyers reasoned, why would Congress sanction a new system without plainly saying so? Why would the lawmakers intermingle such a new system and unrelated qualifications matters like "reinspection" and "reexamination"? Why would section 609 include only one animate object in a long list of inanimate objects? (How do you punish a propeller?) Wilson's lawyers made many of these arguments and more.

CAB argued that it needed the punitive suspension power for "discipline" and "deterrence." Its lawyers argued, and the court so held, that "[b]y resting suspension on a Board determination that 'the interest of the public so requires,' Congress conferred broad discretionary authority upon the Board." Offering no rationale in its one-page decision, the court brushed aside any argument that Congress intended section 901 to be the exclusive mechanism for punishing violators. As the 1926 legislative history reflects, this is precisely what Congress did in fact intend,

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78. 311 F.2d 349; see supra text accompanying notes 63-64.
80. 49 U.S.C. app. § 1429(a) (1982). The 1938 version read, in part:
    The Authority [CAA Administrator] may, from time to time, reinspect any aircraft, aircraft engine, propeller, appliance, air navigation facility, or air agency, may reexamine any airman, and after investigation, and upon notice and hearing, may alter, amend, modify, or [the Board may] suspend, in whole or in part, any type certificate, production certificate, airworthiness certificate, airman certificate, air carrier operating certificate, air navigation facility certificate, or air agency certificate if the interest of the public so requires, or [the Board] may revoke, in whole or in part, any such certificate for any cause which, at the time of revocation, would justify the Authority [Administrator] in refusing to issue the holder of such certificate a like certificate.
81. 49 U.S.C. § 1471(a)(2) (1982). This point would have been made more clear had Wilson's lawyers argued the premier maxim of statutory interpretation, expressio unius est exclusio alterius.
82. See Brief for Petitioner, Wilson. See also Brown v. CAA, 112 F.2d 737 (9th Cir. 1940), reh'g dismissed as moot, 119 F.2d 172 (9th Cir. 1941) ("If the suspension [imposed under section 609] was purely punitive the application [for supersedeas] might be granted but the order also requires that . . . the petitioner should take [a] proposed examination before his right to fly is restored."). The court thereby hints it might have found that section 609 did not authorize punitive suspensions, had time not rendered the case moot.
83. Id. at 11-19.
84. 244 F.2d at 774.
85. Id.
one system (civil) to the exclusion of another (criminal). The basic reason for any system of law enforcement is to provide discipline and deterrence; just how that will be accomplished, and whether it is sufficient for the task, is a legislative decision for Congress, not the courts. Congress clearly chose a particular system in 1926 and did not alter it in 1938. The Wilson court's reliance on the "public interest" clause of section 609 placed undue emphasis on that section without examining the entire legislative scheme.

The suggestion by the Wilson court that the phrase "if the interest of the public so requires" was intended as a comprehensive grant of power to start a new enforcement system is untenable. The phrase "public interest" is a condition subsequent to first re inspecting, reexamining or investigating to determine if the airman, appliance or propeller continues to meet regulatory standards. So long as it was deemed to be "in the public interest," only then could a decision be made to amend, modify, suspend or revoke in order to correct any deficiency. That phrase was clearly intended to be a limitation of the Board's discretion rather than a grant of power to take action.

The appellate court in Wilson simply refused to upset a longstanding enforcement system and used the "public interest" clause as a legal handle on which to base its ruling. "This consistent and, until now, unchallenged administrative practice," the Wilson court said, "will not be overturned except for very cogent reasons . . . ." Concerned it might harm air-safety if it did so, the court held: "The most cogent of reasons—air safety—supports the administrative practice here under attack." Hard, Pangburn, and McGee all struck the same note. These courts were really making a legislative, rather than a judicial determination—we think it is a good idea that you have this power.

The empty logic of the "public interest" argument has been recently exposed. In Jensen v. Administrator of Federal Aviation Administration, the court ruled that the FAA had, in violation of the Alcoholism Act, improperly denied a medical certificate to Jensen, a commercial pilot, who had admitted to a prior history of alcoholism. FAA argued that its "two-tier" procedure (regular application, and if denied, request for exemption), which leaves the matter strictly within the discretion of agency personnel, negated any contention that Jensen was being denied his medical

86. See 1926 History, supra note 54.
87. 244 F.2d at 774. Contra Global Van Lines v. ICC, 714 F.2d 1290, 1295-96 (5th Cir. 1983) ("A general congressional exhortation to go forth and do good, without more, is not a proper foundation for the sound development of administrative law").
88. Id. See also Nadiak v. CAB, 305 F.2d 588, 595 (1962) ("The public—including judges who fly—has a vital interest in air safety.").
89. 641 F.2d 797 (9th Cir. 1981), vacated, 680 F.2d 593 (9th Cir. 1982).
certificate solely on ground of prior alcoholism in violation of the Alcoholism Act. Finding that argument "without merit," the court explained:

[Even if this court accepted the FAA's "two tier" argument, the exemption procedure does not comport with due process. . . .

Due process requires that for a meaningful review of an agency decision, the agency must have articulated standards governing its determination.

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).90

Jensen pulls the rationale right out from under Wilson. Since "public interest" and "safety" do not comport with due process standards, they can hardly provide the foundation for an entire system of enforcement.

By directly attacking section 609 in Wilson, the ALPA lawyers failed to seize upon the real issue in the case—when did Congress, having in 1926 designed an enforcement scheme which provided for civil money penalties and a jury trial, thereafter add punitive certificate sanctions and an administrative hearing? The paradox of Wilson is apparent: legislative history aside, the key phrase "public interest," on which the court pinned its decision, did not exist in 1926,91 so it could not have created the system! Had the court recognized that Commerce officials initiated the certificate system in 1926, then CAB's defense of it would necessarily have been forced into that time frame, and the government would have been compelled to admit the internal inconsistency of their program.

Yet astonishingly, the CAB did inform the Wilson court—in a roundabout fashion—that punitive suspensions started in 1926, not 1938. It is clear that this acknowledgement evaded the grasp of the court and Wilson's lawyers. The latter made no mention of it in their reply brief92 and neither the Wilson decision nor subsequent cases have recognized this fact. How did such an oversight occur?

The answer is that the CAB lawyers apparently overwhelmed the court and opposing counsel with a series of clever, and often specious, arguments which they loaded with statements about "public interest" and "air safety." They made it seem that they were arguing that Congress authorized certificate sanctions in 1938, but never directly said so: "The situation is simply the familiar one in which more than one sanction is provided for a particular offense, a point made clear, we think, by the

90. Id. at 799 (citations omitted).
91. See Air Commerce Act of 1926 § 3(f), 44 Stat. 568, 570; see also Brief for Respondent at 20-21, Wilson ("the safety regulatory provisions of the Civil Aeronautics Act were in substitution for, and largely an extension of, the provisions of the Air Commerce Act of 1926 . . . .").
92. See Reply Brief for Petitioner, Wilson.
[1938] legislative history."93 "In our view, the [1938] legislative history removes any possible doubts as to the Board’s power to suspend for violations."94 Yet they cited no language from any such history to support either of these assertions.

They argued that "suspensions and civil penalties were viewed and administered at least as alternate sanctions by the Secretary [of Commerce—after 1926], a fact duly reported to the Congress."95 This statement was true, but also cleverly misleading because it begged the question whether Congress in 1926 in fact authorized two forms of penalty, as well as two separate systems of justice? The CAB lawyers knew it had not.

To counter the basic argument that section 609 says nothing of violations, offenses, regulations or sanctions, the CAB attorneys bluffed their way through: "Petitioner’s contentions that Congress meant less than it said in section 609 are not persuasive."96 In another part of the brief they wrote: "The absence of any express provision that suspension might be imposed for violation was not to limit the Board’s powers, but to broaden them."97 This statement was nonsense. They were contending that because Congress had said nothing about violations in 609, that meant it had in fact authorized their punitive system. At the same moment that they were conceding that Congress had said nothing, they were criticizing Captain Wilson's arguments on grounds that Congress had said a lot.

Perhaps to make it seem as if they were being forthright, elsewhere they said: "The purpose of the Congress plainly was to continue the familiar pattern of safety regulation established by the Air Commerce Act . . . ."98 And "there appears to have been no direct reference to the suspensions provisions in the [1938] Congressional debates."99 It should by now be easy to understand why not.

While certainly some might see these arguments as coming within the bounds of legitimate advocacy, the CAB’s brief in Wilson (and Hard; and Pangburn, where FAA lawyers were on the brief) is a major facet of government aviation officials’ efforts to cover up their lack of authority for punitive suspensions.100 As the index to their brief reflects,101 in not a single instance did they cite any legislative history for the Air Commerce Act of 1926. Yet careful analysis reveals they were contending that sec-

94. Id. at 27.
95. Id. at 22.
96. Id. at 12.
97. Id. at 27.
98. Id.
99. Id. at 26.
100. See infra sec. VI for details and discussion of this coverup.
101. See Brief for Respondent at iii-ix, Wilson.
tion 3(f) of that Act was their authority for certificate penalties, not the 1938 Act. As stated in the government’s brief, section 3(f) was a bare statement that:

The Secretary of Commerce shall by regulation . . . [p]rovide for the issuance and expiration, and for the suspension and revocation, of registration, aircraft, and airman certificates, and such other certificates as the Secretary of Commerce deems necessary in administering the functions vested in him under this Act. 102

Nothing in this section (which links animate and inanimate objects with issuance and suspension in a single sentence) suggests authorization for a penalty system, only qualifications matters. A careful reading of the government’s brief reveals that the CAB lawyers asserted that they could institute a punitive certificate sanction system because Congress had not forbidden it in section 3(f). 103 Such legislative interpretation has no basis in logic, especially when Congress did speak directly to the subject of enforcement.

As can be seen by comparing the Acts of 1926 and 1938, section 3(f) was the precursor of sections 602 (issuance of certificates) and 609 (suspension and revocation of certificates). In order to clarify section 609’s application to qualifications matters, Congress added the terms “reinspection” (for aircraft, propellers, and appliances) and “reeexamination” (for airmen). Although the legislative history does not reveal who prompted such a change, it is reasonable to assume that government officials played a major role.

If section 3(f) was these officials’ original source of punitive suspension power, why did they not urge that section 609 also be constructed to plainly state that certificates could be suspended or revoked as punishment or sanction for the violation of a safety rule? Wilson and Hard were decided a full year before the Federal Aviation Agency was created. Section 609 in the Federal Aviation Act of 1958, while retaining the same basic structure as the 1938 Act, 104 was substantially revised to reflect the great shift of power from the CAB to the new agency. How, then, could CAB and CAA officials (the latter, soon to become FAA) fail to urge that section 609 be appropriately amended to clearly support the purported authority that they had claimed existed in Wilson? Why has there been no amendment to clarify this anomaly for the past quarter-century? (Nothing found in the public record reveals any such attempt.) The answer is obvi-

102. Air Commerce Act of 1926 § 3(f), 44 Stat. 568, 570.
103. See Brief for Respondent at 21, Wilson (referring to section 3(f) of the 1926 Act) (“There was no statutory specification of the grounds for suspension or revocation, this being a matter obviously left for the Secretary to establish.”). This statement indicates that the CAB lawyers were arrogating the power to determine when and if an airman could ever exercise his right to “demand” a jury trial in a section 901 civil penalty case.
104. See supra text accompanying notes 50 and 80.
ous—any public airing of the matter would risk raising tough questions, such as: When did any agency request this punitive certificate power? When did Congress hold hearings to provide for public input?

It did not happen in 1958. The late Senator Mike Monroney, father of the 1958 Act, clearly did not share the agency’s view of section 609 and was not aware that it was being used to justify punitive suspensions. In his report on the Act, he said:

The right of an airman to appeal to the Board the Administrator’s denial or nonrenewal of a certificate is retained and strengthened [under section 602], while a party whose right to his current certificate or rating is questioned [under section 609] as a result of the Administrator’s reinspection is entitled to a hearing and to an appeal to the courts.\(^{105}\)

Had Senator Monroney been aware that the CAA (to become FAA) was primarily using section 609 for violations, he would not have failed to include violations and sanctions along with reinspection.

Pangburn came down in 1962, when it was clear that Wilson and Hard were based on a gross misconstruction of the law. Did FAA lawyers seek to correct it? On the contrary, as that decision reflects, they cited Wilson for authority. In 1977, they did the same in McGee.\(^{106}\) Wilson, Hard and Pangburn must all fall because the Civil Aeronautics Act of 1938 is not determinative, and punitive certificate sanctions cannot under any circumstances be sustained under the legislation of 1926. The failure of government lawyers to inform these courts of the legislative history of 1926, which shows that Congress carefully chose civil money penalties and that system only, and emphasize that the certificate system started in that year, is inexcusable if not an outright fraud on the courts.

V. CERTIFICATE SANCTIONS

How did those early Commerce officials come to establish the punitive suspension system when its statutory basis was so dubious? Why have their successors maintained it in the face of its many obvious contradictions? Answering the first inquiry is not as speculative as might be expected at this juncture. Those officials violated their mandate from Congress, because they were skeptical about whether civil penalties

\(^{105}\) S. REP. NO. 1811, 85th Cong., 2d Sess. 3 (1958) (emphasis added); see also H.R. REP. No. 2360, 85th Cong., 2d Sess. reprinted in 1958 U.S. CODE CONG. & AD. NEWS 3741. There is not the slightest suggestion in the House report that its writers were aware of any connection between safety violations and suspension and revocation of licenses. Compare id. at 16 (comments on § 609) with id. at 17 (comments on title IX, Penalties) ("This title deals primarily with violations of provisions of the committee amendment which may be punished by the imposition of civil or criminal penalties, or both, and also contains provisions relating to venue and procedure in the case of any such violation. Except as noted below, this title is a reenactment of existing law without substantial change.").

\(^{106}\) No. 76-1092 (D.C. Cir. 1977).
would be an efficient enforcement tool\textsuperscript{107} and were unwilling to wait and go back to Congress to ask for change. Instead, they set up their own unauthorized system of summary justice, a system far more efficient than processing civil penalties through reluctant United States Attorneys with the formalities of federal district court, and the potential burden and expense of jury trial. They could see that civil penalties had severe limitations which Congress should have foreseen. Although over the years it is certain that some government lawyers have recognized that the certificate system has never had any basis in law, they have found it best to rationalize their acts and the program in the name of air safety.

The 1926 legislative history helps explain the genesis of the problem. One reason that civil rather than criminal penalties, which were proposed by the House,\textsuperscript{108} were authorized was that:

Under the present crowded condition of the Federal Courts criminal proceedings for the enforcement of minor infractions of the air commerce laws would be extremely expensive, add to the present congestion, and in most cases penalties would be long delayed in their collection. The civil administrative penalty is summary and proceedings are noteworthy for their absence of technical rules of evidence and pleading [in the compromise stage].\textsuperscript{109}

The House bill's criminal system did address two problems: 1) although it was unlikely that anyone would go to jail, that threat assured prompt payment of any fine; 2) by allowing prosecution in state courts as well as federal,\textsuperscript{110} the scheme increased the number of courts available for enforcement action. When the criminal system was not instituted, early aviation officials must have realized that civil penalties lacked sufficient coercive force to ensure payment. It stood to reason that if United States Attorneys were unwilling to prosecute minor criminal air-traffic infractions, they would be no more likely to take small civil penalty cases, or prosecute them vigorously. This would allow a significant number of violators to escape punishment. To address this problem, a \textit{modus vivendi} was worked out in the late 1970's with the Justice Department so that FAA lawyers could bypass the United States attorney "who indicates a general unwillingness to handle the case" and file the complaint directly in district courts themselves.\textsuperscript{111}

More importantly, some FAA officials have developed an effective method to assure payment of a civil penalty. Based upon interviews with FAA field inspectors,\textsuperscript{112} it is certain that at least one FAA regional headquarters sometimes changes violation cases against professional pilots

\textsuperscript{108} 1926 History, \textit{supra} note 54, at 45.
\textsuperscript{109} \textit{Id.} at 60.
\textsuperscript{110} See \textit{supra} note 55.
\textsuperscript{111} 1980 Handbook, \textit{supra} note 17, ¶ 1202.e(6), at 166-67.
\textsuperscript{112} These took place in May 1980, while working as a consultant to the General Accounting
from the civil penalty recommended by the investigating field inspector to a certificate sanction, out of fear that the airman might be knowledgeable about the weaknesses of the civil penalty system and sit tight, knowing that it is unlikely that the U.S. attorney will vigorously prosecute the case. The same officials assume that the airman, once a suspension is proposed, will ask if he can pay a civil penalty which will surely be paid to avoid the harsh consequences of forced unemployment.\textsuperscript{113} Decades ago, the General Counsel of the Civil Aeronautics Administration formally acknowledged that the public criticized this procedure as "blackjacking," and all but forbade it.\textsuperscript{114} Because so many shifts from certificate to civil penalty are reflected in the FAA's enforcement docket (shifts resulting in fines of $100-$300, rather than the much more costly suspension proposed), it is a reasonable inference that many, if not most, of these cases were so rearranged.\textsuperscript{115}

Office, during a second field trip to Los Angeles. I visited several General Aviation District Offices throughout the state, and interviewed more than a dozen FAA inspectors.

113. \textit{Id}. One inspector (who shall remain nameless) told me that this had occurred in at least five cases during the previous six months. He had recommended civil penalties because, among other reasons, he was aware of the substantial economic impact a suspension would have on these pilots by keeping them from performing their jobs. When regional headquarters in Los Angeles changed his recommendation to one that certificate action be used, he called to find out why. He was told that headquarters was afraid the airmen might know that United States Attorneys might not process the case; the office feared that the airmen might sit back, ignore the matter, and wait to see what happened, and perhaps escape any penalty whatsoever. In at least one case the inspector got the civil penalty restored. So instead of a 30-day suspension, which would have cost the accused around $4,000 during the height of cropdusting season, the pilot paid a $250 civil penalty. Interview of May 29, 1980.

114. CAA, Aviation Safety Manual of Procedure 103, at 65 (1954). In a memorandum to field lawyers appended to this manual, R.E. Elwell told them:

There has been unfavorable public reaction to the few instances in which the [CAA] has [shifted from certificate to civil penalty action]. . . . Concurrent imposition of sanctions is attacked as "double jeopardy": the withdrawal of one remedy to pursue another is criticized as "black jacking." The only way to assure the public of [our] good faith is to . . . consider the filing of a complaint for suspension or revocation as an election not to seek civil penalties for the same offense.

Only "under unusual circumstances," Elwell added, could the shift be made, and it would require "prior approval" from Washington.

115. Cases picked at random from FAA's enforcement docket show that in June 1980, of 71 civil penalty cases against individual certificate holders, 26, or 37\%, began as certificate actions and that 92\% of these airmen held professional licenses. The average suspension proposed (for all certificates) was 53 days, the average money penalty paid instead, $340. The November 1977 docket shows that 28 of 79 cases, or 35\%, originated as certificate actions; 82\% held professional licenses. Average suspension was 63 days; average penalty paid, $209.

Typically the closing letters in these cases read:

You are hereby advised that the Notice of Proposed Certificate Action [ATP, 15 days] dated March 5, 1980, is withdrawn in view of the fact that subsequent to its issuance in accordance with the offer of compromise suggested at your informal conference, you submitted a settlement offer of $300 in compromise of the civil penalties arising out of your alleged violation. . . . it has been concluded that the public interest requires no further action . . . .
Another glaring weakness of civil penalties is that they are as difficult to collect as any other civil judgment. How do you levy execution on a $1,000 penalty against some youngster with no assets who buzzed his high school stadium during a football game? Recognizing that the civil penalty system has its weaknesses, this hardly justifies executive branch officials in taking the law into their own hands. Why didn’t those early officials conscientiously work with the Justice Department, identify weaknesses, build data on civil penalty actions, then return to Congress and ask for something more effective? The answer lies partly in the nature of bureaucracy to never admit mistakes and the public pressures on aeronautics agencies to fulfill their mission of air safety. That pressure was exacerbated here by the sensationalism and emotionalism always attendant upon aircraft accidents.

Part of the problem was that in 1926, except in a few developed areas, the federal government was not a pervasive regulating force. Air traffic and maintenance rules were the sort of laws that states and cities routinely enforced. And significantly, they could do this in a well established infrastructure of petit courts where the threat of jail (‘ten dollars or ten days’) deterred non-payment of fines. To gain use of that infrastructure was no doubt a central reason why the House bill incorporated state courts into its criminal air-safety enforcement system.

FAA officials have attempted to justify their policy by invoking certificate actions in ‘operational’ cases, stating that ‘the withdrawal of the privileges of certificate is a natural, equitable, and just consequence of the abuse of such privileges.’ This is the same logic that cuts off the hands of thieves. Moreover, the agency’s sincerity in these statements is undercut by its own enforcement manuals, one of which notes that ‘most

Ulmer, CE-80-OG-28 (June 18, 1980). Note how with a few spoken words a section 609 action was instantaneously transformed into a section 901 action. Occasionally the file reflects why the shift was allowed: ‘WHEREAS, you . . . advised that a 60-day suspension of your Commercial Pilot Certificate would render an air-taxi business owned and operated by you insolvent . . . it would be in the public interest to accept the . . . compromise offer [of $1,000].’ Faulkner, AL-71-OG-36 (Feb. 25, 1972).

That ‘blackjacking’ is an effective collection tool was amply demonstrated when one airman, allowed to pay $150 in installments of $50 per month, was told: ‘Please understand that this compromise is for settlement purposes only. If you fail to comply with all the terms of our agreement, we shall then have to enter an Order of Suspension in accordance with our Notice of Proposed Certificate Action dated January 7, 1980.’ Bell, NW-79-OG-244, (Jan. 24, 1980). See also Smith, FAA Blackjack, PROFESSIONAL PILOT, Feb. 1981, at 91.

116. See 1968 Handbook, supra note 8, ¶ 9.c, at 9. (‘Certificate actions should generally be used in operational violation cases . . . .’) The new manual is less specific. See, e.g., 1980 Handbook, supra note 17, ¶ 205.e(1) (‘Civil penalties also may be initiated in any case where normally a suspension would be manifestly unfair or create an undue hardship and is not required for aviation safety’), 205.b(4) (‘Suspension may be used for punitive purposes where the nature of the violation warrants it . . . .’).

violations are inadvertent," while another urges that "suspension action should be considered in serious cases where a severe penalty is warranted." The real reasons FAA officials use certificate actions are: 1) fear that United States attorneys will turn down small civil penalty cases so that the airman goes unpunished; 2) it is an administrative burden to transfer the case or get permission to file directly in court where the FAA lawyer will be a mere technical advisor; 3) under the administrative license sanction procedure the FAA lawyer controls the action, the case moves predictably through the NTSB, and he enjoys the challenge of playing prosecutor and trying the case himself; 4) FAA's desire to put the violation on the certificate holder's record, so if he commits further offenses

120. Responding to a request from the FAA General Counsel Office (now Chief Counsel) for comments on proposed changes to the lawyers' 1968 Handbook, supra note 8, one official noted that:

We have found in the past that some U.S. Attorneys are reluctant to process violation actions when the civil penalty involved is relatively small. In states where criminal cases are frequent and the U.S. Attorney's workload is great, the relatively minor civil penalty cases are given priorities which preclude timely disposition.

Letter from Paul J. Baker, Chief, Flight Standards Division, ANE-200, to AGC-30, Office of General Counsel (Mar. 7, 1973). During a later attempt to revise the 1968 Handbook, another noted:

Many of the civil penalty actions which we are unable to settle are simply not of sufficient significance to warrant referral. The routine transmittal of such cases to the United States Attorney tends to take emphasis away from those cases which are genuinely significant to the agency.

Letter from Lawrence C. Sullivan, Regional Counsel, ANE-7, to AGC-20, Office of General Counsel (Oct. 6, 1977).
121. See 1980 Handbook, supra note 17, ¶ 1202.e(6), at 166.
122. In another comment on proposed changes to the 1968 Handbook, supra note 8, one FAA lawyer explained his frustration with civil penalties:

We recently had occasion to try a case involving [an airline pilot] before Judge Hill of the U.S. District Court for the Northern District of Texas, Fort Worth, Texas. The Judge dismissed our case. We charged [the captain] with operating an unairworthy aircraft from Tampa... to Orlando, Florida. While we do not believe the particular facts warrant discussion here, we do want to point out that during the trial the Judge (and the U.S. Attorney trying the case) became hopelessly confused with our technical phrases and terms. At times the trial was almost a comedy in that the witness, the Assistant U.S. Attorney and the Judge were virtually speaking three different languages. Unfortunately, the true merits of the case were not the basis for the decision. It is our view that in enforcement cases we should avoid, when possible, going into court because, in most cases, none of the participants will have the slightest idea what is going on. While the phrase "unairworthy" is a difficult one for even agency personnel to discuss, we would recommend that you consider substituting certificate actions in lieu of civil penalties in most instances, the obvious reason being, of course, that success in imposing a sanction will greatly depend upon the forum of the case. We definitely recommend that technical matters be kept out of court and be tried before the NTSB if at all possible.

Letter from J.N. Coker, Regional Counsel, SO-7, to GC-1, Office of General Counsel (May 25, 1971). Note the clear assumption here that FAA officials have the unfettered right to determine
the agency can justify more serious action;\(^{123}\) and 5) as one manual suggests, FAA officials will deliberately put a man out of his job when they think even a stiff money fine would not be sufficiently harsh for the alleged violation.\(^{124}\)

These reasons illustrate the pressure on FAA officials to unduly emphasize certificate actions, and indicate that the agency’s enforcement program has been shaped to suit its, not the public’s, convenience. In particular, they underscore the unfairness of a two-track, administrative-judicial enforcement program which allows the agency that initiates the prosecution to choose between the two tracks. That choice necessarily sets in concrete, right from the start, the method by which the accused is going to be punished and the kind of trial he will receive.

VI. THE COVERUP

It is reasonable to assume that a small core of government lawyers have always known of the certificate system’s illegal nature. The troubling question is why none of these public officials have ever blown the whistle. The evidence is abundant that a conscious effort has been made by some government officials over the years to hide the lack of legitimacy of punitive suspensions and revocations. This effort has had many facets. We have noted several already: the specious arguments government lawyers have used to defend challenges to section 609; their continued citation to cases they know to be based on fundamental error; their failure to cause, or even attempt to cause, section 609 to be amended to say in plain language what they claim it authorizes them to do. Additionally, two other facets of interest are worth describing: 1) a deliberate effort to avoid telling the public how the FAA enforcement program works, the central feature of which is these officials’ failure to promulgate rules that explain the two-track program; 2) the use of euphemisms, or word

\(^{123}\) See 1968 Handbook, supra note 8, § 12.a, at 12 ("Among questions to be considered in determining an appropriate sanction is whether the violator has a prior record. If so, its recency and nature should be considered. In an airman case, repetition of similar types of violations would normally require a greater sanction."). Although FAA counsel in my experience will consider a prior civil penalty in proposing the size of a certificate penalty, agency policy is that he cannot introduce that before the NTSB where the ALJ might use it. See 1980 Handbook, supra note 17, fig. 12-5, at 208 ("[A] settlement will not constitute an admission of violation.").

\(^{124}\) See 1968 Handbook, supra note 8, § 9.b, at 8. ("Civil penalties . . . should also be used as the normal sanction for less serious violations . . . ") Michael Pangia also relates: "By holding his client in check [at the informal conference] the attorney was able to obtain a reduction of the proposed six-month suspension to a civil penalty." Pangia, supra note 15, at 595.
games, to make it seem that certificate sanctions have nothing to do with "punishment."

A. FAILURE TO PROMULGATE RULES

The efforts of federal aviation officials to prevent the public from comprehending the enforcement program and to deflect attacks on it have involved acts of both omission and commission. For example, the FAA has never in its quarter-century of existence published a simple, comprehensible booklet that explains the program to pilots or mechanics. Although agency officials would argue that their enforcement handbook serves this purpose, the fact remains that this manual, a consolidation of materials intended to be internal documents, is lengthy and complicated. As a matter of agency policy, its enforcement manuals were kept from the public until 1970 when a Freedom of Information Act lawsuit125 forced their release. The present handbook can sometimes be helpful, but many airmen do not know it exists. It is not readily available at airports or FAA field offices and must be ordered from Washington.

Nor does the FAA mention the handbook in the Notice of Proposed Certificate Action126 or Civil Penalty Letter,127 which is when it would be of the most help to the accused. Moreover, this handbook, though the only information source, is as notable for what it does not explain as for what it does. It does not explain how easy it is to go to trial before the NTSB: that an ALJ will fly out from Washington to the airman’s hometown to preside over the case; that the trial is much like any traffic court; that many airmen defend themselves without counsel; and that there are no court costs. One regional counsel, when asked why FAA has never prepared a booklet that explains the system in layman’s terms, and especially one that explains the NTSB hearing process, underscored the reason for the omission. "If we told pilots how easy it was to go to trial at NTSB, we would be swamped with trials."128 My own experience confirms that many airmen, even lawyers, do not know about civil penalties and the possibility of switching to a money fine from a suspension. They

127. See id., figs. 12-1 to 12-5, at 201-09.
128. Statement by Dewitte T. Lawson, Jr., FAA Western Region Counsel at a Meeting on Jan. 24, 1980, at FAA Western Region Headquarters, Los Angeles. Among those present were Lawson, his assistant Fred Woodruff, U.S. General Accounting Office officials Ken Dobbs and Jeffrey McGowan and myself. The purpose of the meeting was to have Lawson explain to Dobbs and McGowan how FAA enforcement worked. Asked if from a philosophical standpoint (meaning due process) the airman ought to be told how enforcement worked, Lawson replied, "No." Neither did he think the pilot needed to know in advance whether the sanction for a violation was going to be a suspension or a civil penalty.
naturally focus on the certificate notice they have just received and are given no reason to assume there is any other alternative.

The centerpiece of this facet of the coverup is FAA's failure, in violation of the Administrative Procedure Act (APA),\textsuperscript{129} to adopt as formal rules a formidable array of enforcement policies. The APA mandates that federal agencies inform the public of their basic policies and procedures and allow public comment when they are formulated and promulgated.\textsuperscript{130} Interestingly, one rule FAA did promulgate underscores the basic reason for this failure—FAA officials' sensitivity to their lack of authority for the two-track enforcement program. This rule purports to restate section 901, which provides that "Any person who violates . . . any provision . . . [of this Act], or any rule, regulation or order issued thereunder . . . shall be subject to a civil penalty of not to exceed $1,000 for each such violation . . . ."\textsuperscript{131} FAA's version, contained in FAR section 13.15, states:

(a) Under sec. 901 of the Federal Aviation Act of 1958 . . . a person who violates any provision . . . of that Act, or any regulation or order issued thereunder . . . is subject to a civil penalty . . .

(b) The Administrator may compromise any civil penalty. If a civil penalty is contemplated and it is considered advisable to compromise it . . . the Regional Counsel concerned sends a letter . . . .\textsuperscript{132}

Regardless of how many courts of appeal uphold punitive suspensions, FAA officials realize that the plain command of section 901 ("shall be subject to a civil penalty") cannot be reconciled with their two-track enforcement program. They have subtly twisted the law to fit their rule, rather than fit their rule to the law.\textsuperscript{133}

The most striking aspect of the FAA's failure to promulgate rules explaining enforcement is the fact the agency has no rule that tells pilots and mechanics that licenses are at risk for a safety violation.\textsuperscript{134} FAA officials

\textsuperscript{130} Id. § 553.
\textsuperscript{133} Note that while the rule mentions further proceedings in federal court, it does not mention jury trial; were it to, it would raise the obvious questions. But see 14 C.F.R. §§ 94.31, 94.310 (1938) (which advised the public of the civil penalty right to jury).
\textsuperscript{134} The regulations that FAA has promulgated demonstrate that exceptions often prove the rule. See 14 C.F.R. §§ 61.15, 91.12, and 67.20 (1985). The first two, by a kind of incorporation by reference, combine to prohibit the operation of civil aircraft "with knowledge that narcotic drugs" are aboard; sec. 61.15(c) makes this action "grounds for suspending or revoking any certificate or rating issued under this part." Section 67.20 provides that "any fraudulent or intentionally false statement on any application for a medical certificate. . . . is a basis for suspending or revoking any . . . certificate . . . ." Although the word violation is never used in these, we see here that FAA lawyers can write a regulation that tells the public, "you break a rule, we'll take your license." If FAA claims authority to suspend or revoke for all violations, why single out just these two?
would claim that FAR section 13.19 serves this function. Yet this rule simply paraphrases section 609, which says nothing of violations, offenses or regulations; it speaks only of reinspections and reexaminations, matters unrelated to violations, and is for that reason misleading. Other FAA rules, such as FAR sections 13.11, 13.15 and 13.16, however, do use "violation" and similar terms freely. It is clear that use of the word "violation" was carefully avoided in section 13.19 in order not to draw attention to section 609's deficiencies.

As we have seen, at one time the federal government did have a concise rule that informed pilots and mechanics that their licenses could be suspended or revoked for safety violations. In 1938, this rule, along with an entire body of regulations promulgated under the 1926 Act, was recodified for publication in the seminal edition of the Code of Federal Regulations. Then inexplicably, in 1940, this rule, and several related ones, simply disappeared from that Code, never to resurface.

The new five-member Civil Aeronautics Authority, established under the 1938 Act, took office in August of that year. Except for technical changes to assure conformity with the new Act, its members adopted the existing regulations in the CFR in toto, which included the violation-suspension rule. A thorough search of original Civil Aeronautics Authority minutes at the Federal Records Center at Suitland, Maryland, unearthed no record of any subsequent action in connection with that rule. So how did it disappear? The only reasonable inference is that former Commerce Department aviation officials, now working for the new Authority, took it upon themselves, when supplying revisions for the 1940 CFR, to drop the suspension-revocation rule without Authority members' approval or knowledge.

Why would these men tamper with the regulations? They were faced with a problem, created by an obtuse clause in section 609 of the 1938 Act: "The Authority . . . may revoke, in whole or in part, any such certificate for any cause which, at the time of revocation, would justify the Authority in refusing to issue to the holder of such certificate a like certificate." The 1926 Act contained no such clause, and the 1938 legislative history gives no clue as to its purpose or roots. The clause was

136. Id. §§ 13.11, 13.15, 13.16.
137. When drafting Administrator Langhorne Bond's "get tough" enforcement policy, FAA lawyers used "violations" or similar terms 28 times. See FAA Order 1000.9C (Apr. 26, 1979).
138. 1926 Rule, supra note 12.
141. See 10 C.A.A. AIR COM. BULL. 84 (Sept. 15, 1938); see also id. at 184 (Jan. 15, 1939).
later deleted in the 1958 Act, also without explanation.  

This clause, in a roundabout fashion, made it plain that licenses were to be revoked only for lack of qualifications, not as a penalty for safety violations. It is fair to assume that these officials, who for the previous twelve years had been doing just that, realized that their rule was now directly contradicted by the new statute. They knew that in order to have the rule amended they would have to go through a hearing process before the Authority. They had to have been painfully aware that the emperor wore no clothes and that their lack of authority in the first instance would become evident, so they decided not to risk public involvement and the questions such a move would entail. At first opportunity, then, they let the suspension-revocation regulation slip through the cracks. Since their successors have also failed to promulgate a replacement, it is now clear why for forty-five years the federal government has had no rule that directly tells pilots and mechanics that their licenses are at risk for a rules violation.

In 1946, the Civil Aeronautics Administration (in 1940 the Authority was split into the CAB and CAA) gave the enforcement rules, which had been retained, a major overhaul. It promulgated a comprehensive rule on procedure that only indirectly referred to certificate sanctions, and which explained that violation cases would be handled by: (a) administrative letter of reprimand; (b) section 901 civil penalties; or (c) filing of a complaint before the CAB "with a view toward the suspension or revocation of a safety certificate issued . . . to the alleged violator." Note that the CAA here cited section 901 but not section 609.

In 1950 this rule underwent major change and each subparagraph was placed in a separate rule of its own. Subparagraph (c) read:

Complaints. Under section 1002 of the act, the Administration [CAA] may file with the Board a complaint in writing, with respect to anything done or omitted to be done by a person in contravention of any provision of the act or any requirement established pursuant to the act. Under section 609 of the act the Board may suspend, in whole or in part, any type certificate, production certificate . . . airman certificate . . . air agency certificate issued by the Administration, if the interest of the public so requires, or it may revoke, in whole or in part . . . . After such a complaint has been filed, the Board will determine administratively whether a certificate issued by the Administration to the alleged violator shall be suspended or revoked . . . .

This regulation was a calculated misrepresentation of section

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144. See Laster, 31 C.A.B. 1162 (1960) (indicating that even though the clause was dropped in 1958 the Board continued to act as if it were still there). See also infra note 178.
146. 14 C.F.R. § 408.22 (1951) (subpara. (a)); id. § 408.23 (subpara. (b)); id. § 408.26 (subpara. (c)).
147. 14 C.F.R. § 408.26 (1951) (emphasis added).
1002. That section allows "any person" to file a complaint with the Board; it says nothing of "Administration." That section's main thrust was not safety enforcement but rather, for instance, to allow residents of Cedar Rapids, Iowa, to complain to CAB if United Airlines failed to provide the service called for by its certificate of convenience and necessity. Section 609 says nothing of "complaints."

This was policy searching for a rationale. Coupling section 1002 to section 609 was an attempt to invest the latter with authority it plainly did not contain itself. This long forgotten CAA regulation is compelling evidence that government aviation officials have never acted in good faith when claiming that section 609 authorizes a punitive certificate sanction system of administrative justice.

No such claim about "complaints," invoking section 1002, has ever been made in any subsequent regulation. When, in 1958, many of these same officials, now part of the new Federal Aviation Agency, were required to promulgate new regulations in all areas of the Agency's activities, their solution to the lack of a legal rationale for certificate actions was to remain silent. They simply formulated their new certificate rule, FAR section 408.25 (the forerunner to today's section 13.19) to paraphrase section 609.

As mentioned above, public input has never been allowed in the making or shaping of punitive certificate sanction policy. Created in 1958 as a new and independent agency (and since 1966 an "administration"
within the Transportation Department), FAA was required to promulgate totally new rules. How, then, did agency officials avoid the APA mandate that "interested persons" be given "an opportunity to participate in the rule making," when it adopted its new enforcement procedure rules (including FAR section 408.25)? They simply ignored it. Making no mention of APA requirements for public participation, their Federal Register notice recited:

Effective December 31, 1958, Part 408 of the Regulations of the Administrator of Civil Aeronautics is hereby repealed, and a new Part 408 containing the enforcement procedures of the Federal Aviation Agency is hereby adopted to read as follows . . . .


149. See Nebraska Dep't of Aeronautics v. CAB, 298 F.2d 286 (8th Cir. 1962) (concerning adequacy of certain air service within the state of Nebraska); see also Flying Tiger Line v. CAB, 350 F.2d 462 (D.C. Cir. 1965), cert. denied, 385 U.S. 945 (1966); Foremost Int'l tours, Inc. v. Qantas Airways, Ltd., 525 F.2d 281 (1975), cert. denied, 429 U.S. 816 (1976).

150. See supra note 80 for the 1938 version and supra text accompanying note 50 for the 1958 version.


153. 24 Fed. Reg. 10 (1959). The FAA has also ignored the clear APA directive that a "sanc-
Earlier in this same Federal Register issue, in a notice about the new Part 405 on rulemaking procedures, the FAA explained their failure in that instance to allow public participation: "Since this amendment is not a substantive rule but one of Agency procedure, notice and public procedure hereon are unnecessary."\textsuperscript{154} Notably—and rather ironically—in their preamble to part 405, the FAA stated:

The Agency will follow the procedures required by the Administration Procedure Act for prescribing both substantive rules, on the one hand, and interpretive rules, general statements of policy, rules of Agency organization, procedure and practice, on the other hand.\textsuperscript{155}

Under the APA, FAA enforcement policies are subject to the following Congressional commands:

1. Each agency shall separately state and currently publish in the Federal Register for guidance of the public—(C) rules of procedure, descriptions of forms available or the places at which forms may be obtained . . . . (D) substantive rules of general applicability adopted as authorized by law, and statements of general policy or interpretations of general applicability formulated and adopted by the agency.\textsuperscript{156}

2. Except to the extent that a person has actual and timely notice of the terms thereof, a person may not in any manner be required to resort to, or be adversely affected by, a matter required to be published in the Federal Register and not so published.\textsuperscript{157}

The APA and court decisions leave little doubt of its application here, and that the government's failure to promulgate rules is an absolute defense to punitive certificate action.\textsuperscript{158} It is surprising that the vulnerability of FAA enforcement to the APA has escaped the attention of the aviation bar for so long. Perhaps this is because too many aviation bar members have never really understood the depth and importance of the APA. Senator Pat McCarran, its sponsor, called that Act: "a bill of rights for the
hundreds of thousands of Americans whose affairs are controlled or regulated in one way or another by agencies of the federal government. It is designed to provide guaranties of due process in administrative procedures.\textsuperscript{159}

In \textit{NLRB v. Wyman-Gordon Co.},\textsuperscript{160} the Court noted that:

the rule making provisions of [the APA] . . . were designed to assure fairness and mature consideration of rules of general application . . . . There is no warrant in law for the Board to replace the statutory scheme with a rule-making procedure [here by adjudication] of its own invention.\textsuperscript{161}

In the landmark case of \textit{Morton v. Ruiz},\textsuperscript{162} the Court declared agency action void for lack of formal promulgation and publication in the \textit{Federal Register}. Ruiz and his wife were Indians who lived off their reservation but nearby. They were denied special welfare benefits by the Bureau of Indian Affairs (BIA) because a rule in a BIA staff manual limited eligibility to those Indians who were living "on reservations." The Court held that the complainants' rights could not be extinguished since the rule in the manual had not been published. The Court made it plain that if and when BIA should adopt such a rule:

[It would be incumbent upon [the agency] to develop an eligibility standard . . . [and] must, at a minimum, let the standard be generally known so as to assure that it is being applied consistently and so as to avoid both the reality and the appearance of arbitrary denial of benefits to potential beneficiaries.

. . . . No matter how rational or consistent with congressional intent a particular decision might be, the determination of eligibility cannot be made on an \textit{ad hoc} basis . . . .

The Administrative Procedure Act was adopted to provide, \textit{inter alia}, that administrative policies affecting individual rights and obligations be promulgated pursuant to certain stated procedures so as to avoid the inherently arbitrary nature of unpublished \textit{ad hoc} determinations.\textsuperscript{163}

\textit{Morton v. Ruiz} is particularly applicable because FAA officials have no publicly known, sensible criteria or standards for making the choice between placing an accused on the certificate track or on the civil penalty track, nor any criteria for switching from one to the other. An airman is left to wonder why another airman was allowed to pay a money fine, and thus save his job, while he was not. Nor do airmen know that all such determinations are made on an \textit{ad hoc} basis, and are often based on personal whim or prejudice.

Just after its creation, then, in direct violation of the APA, the FAA failed to lawfully promulgate its entire set of enforcement procedures, in-

\begin{footnotes}
\footnotetext{159}{S. REP. NO. 248, 79th Cong., 2d Sess. 298 (1946).}
\footnotetext{160}{394 U.S. 759 (1969).}
\footnotetext{161}{\textit{id.} at 764.}
\footnotetext{162}{415 U.S. 199 (1974).}
\footnotetext{163}{\textit{id.} at 231-32.}
\end{footnotes}
cluding the rule they would claim spells out their punitive certificate sanction system. Although minor bits and pieces added later may have been properly adopted, that illegal action has never been rectified. Government aviation officials in 1958—and of course since—knew it was risky to open up the section 609 legal issues by placing on record a purported statement of their statutory authority, that it would likely unleash a hornet's nest of opposition from tens of thousands of pilots and mechanics who to this day do not comprehend the FAA's inordinate use of license suspensions and revocations.

This is also why the FAA has never adopted as formal rules many basic enforcement policies. Among these, critical to airmen's rights is agency policy about "blackjacking:"

*Shift in sanctions.* Ordinarily it will not be FAA policy to withdraw one remedy, after it has been commenced, to pursue another, although circumstances may arise in which such action is appropriate. An example where such action would be appropriate is when counsel has commenced certificate action against a pilot and thereafter learns that the pilot uses an aircraft in business or a profession and that the proposed suspension would constitute a sanction more severe than is warranted by the violation. Contrary situations will also occur.  

Although this power to shift a sanction can affect the livelihood of a pilot, mechanic or air-taxi operator, it is not contained in any formal FAA regulation. The CAA, however, did have a formal regulation that at least indirectly recognized the civil penalty as an alternative to certificate action. When it had its own hearing program, FAA promulgated a rule that authorized its hearing officer to settle any certificate case he was hearing with a civil penalty, but the agency has never had any rule that tells the airman he may ask for the shift, or the criteria for its use. The hearing officer rule is no longer on the books because the program was dropped long ago.

The suggestion in the 1980 handbook that shifts are seldom made, and then only when the pilot's need for his license comes as a surprise to FAA counsel, is a good example of the Agency's lack of candor about its two-track program. Field inspectors invariably find out what the pilot does with his license and note that in their report. It would be highly unusual if counsel was not keenly aware of it. As discussed earlier, the practice of making shifts in sanction has become routine.

The reason FAA officials have never promulgated this major policy as a rule is clear: There is nothing in the Federal Aviation Act of 1958 to

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165. See 14 C.F.R. § 651.21 (1947).
168. See *supra* note 115.
back it up. In 1951 the CAA General Counsel tacitly conceded that the procedure was a form of blackjacking; any Notice of Proposed Rulemaking (NPRM) would necessarily rekindle public sentiment, and the extensive use of blackjacking would become apparent. Public debate would then force FAA to address the unanswerable questions concerning the accused’s right to jury trial and criteria used to choose the certificate or civil penalty track in the first instance.

As late as 1980, these same officials, in their new handbook, repeated the timeworn claim that they may institute both civil penalty and certificate actions for the same offense. They claim that “as a matter of law” an election to impose one sanction is not a bar to a concurrent proceeding to impose another, although “such action has the appearance of ‘double jeopardy’ and, in the usual situation, it is not necessary . . . .” Were FAA to make a formal rule of this, these officials would have to explain on the record why Congress would authorize an enforcement program in which the FAA could prosecute an airman in federal court where a jury could find him not guilty—and in any event impose only a money fine—and at the same time pursue him before NTSB where an ALJ could find him guilty of the exact same violation and take away his license as punishment.

The CAB, until 1966, and then NTSB, which assumed CAB’s quasi-judicial authority in air-safety cases, as well as accident investigations, bear much of the responsibility for allowing this to go on. In Petition of Sichel, the CAB stated that the FAA could not deny an application for a student pilot certificate (by a formerly revoked private pilot) on grounds he lacked “the care, judgment, integrity and responsibility required of the holder of an airman certificate.” The Board indicated that it thought FAA had the authority to lay down such standards, but said:

[I]t does not follow that the administrator may apply such standards to applicants where he has not prescribed [them] . . . in the Regulations . . . .

[I]t is our view that applicants for certificates are entitled to have notice of the eligibility requirements which they must meet . . . .

This is precisely what the APA commands, and the Board cited that Act as authority for overturning the denial.

Sichel highlights a continuing conundrum, the existence of which re-

169. See supra note 114.
170. 1980 Handbook, supra note 17, ¶ 1202.a(3), at 163; see also id. ¶ 205.a(2), at 15.
171. “It is the present policy of the FAA not to bring both types of actions for the same violation so as to avoid any appearance of double jeopardy, although if the violations are serious enough there is nothing to prevent the FAA from doing so.” Pangia, supra note 15, at 593.
173. Id. at 976-77.
174. Id. at 976.
175. Id. at 977 n.10.
fects unfavorably on both NTSB and FAA. Although the Board recognized that the APA requires formal promulgation of rules which set forth the standards for a given certificate, it pointed out that it was also CAB policy to approve revocations ordered by the FAA under section 609 that were based on the same grounds that the Agency was using to deny Sichel his student license. 176 Yet the Board made no effort to reconcile the blatant inconsistency of this policy. If there must be rules on the books to deny a certificate, why would there not have to be similar rules and standards on the books in order to take it away?

The NTSB and FAA continue to ignore Sichel to this day. The Board, when it believes the airman's "repeated offenses" warrant it, continues to affirm FAA revocations on an ad hoc basis. 177 It does this by sleight of hand: the case often begins as a punitive action for the immediate violation that triggered the case, a violation that usually only deserves a suspension. But with any prior violations tacked on (for which the airman has already paid the penalty), the ALJ may determine that he lacks the "qualifications" to hold his license; 178 or he may determine, also ad hoc, that the infraction alone is serious enough to reflect a lack of qualifications. 179

One cannot deny there is some logic to linking qualifications and number of violations, but the problem is that there is no rule. 180 There is no specific cutoff period for considering past infractions. In one case, the

176. Id. at 976.
178. See Laster, 31 C.A.B. 1162, 1163 (1960) ("[W]e agree with the examiner's adherence to our traditional view that revocation, unlike suspension, is not warranted absent a showing that the holder is lacking in qualifications to hold the certificate. Although the 1958 Act no longer explicitly makes this distinction between the grounds for revocations and for suspensions, we do not view the amendment of section 609 to require abandonment of this appropriate differential standard adopted by the Board and approved by the courts . . . . Although wilful and deliberate disregard of the Civil Air Regulations is evidence of lack of qualifications, respondent's knowing violations, of which only the acrobatics caused a safety hazard, are isolated and not part of a pattern of continuing or defiant disrespect for the regulations."); Bittner, 39 C.A.B. 952 (1964).
179. See Otten & Gabrick, 1 N.T.S.B. 1002, 1007 (1970) ("We recognize that a finding of lack of qualifications in cases involving a single flight has traditionally been based on deliberate or reckless violations of the regulations. We also are of the view, however, that carelessness of an extreme nature, such as that involved herein, is grounds for such a finding [on an ad hoc basis]."); Hall, 1 N.T.S.B. 824 (1970).
180. But it cannot be disputed that FAA lawyers know there should be a rule. In a 1971 memorandum, then General Counsel (the title is now "Chief Counsel") George U. Carneal, Jr., told the FAA Deputy Administrator:

        [T]he regulatory proposals are progressing satisfactorily . . . . The project dealing with compliance disposition [a euphemism for "repeated offenses"] has been restructured and returned to Flight Standards for further work. We will by this project require willingness or "compliance disposition" as a prerequisite [for section 602 certificate applications] and continuing element of qualifications [under section 609] for all FAA certificate holders.

FAA Memorandum (Oct. 18, 1971). Never completed, it is my view this project was quietly buried by the bureaucracy after Carneal left. The project is an admission that the FAA has re-
ALJ talked about (but decided not to consider) a violation that was fifteen years old, committed when the pilot was a youngster, but who was now supporting a family as a flight instructor.\textsuperscript{181} A review of hundreds of FAA enforcement cases indicates that ALJs routinely look at violations that are five and ten years old. Often the airman is not told up front that any past violations will be used against him, and they are brought up at the last minute when he has no chance to prepare to explain them.\textsuperscript{182} Fair warning, standards for what type of past violation will be used, and a sensible cutoff date constitute due process and provide a method for public participation.\textsuperscript{183} The Court of Appeals for the Ninth Circuit touched upon the heart of the matter when it said in \textit{Jensen v. Administrator of Federal Aviation Administration}\textsuperscript{184} that ""public interest"" and ""safety"" as standards, and nothing more, "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)."

Why has this been allowed to go on? FAA lawyers are no strangers to the APA—they have drafted hundreds of regulations in accordance with its procedures. It is no burden on agencies to promulgate their policies as rules, especially when they have been in force for half a century. FAA failure to do so is not from oversight: ""The Office of Chief Counsel," an FAA Order commands, ""is responsible for . . . [r]eviving internal directives and advisory circulars to assure they are neither used for nor

\textsuperscript{181} Transcript at 453, 482-83, McGee, No. SE-5047 (N.T.S.B. Nov. 18, 1981).
\textsuperscript{182} There is no rule on the subject today, but see 14 C.F.R. § 301.5 (1956):
\textit{Record of previous violations}. Where a Respondent has had a certificate suspended or revoked or has had a civil penalty assessed against him for a violation . . . or has been subjected to any previous disciplinary action for violation of air safety standards, the [CAA] Administrator shall serve notice on the Respondent prior to hearing, or to submission of evidence where hearing has been waived, that he intends to call such matters to the attention of the examiner . . . . The Respondent may file with the Administrator such reply as he deems advisable.

\textit{See also id.} § 301.26.
\textsuperscript{183} \textit{See supra} notes 158-63 and accompanying text.
\textsuperscript{184} 641 F.2d 797 (9th Cir. 1981), vacated, 680 F.2d 593 (9th Cir. 1982).
\textsuperscript{185} \textit{id.} at 799.
have the effect of regulations and are consistent with the regulations." 186 FAA lawyers are keenly aware of their obligations to the public. In 1965, the FAA Associate General Counsel, Regulations and Codification Division, told the Associate General Counsel, Enforcement Division:

This paper discusses the investigation procedure in the memorandum on "Change No. 13 to Enforcement Handbook Formal Investigation . . . ." This division is concerned in the matter because it will have to write the rules to implement the proposed Handbook Change. The rules and the Handbook would of course have to be substantially identical. . . .

Under sec. 3(a) APA the internal rules cannot be effected via-a-vis the public until the procedural rules are published. 187

Each of the policies we have examined here is referred to, at least to some extent, in FAA's enforcement handbook. Although it is the Agency's official position that they need not be formally promulgated, how can it be argued that these policies are less deserving of promulgation as formal regulations than a policy about investigation procedure? The FAA memorandum underscores the logical inconsistencies that FAA officials must ignore in order to maintain their unauthorized punitive certificate sanction system. 188

FAA officials themselves have acknowledged the importance of their handbook. Administrator Langhorne Bond, who, along with his well-advertised "get tough" policy, instigated the new handbook, said of it: "This not only will help the FAA itself become more consistent, but will also let the public know what they can expect from us." 189 His Chief Counsel Clark Onstad stated: "[A] key advantage of the new 280-page handbook, which replaces four previous handbooks, is that it codifies enforcement procedures for handling proceedings and provides the public with a way to appeal FAA actions." 190 Testifying before a Congressional committee, Deputy Chief Counsel Jonathan Howe stated: "We think we are bound [in hazardous materials cases] just as strongly by the provisions in this handbook and we certainly have, in the past, administered our civil penalty statute [for air-safety cases] in exactly that manner . . . ." 191

188. See FAA Rulemaking Policies, FAA Order 2100.13, ¶ 22.a, at 8 (1976). This counsels FAA officials:

A primary Congressional consideration underlying the Administrative Procedure Act is that a regulatory agency afford the public an opportunity to participate in its rulemaking processes. Both the letter and the spirit of the rulemaking provisions of this act shall be observed. FAA follows the principle that the public interest is best served when regulatory affairs are open to the public to the fullest extent possible.

Despite these grandiose statements, FAA officials continue to operate as if they have never heard of the Administrative Procedure Act. It is clear that although the failure to promulgate rules, and lack of statutory authority for certificate sanctions, are legally distinct issues, on the practical level they are inextricably intertwined. It should be obvious by now that FAA officials do not do the former because they know they lack the latter.

B. The Word Game

A most interesting part of the coverup is the FAA’s use of euphemisms designed to make punitive suspensions and revocations seem as if they are something else besides penalties (though just what else is unclear). One FAA lawyer volunteered, during a meeting, that: “When we suspend a man’s license for a violation, that is not ‘punishment,’ that is a ‘remedial’ action.”\(^{192}\) He freely conceded, however, when asked, that he could have begun the same case as a civil penalty, and that of course would make it punishment; or that having started it off as a certificate action, he could shift it over to the money fine.\(^ {193}\) At the same time, during an informal conversation, an NTSB lawyer related that: “The Board never uses the word ‘punishment,’ all our actions are ‘remedial.’”\(^ {194}\) Throwing reality to the winds, both officials were following the company line.

Although most of the hundreds of section 609 punitive certificate cases appealed to the Board every year involve one or more “violations,” and the pleadings, parties, ALJ and Board freely use the term, nowhere in the Board’s rules of procedure for these situations does that term, or “punishment,” or “penalty” appear.\(^ {195}\) In one rule it does mention “offenses” and “proposed remedial sanction.”\(^ {196}\) It would strain credulity to assert this careful wording was accidental.

The “remedial” fiction is a legacy from the CAB. It may have gotten started in the mid-1950’s when sensitivity to the section 609 challenges of Captains Wilson and Hard became acute, or circa 1940 when the 1926 Rule was surreptitiously dropped because of that peculiar clause in section 609 of the 1938 Act which made it clear revocation could be used only for qualifications. In Wilson, CAB averred that “[t]he Board’s purpose is the remedial one of promoting safety, and not of punishing the offending pilot.”\(^ {197}\) This was pure sophistry. The purpose of any en-

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192. See supra note 128.
193. Id.
194. This meeting took place during February 1980 with NTSB staff lawyer Margaret Sweeney, in her office (emphasis added).
196. Id. § 821.33, 821.33(b)(2).
197. Brief for Respondent at 7, Wilson. Another splendid example of how this patent non-
forcement system is to punish offenders so they will not do it again, and to serve as a warning to others, in order to promote the goals of that particular system of laws or rules. Yet the "remedial" word game has persisted to this day. The effectiveness of this strategy is demonstrated by Wilson, where CAB succeeded in causing the Court of Appeals for the D.C. Circuit to become preoccupied with terms like "discipline" and "deterrence"; the same is true for Hard, its companion case before the Seventh Circuit. In an apparent putdown, the Hard court said: "'Penalty,' as a symbol repeatedly used by this petitioner is singularly ineffective for gauging the scope of power granted the Board by Congress.'"\footnote{198}

The hypocrisy of this softpeddling of certificate sanctions is no better exposed than by FAA's enforcement manuals: "Suspension may be used for punitive purposes where the nature of the violation warrants it . . . ."\footnote{199} "Revocation should also be used for punitive purposes where the nature of the violation warrants it."\footnote{200} The field inspectors' manual notes: "Although reexamination of . . . airmen and reinspection of . . . aircraft . . . do not involve enforcement in the strict sense of 'punishment of offenses,' they are considered in this handbook because the objective and the procedures are identical with those applicable to enforcement matters."\footnote{201} The Agency's very first enforcement handbook provided:

[.]It should be noted . . . that a violation of any rule, regulation or order issued by the Administrator is punishable either by certificate or civil penalty action. Furthermore, a certificate holder may perform some act which is neither a violation of the Federal Aviation Act nor any rule, regulation or order issued thereunder, which might be considered either as demonstrating a lack of qualification to continue to hold the certificate or as being an act for

\footnote{198}{248 F.2d at 761-62.}
\footnote{199}{1980 Handbook, supra note 17, ¶ 205.b(4), at 15.}
\footnote{200}{1968 Handbook, supra note 8, ¶ 9.d, at 10.}
\footnote{201}{1970 Handbook, supra note 119, ¶ 200, at 141. Two more examples come to mind. In their official publication, Commerce Department aviation officials, in recapping enforcement activity, noted that "[t]he penalties assessed for the 345 violations included 28 civil penalties, 48 reprimands, 75 suspensions, 15 revocations, 6 denials of license, and 62 dismissals of charges." 5 DEP'T COM. AIR COM. BULL. 108 (Aug. 15, 1933). Then again, discussing an aircraft accident, they noted: "The penalty exacted of this pilot by the Bureau of Air Commerce was a suspension of license." 7 id. at 185 (Feb. 15, 1936).}
which safety in air commerce and the public interest requires he should be punished by a suspension of his certificate.\(^{202}\)

In this explanation of its own powers, FAA was stating that despite the fact that the airman has not committed a violation, or is not technically unqualified to hold his certificate, if FAA does not approve of whatever he did, and FAA deems it to be in the interests of air safety and the public, FAA will punish him by suspension. This attitude towards enforcement and the public’s right to know is no better exemplified than by this accompanying directive:

Manual of Procedure 22 is an internal Agency issuance and is intended solely for the use and guidance of Agency personnel. The contents shall not be released to anyone outside of the Agency nor shall any reference to this manual be cited in oral or written communications to the public.\(^{203}\)

These formal statements are nowhere to be found today. Nevertheless, that these attitudes remain unchanged can be seen from the actions of FAA’s professional bureaucracy.

Underscoring the deceptive nature of the "remedial" word game is the fact that over two decades ago the FAA General Counsel himself undercut any pretension to legitimacy the term might have had. Concerned about problems he felt were created by CAB’s proposed new set of procedural regulations,\(^{204}\) rewritten because of the 1958 redistribution of enforcement power, Daggett H. Howard told FAA’s first administrator, Elwood “Pete” Quesada:

Throughout the rules the Board speaks in terms of "remedial" orders. This, too, is a discarded concept. There is no provision in the Act which would prohibit the Administrator from taking certificate action for disciplinary, as well as a remedial, reason, provided he makes the appropriate findings [in the public interest] as required by section 609. This emphasis by the Board on "remedial" orders has serious connotations. For example, it would be quite proper for the Administrator to suspend a pilot certificate simply as punishment as a deterrent to the pilot and others. The Board, under the rules, could reverse the Administrator’s order merely on the basis the action is not "remedial."\(^{205}\)

The likely source of Howard's determination that "remedial" was a "discarded concept" was the CAB's brief in Lee v. Civil Aeronautics Board.\(^{206}\) There, the CAA administrator asked the court to overturn a CAB order of dismissal so that the prosecution of two airline pilots for alleged safety violations could proceed. The pilots were involved in a near miss with another airliner for which there was some evidence they

\(^{202}\) FAA Manual of Procedure 22, ¶ 0 (1960).
\(^{203}\) Id. at foreword.
\(^{205}\) Memorandum dated Feb. 4, 1959 (emphasis added).
\(^{206}\) 225 F.2d 950 (D.C. Cir. 1955).
were responsible. The CAB, in a hearing conducted pursuant to its separate accident investigation powers, determined that they had to grant the pilots immunity from prosecution in order to acquire their testimony. CAA appealed and argued that the pilots were not entitled to immunity. The court dismissed the Administrator for lack of standing.

CAB strenuously argued during these proceedings that suspensions are a "penalty" which would require that immunity be granted:

>This purpose marks the suspensions as punitive in the legal sense, and as a penalty . . . . The Board did not exceed its authority in differentiating between punitive suspensions on the one hand and remedial suspensions and revocations on the other. [T]he fact that law enforcement is in the interest of the public cannot serve to convert punitive action to remedial action . . . . [A suspension] meets all of the tests of a penalty . . . . While it may be said to be remedial in the sense that it promotes safety by discouraging violations, the same can be said concerning the effect of any criminal prosecution.207

Yet the lawyers who wrote this brief, two years later in Wilson, told the same court that the Board was really only interested in the remedial purpose of promoting air safety, certainly not in punishing pilots.

The Board's desire to defend its immunity policies in Lee was understandable, given that the testimony of pilots was crucial to its investigations in those pre-cockpit recorder days. Yet by taking a contradictory position in Wilson, the CAB revealed that protection of the Agency's best interests, not the public's, was foremost in their minds.

VII. CONCLUSION

In 1980, in the face of a fifty-four year old law stating that any pilot or mechanic who violates any FAA regulation "shall be subject to" a civil money fine with right to jury trial, the Agency's Office of Chief Counsel prepared Congressional testimony for Administrator Langhorne Bond that said:

>W]e as a rule take certificate action in the form of a suspension for violation of operational rules. However, we do give consideration to a person's livelihood and the need for his services as for example use of an aircraft in a person's business or farm operation, company pilots, air taxi pilots and so forth. These people are often given civil penalties so that there is no undue financial burden by taking their certificates away from them.208

Like so much that FAA officials say about enforcement, this is grossly misleading, and it exposes the insurmountable contradictions of the two-track program. Except for airline pilot cases, FAA's own statistics show that the majority of professionals—commuter, air-taxi, corporate pilots

207. Brief for Respondent at 7, 24, 28, Lee. Briefs may be found at Vol. 1041, Records and Briefs, United States Court of Appeals, D.C., of the D.C. Bar Association.

208. BRIEFING BOOK, supra note 25, at 1 (emphasis added).
and the like—are penalized by suspension, not civil penalties.\textsuperscript{209}

The institution of punitive suspensions and revocations by government aviation officials in 1926, and their continued use and coverup, constitutes one of the great abuses of power in the history of the federal bureaucracy. One recent case can serve as a vivid example of the human impact of this abuse.\textsuperscript{210} A helicopter pilot, instructed by the station’s news director to get pre-game shots of the crowd filling the Denver football stadium, took the TV cameraman in closer, lower and slower than FAA officials thought was proper in the event of engine failure. In what was clearly a response to the notoriety of the incident (several in the crowd felt threatened and complained), rather than a justifiable belief that the pilot would do this again, FAA officials issued an emergency order suspending the pilot for six months. Although there was no accident or any harm done, the ALJ routinely upheld the FAA.\textsuperscript{211}

Caught short by the emergency order, without a job and unable to afford counsel, the airman did not perfect his appeal properly. With this, his first violation in 2,000 hours of combat and civilian flying, this young family man lost his job because his sympathetic employer could not keep it open that long and lost half his modest annual salary. Afterwards, in order to take the only job he could find, he had to uproot his family from the city where he and his wife had settled and move to another state. Ironically, the regulation he allegedly violated leaves much to the judgment of the pilot.\textsuperscript{212} The FAA lawyer who prosecuted the case, when interviewed later, agreed that had the man been just 100 feet further from the side of the stadium, and been flying ten miles an hour faster, the case would have been far more difficult to prove.\textsuperscript{213} A reasonable person, had he learned that this young man paid a civil penalty of $500, even $250, would have thought that sufficient and justice well served.

Congress as well bears responsibility for these injustices. Never has there been any planned, regular Congressional oversight of federal aviation enforcement. Congress should set up and fund a commission of prominent citizens, including constitutional and administrative law experts, with its own staff, to completely overhaul the FAA enforcement program. This body must hold nationwide hearings so that it will understand the depth and breadth of the problems that need rectifying, and to maxi-

\textsuperscript{209} Enforcement Report, supra note 1, at 1, 6.
\textsuperscript{210} Jones, No. SE-4889 (N.T.S.B. Dec. 8, 1980).
\textsuperscript{211} Id.
\textsuperscript{212} 14 C.F.R. § 91.79(a), (d) (1983) (basically that he was operating at an altitude and at less than the minimum airspeed in which an autorotative landing could be safely executed in the event of engine failure).
\textsuperscript{213} Telephone interview with Allan Horowitz, FAA lawyer—Rocky Mountain Region (Dec. 17, 1980). Horowitz also commented: "If we had only civil penalties, we wouldn’t have an enforcement system."
mize public participation. Any revised program should be patterned after auto traffic systems of justice, providing in most cases for fixed penalties and for forfeiture of collateral. Then it can concentrate on repeat offenders and serious offenses. Safety violation cases, when contested, should be heard by federal magistrates. Congress never intended that questions of “guilt or innocence” be heard by a panel, like NTSB, which has direct responsibilities for air-safety. That’s like having the policeman serve as traffic judge.

Certainly, there is nothing unfair about making air-safety violations minor misdemeanors (and in some cases more serious crimes), so long as FAA’s enforcement program is completely overhauled and Congress makes it clear that most violations are no different than speeding in a national park. It will not be an easy or inexpensive task to revamp the enforcement system so that violations are fairly and equitably handled, but it is one that justice demands.
FACULTY COMMENT

Transportation Deregulation (1976-1984): Turning the Tide

ROBERT M. HARDAWAY*

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I. INTRODUCTION

President John F. Kennedy, in his Transportation Message of 1962, called for "greater reliance on the forces of competition and less reliance on the restraints of regulation."1 The "Great Deregulation Debate"2 has


Arguably, the seeds for the "deregulation movement" were first planted in the Transportation Act of 1958, Pub. L. No. 85-625, 72 Stat. 568, implementing several recommendations of the Presidential Advisory Committee, the chief objective of which was to "increase reliance on competitive forces of transportation in rate making."3 Harris, Introduction, 31 GEO. WASH. L. REV. 1, 20 (1962) (prepared prior to President's Message to Congress Discussing an Efficient Transportation System, U.S. CODE CONG. & AD. NEWS 4148 (Apr. 5, 1962), which made substantive recommendations for amending the Interstate Commerce Act.) However, what little deregulation philosophy was expressed in that Act was not translated into substantial air fare carrier relief. The year 1976 is perhaps a more appropriate year to begin the "age of deregulation," as this year marked only the beginning of a reversal of Civil Aeronautics Board (CAB) policy in initiating administrative de facto deregulation, but it was also the year of passage of the Railroad Revitalization and Regulatory Reform Act of 1976, Pub. L. No. 94-210, 90 Stat. 31 (codified as amended in scattered sections of 45, 49 U.S.C.) (4R Act), which with the later Staggers Rail Act of 1980, Pub. L. No. 96-448, 94 Stat. 1895 (codified as amended in scattered sections of 45, 49 U.S.C.), began the legislative process of deregulation in the railroad industry. The passage of these acts, along with the airline Deregulation Act of 1978, Pub. L. No. 95-504, 92 Stat. 1705 (codified as amended in scattered sections of 45, 49 U.S.C.), led Professor P.S. Dempsey to observe that "the five year period from 1976 to 1981 will be remembered as perhaps the most active in the almost one hundred year history of governmental regulation of transportation."4 Dempsey, Congressional Interest and Agency Discretion—Never the Twain Shall Meet: The Motor Carrier Act of 1980, 58 CHI.-KENT L. REV. 1, 11 (1981).

The de facto administrative deregulation of the ICC/CAB effectively extends the deregulation period up to the present. See, e.g., Lawfulness of Volume Discount Rates by Motor Common Carrier of Property, 365 I.C.C. 711 (1982); Conrail Abandonment in Jeannette, Pa, 366 I.C.C. 384 (1982); Chicago & N.W. Transp. Co.—Abandonment—Between Marion City and Kesley IA, 366 I.C.C. 373 (1982). Staff standards of administrative review, if not a rederegulatory philosophy, have resulted in a large number of judicial opinions upholding the deregulatory decisions of the ICC and CAB. See, e.g., National Small Shipments Traffic Conference, Inc. v. CAB, 618 F.2d 819 (D.C. Cir. 1980) (CAB within its authority in exempting domestic air cargo carriers from duty to file tariffs); Central Vermont Ry. v. ICC, 711 F.2d 331 (D.C. Cir. 1983) (competitor of merging railroad not entitled to protection); Brotherhood of Maintenance of Way Employees v. ICC, 711 F.2d 331 (7th Cir. 1983) (ICC has authority to reject conditions for protection of tariff routing for benefit of competing carriers). But see American Trucking Ass'n v. ICC, 659 F.2d 452 (5th Cir.
been raging ever since. The battle lines have now been drawn, while each side waits for the latest data that might confirm its position or discredit the opposition. In the long run, only the final results will count. During the present transitional phase, the returns have often been conflicting and confusing.\(^3\) and it has been difficult to distinguish the effects of dereg-

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1981); C&H Transp. Co. v. ICC, 704 F.2d 850 (5th Cir. 1983); Steere Tank Lines, Inc. v. ICC, 687 F.2d 104 (5th Cir. 1982) (ICC exceeded its authority); Ritter Transp., Inc. v. ICC, 684 F.2d 86 (D.C. Cir. 1982); Aero Mayflower Transit Co. v. ICC, 535 F.2d 938 (7th Cir. 1976); Modification of the Motor Carrier Fuel Surcharge Program, 365 I.C.C. 311 (1981); Central Forwarding, Inc. v. ICC, 698 F.2d 1266 (5th Cir. 1983); American Trucking Ass'n v. ICC, 672 F.2d 850 (11th Cir. 1982) (ICC extension of intercorporate handling exemption to nonincorporated entities deemed ultra vires); Wheaton Van Lines, Inc. v. ICC, 671 F.2d 520 (D.C. Cir. 1982) (ICC authorization of sale of dormant authority and gateway elimination not supported by the evidence).

2. In the broader historical context, the debate has been going on for a much longer period. For a description of the debate over railroad regulation from 1877-1976, see infra text accompanying notes 42-78. There was a flurry of debate over the philosophy of regulation just prior to the passage of the Motor Carrier Act, ch. 498, 49 Stat. 543 (1935) (codified as amended in scattered sections of 49 U.S.C.). Congressman George Huddleston probably spoke for the majority of those who opposed the Act when he observed that “the proponents of the bill admitted candidly that its main purpose was to give a monopoly to eliminate competition.” H.R. REP. No. 783, 71st Cong., 2d Sess. 16-17 (1930), cited in Webb, Legislative and Regulatory History of Entry Controls on Motor Carriers of Passengers, 8 TRANSP. L.J. 91, 96 (1976). Senator Wheeler, at the time, also argued in a minority report that “[t]his . . . bill will establish one more bureaucratic department of the government to interfere with the natural development of the people's business. It will mean more red tape on the part of both operators and government officials. Worst of all, it will prevent that competition that brings lower rates and better service to the people.” S. REP. No. 396, pt. 2, 71st Cong., 2d Sess. 3 (1930). Webb, however, points out that most of the congressional debates about federal regulation prior to passage of the Motor Carrier Act of 1935 gave little consideration to economic regulation which did not include control of entry, and that in fact the greatest concerns were with safety, and the unfairness of a system which regulated the railroads but not many of the motor carriers. Webb, supra, at 97-98. It was presumably the view at the time that the best way to help the railroads was to burden the motor carriers with the same type of regulations as the railroads. Now, after several years experience with deregulation, lively debates still spark interest at conventions. See, e.g., Barry, Speakers in 'Great Debate' in Detroit Differ in Appraisals of Deregulation, 30 TRAFFIC WORLD 188 (1981).

3. Air fare data, for example, has been interpreted in a variety of ways. Senator Andrews, in a recent televised appearance on Face the Nation announced that his data revealed that air fares had increased 110% since deregulation while the general inflation rate was 48%. See Dempsey, Deregulation: The Great American Aviation Catastrophe, AIR CARGO WORLD, Mar. 1984, at 44, 46. While his source was unclear, this figure was apparently based on a comparison of regular coach fares. Thus, the figure does not take into consideration the increase in discount fares from approximately 40% to 80%. Deregulation Oversight: Hearings Before the Subcomm. on Aviation of the House Comm. on Public Works and Transportation, 98th Cong., 1st Sess. 10 (1983) (statement of Paul R. Ignatious, President of the Air Transport Association); see also AIR TRANSPORTATION ANNUAL REPORT OF THE U.S. AIRLINE INDUSTRY (1983). According to the Air Transportation Annual Report, airfares in the first year of deregulation decreased from 8.4c per passenger mile to 8.3c per passenger mile, rising slightly to 8.7¢ in 1979, and then rising with fuel prices in 1980 to 11.0¢, and to 12.3¢ in 1982 and staying the same through 1982. The Harvard Faculty Project on Regulation reported in 1981 that real average fares decreased by seventeen percent during the first few years of deregulation. J. MEYER, C. OSTER, I. MORGAN, B. BERMAN & D. STRASSMANN, AIRLINE DEREGULATION: THE EARLY EXPERIENCE 71 (1981) [hereinafter Harvard Faculty Project Report].
ulation from the effects of such independent economic forces as recession, fuel prices[^4] and inflation. Nevertheless, it is argued here that the transition phase of deregulation, led by the airline industry, is drawing to a close and that the tide has now turned in favor of deregulation. Airline industry losses[^5] were sustained during the worst recession since the Great Depression, which coincided with pioneering deregulation. These losses are now yielding to record industry traffic, revenues and profits.[^6] Concerns about service to rural communities[^7] are proving unfounded[^8]


[^5]: During the first four months of 1979, fuel prices increased 86%. Between March 1979 and March 1980, prices increased by 105%. *Harvard Project*, *supra* note 3, at 163. It is interesting to note that during deregulation these staggering fuel price increases resulted in only very modest fare increases. *See supra note 3.* It is understandable then, that critics of deregulation often choose the 1979-80 time period to compare fares. Charles Murphy notes with concern that average fares from 1979 to 1980 increased by 26%. Murphy, *Airline Deregulation and Antitrust*, 50 *Antitrust L.J.* 381, 383 (1981). The 105% increase in fuel prices during that period is not noted, of course, nor is there any opinion expressed as to how such fuel price increases might have affected fares had there been regulation during that period. Professor Dempsey also chooses the year 1979 to note a "26 percent increase in passenger fares." *Dempsey, Rise and Fall of the Civil Aeronautics Board—Opening Wide the Floodgates of Entry*, 11 *Transp. L.J.* 91, 182 (1979).


[^7]: American Airline's profits alone exceeded $15.6 million in the fourth quarter of 1983. *Wall St. J.*, Jan. 19, 1984, at 62, col. 4. Air traffic increased in 1983, with only Continental among all major carriers showing a decrease. US Air showed a 19% increase in traffic, followed by United with 11.8%, Delta 9.6%, Eastern 8.4%, TWA 6.8%, Pan American 6.2% and Western 6.0%. *Hamel, Airline Traffic Up as We Go to the Sky*, USA Today, Jan. 9, 1984, at B-1, col. 3.


[^4]: Even in the early years of deregulation, the effects of deregulation on small community service were often exaggerated. The Harvard Foundation Report, for example, investigated a Kysor Industrial Corp. advertisement in the March 7, 1980 issue of the *Wall Street Journal* which screeched: "Deregulation has shot down more planes than the Red Baron," and asserting that 25 small communities had lost their service due to deregulation. The report's investigation of the ad revealed that 7 of the 25 communities listed had lost their service *before* deregulation, and that the remaining communities were receiving replacement service, some at a higher level than before deregulation. *Harvard Project*, *supra* note 3, at 120. Recent CAB statistics reveal an overall increase in service to small communities, especially to small community or sequitur hubs. *See generally Civil Aeronautics Board, CAB DRAFT REPORT* (1984); *Richard Ferris reports that, '"In the ten years prior to the Deregulation Act, 173 communities lost air service. In the four and a half years since deregulation, no community has lost air service.'" *Deregulation Oversight: Hearings Before the Subcomm. on Aviation of the House Comm. on Public Works and Transportation*, 98th Cong., 1st Sess. 420 (1983) (statement of Richard Ferris, Chairman and Chief Executive Officer, United Airlines, Inc.). Partly because the Airline Deregulation Act made smaller
and misdirected. Safety records have actually improved considerably since deregulation; airfares are continuing a downward trend; the necessity for subsidies has been reduced; and, contrary to many predictions, the number of carriers has increased rather than decreased. In light of all these benefits wrought by deregulation, it is no wonder that at least twenty-nine of the thirty air carriers represented by the Air Transport Association would not oppose any attempt to re-regulate their industry.

Professor Paul Stephen Dempsey in his recent article, *Transportation Deregulation—On a Collision Course?*, argues that deregulation of transportation has been a failure and there should be a return to "responsible" regulation. Looking at the history of railroad, motor carrier and airline de-

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9. It is interesting to note that it was during the regulatory climate created by the CAB between 1960 and 1977 that service to over 179 communities was terminated. Havens & Heymsfield, supra note 7, at 643. Indeed, it was not until deregulation in 1978 that replacement service was being provided at about sixty of those communities. H.R. REP. No. 1211, 95th Cong., 2d Sess. 11 (1978). Those expressing concern about loss of service to small communities might do well to look at the economic disincentives created by regulation which resulted in the devastating loss of service prior to deregulation. See generally HARVARD PROJECT, supra note 3, at 156.

10. National Transportation Safety Board statistics reveal a decrease in fatal crashes per 100,000 take-offs from .10 in 1978 to .08 in 1982. The FAA reports that safety "performance indicators"—accidents, FAA violations, etc.—have improved by 30% in the last few years. Wall St. J., Oct. 18, 1983, at 35, col. 4. Even the most vigorous opponents of economic deregulation concede that safety has improved under deregulation. Murphy, supra note 4, at 383. Professor Dempsey concludes that “[s]erious questions arise as to whether an unhealthy industry can be a safe industry.” He cites several commentators who opine that deregulation ought to result in decreased safety, but cites no studies or statistics to support this view, other than to recite several highly publicized crashes that have occurred since deregulation. Dempsey, supra note 5, at 352.

11. See supra note 3.

12. The Airline Deregulation Act “encouraged the use of appropriate size aircraft and made commuter carriers eligible for subsidy. The net impact of deregulation on small community subsidy levels in the first year of deregulation has been to substantially reduce the subsidies paid.” HARVARD PROJECT, supra note 3, at 156-57. Indeed, in the first few years alone of deregulation, there was a "net reduction in annual subsidy payments of $5,297,326" under Section 419. Id. at 146.

13. Dempsey, supra note 4, at 183; see also Dempsey, supra note 5, at 344 (Professor Dempsey cites commentators who have expressed the opinion that deregulation would result in greater concentration in the airline industry).

14. Dempsey notes that Braniff and 17 smaller carriers have gone bankrupt, but did not mention 30 new entrants which have taken their place; and even Braniff has come back. Dempsey, supra note 5, at 343. In fact, it seems that for every inefficient or lumbering carrier that goes under, several lean and efficient carriers rise to take its place.

15. Telephone Interview with William E. Jackson, Vice-President for Public Information of the Air Transport Association, in Denver (Jan. 20, 1984). Only Republic would favor re-regulation. Notably, however, even Republic did not express this view at the ATA Directors meeting.
regulation, Professor Dempsey has compiled an impressive array of opinions hostile to deregulation and argues that deregulation has led to: 1) economic decline in the industry, 2) diminution of safety, 3) discrimination in pricing, 4) deterioration of service, and 5) erosion of carrier liability for loss and damage. 16 This article will critically examine these arguments through application of economic and legal principles, and reference to empirical data compiled from industry, labor and government sources.

Discussion and application of economic principles is often lacking in legal analyses of deregulation. This lack of cross-fertilization of ideas between the economic and legal spheres is illustrated by the observation that articles in the economic journals tend to favor deregulation, 17 while those in the legal journals tend to favor regulation. 18 One suggested reason for this difference in opinion is that lawyers themselves have an interest in regulation 19 because they play a significant role in its administration. 20 As a former associate general counsel of the CAB has observed, "it is understandably painful for one involved in economic regulation over a professional lifetime to consider his life's work outdated, or

16. Dempsey, supra note 5.
17. See, e.g., Trapani & Olson, An Analysis of the Impact of Open Entry on Price and the Quality of Service in the Airline Industry, 64 Rev. Econ. & Statistics 67 (1982); Cartlon & Lanches, Benefits and Costs of Airline Mergers: A Case Study, 11 Bell J. Econ. & Mgmt. Sci. 65 (1980); Schmatanese, Comparative Static Properties of Regulated Airline Oligopolitics, 2 Bell J. Econ. & Mgmt. Sci. 3 (1971); Stigler, The Theory of Economic Regulation, 2 Bell J. Econ. & Mgmt. Sci. 565 (1971); Levin, Railroad Rates, Profitability and Welfare Under Deregulation, 12 Bell J. Econ. & Mgmt. Sci. 1 (1981); Anderson & Kraus, Quality of Service and the Demand for Air Travel, 63 Rev. Econ. & Statistics 533 (1981); Spann & Erickson, The Economics of Railroading: the Beginning of Cartelization and Regulation, 1 Bell J. Econ. & Mgmt. Sci. 227 (1970). Articles in the Journal of Law and Economics have a decidedly economic bias, with very few cross-references to the legal periodicals. See, e.g., Stigler & Friedland, What Can Regulators Regulate? The Case of Electricity, 5 J.L. & Econ. 1 (1962); Jordan, Producer Protection, Prior Market Structure and the Effects of Government Regulation, 15 J.L. & Econ. 151 (1972); Peltzman, Toward a More General Theory of Regulation, 19 J.L. & Econ. 211 (1976). It is interesting to note that the articles on regulation in the legal periodicals place greater reliance on secondary sources for data, while the economic articles are generally more empirical, and less reliant on the opinions of others.


even worse, misdirected.”

It is the purpose of this article to explore the social, economic and legal consequences of deregulation during its phase of transition, with emphasis on the application of economic principles to hard data obtained from industry, labor and government sources.

II. THEORIES OF REGULATION

The history of economic regulation reveals a now familiar pattern: a failure to learn from previous mistakes and a constant hope that basic economic laws can be made to disappear if they are only ordered to do so. It has been thousands of years since the first attempts by a civilized society to regulate economic activity by fiat. Still, there are those who believe that wealth can be increased by simply printing more money, that real prices can be lowered (or raised) by the waving of a regulatory wand, and that an efficient industry can be mandated. The result of these failures to learn from previous mistakes has caused human tragedies of unparalleled proportions. For example, stringent rent controls in France from 1914 to 1948 resulted in an almost complete cessation of residential building during that period. (It was only after the lifting of rent control after World War II that there was a vigorous boom in French residential building.) New York City, which failed to learn from that experience, later instituted rent controls which resulted in the tragic abandonment of thousands of apartments at a time when shelter was desperately needed. Federal ceilings on natural gas have caused severe gas shortages and curtailment of vitally needed operations and explorations.

22. It is important not to confuse economic with social regulation. For example, child labor laws, food and drug laws, and FAA safety regulations are remedial and social in purpose, and have only an indirect effect on resource allocations.
23. By 301 A.D., economic regulation was well established as an instrument of state power. In that year the Emperor Diocletian issued his famous edict threatening death for violations of laws setting a “just price.” H. SPIEGEL, THE GROWTH OF ECONOMIC THOUGHT 63 (1983). By 1359, private companies had obtained monopoly powers by charter from their respective governments. In that year, the society of Merchant Adventurers obtained a charter, and benefits of regulation; in 1600, the East India Company received its charter. Both attempted to suppress the competition, whom they called “free-traders” and “interlopers.” Id. at 99.
24. Id. at 27. The simplistic notion that printing more money increases wealth should be distinguished from the more complicated, but now generally accepted liquidity preference theories of John Maynard Keynes. See generally J. KEYNES, THE GENERAL THEORY OF EMPLOYMENT, INTEREST AND MONEY (1936). For a discussion of the “acceleration” and “multiplier” effects of money and investment, see P. SAMUELSON, Economics 51-52 (6th ed. 1972).
25. P. SAMUELSON, supra note 24, at 51-52.
26. See generally Jones, supra note 18, at 315-16; Jordan, supra note 17; A. FRIEDLAENDER, supra note 1, at 99.
27. P. SAMUELSON, supra note 24, at 372.
28. Id. at 372-73.
tions.29 So called wage-price controls still result in black markets, and renewed inflation.30 The list goes on and on. These controls are always justified on grounds of "public interest." Yet, the government often has a difficult time in deciding whether to order prices down to "protect the consumer" or order them up to "protect an industry."31 This ambivalence has often led to conflicting, inconsistent and ultimately counter-productive regulatory practices. It is not surprising to learn that regulation, while often eliminating one short-run consequence of market failure, more often that not results in more resource misallocation than it cures.32

This does not mean that economic regulation should not play an important role in a mixed economy. The laws of supply and demand result in equilibrium and maximum efficiency only in an idealized, perfectly competitive market.33 Since such markets rarely occur,34 it follows that equi-


The natural gas story also is well known. Federal ceilings on natural gas producer prices resulted in an imbalance between supply and demand. For years, natural gas was consumed more rapidly than new supplies could be obtained. The result was a reduction of supply to the point where neither peak nor annual demands for gas could be met. Industries dependent on gas supplies were curtailed in their operations and were shut down completely for limited periods. Residential consumers of gas were not far removed from interruptions in supply that could work major hardships. Natural gas users, deprived of supplies, imposed additional demands on their energy sources, aggravating energy problems elsewhere. Again public and industry dissatisfaction led to a legislative program of deregulation.

id. at 318 (footnotes omitted).


32. Peitzman, supra note 17; Stigler, supra note 31. See also Spann & Erickson, supra note 17.

Regulation with effects which cut across boundaries between competitive and non-competitive sectors, even if it is successful in achieving its objective in the non-competitive sector, can impose costs in the competitive sector which far outweigh the benefits in the non-competitive sector.

id. at 243.

33. See J. HIRSCHLEIFER, PRICE THEORY AND APPLICATION (1976). Hirshleifer defines a competitive trader as a "price taker. The terms of control facing him in the market are, in his view, outside his sphere of control; he regards himself as able to buy or sell price." id. at 198. There are three additional characteristics of a perfect market: 1) Perfect communication, 2) instantaneous equilibrium, and 3) costless transactions. id. at 200-01. Obviously such characteristics occur in theory only. Another important characteristic of perfect competition is that entry into the market be "absolutely free in the long run." P. SAMUELSON, supra note 24, at 448. Samuelson shows that the long-run break-even condition:

comes at a critical P[rice] where the identical firms just cover their full competitive costs. At lower long-run P[rice], firms would leave the industry, until P[rice] had returned to the critical equilibrium level; at higher long-run P[rice], new firms would enter the industry replicating what existing firms are doing and thereby forcing market price back down to the long-run equilibrium P[rice] where all competitive costs are just covered. . . . P[rice] = MC (Marginal cost) — minimum competitive costs.

id.

34. In the pure sense, of course, they almost never occur. Samuelson notes that a few
librium in imperfectly competitive markets can result in economically and socially harmful resource misallocation.\textsuperscript{35} The textbook definition of an imperfectly competitive industry is an industry where an individual seller controls such a large percentage of the total market that it can affect the price of a product by restricting or expanding its own production. In such an oligopoly (or monopoly) the equilibrium point of supply and demand does not result in maximum production or efficiency because it is always to the imperfect competitor’s advantage to keep prices above marginal cost by restricting production. With no need to cut price in order to increase quantity, the incremental marginal revenue of each additional unit produced is “precisely the price received for that last unit, with no loss on previous units being subtracted.”\textsuperscript{36} Therefore an oligopolistic producer “maximizes profits by equating marginal revenue to marginal costs, which leads to a price that is above marginal cost. . . . The canny seller contrives an artificial scarcity of his product so as not to spoil the price he can get on the earlier premarginal units.”\textsuperscript{37}

The regulators have failed to distinguish degrees of oligopoly power in the industries they seek to regulate. Such distinctions are necessary to ensure that the extent of regulation is proportionate to the degree of oligopoly power in the industry. Judicious use of regulatory powers may indeed serve to counteract the misallocative effects of oligopoly power on resource distribution; indiscriminate regulation, however, results in far greater resource misallocation than the oligopoly it is designed to neutralize.\textsuperscript{38} Since the administrative costs of regulation are high, and the polit-

\textsuperscript{35} As Samuelson explains: “Under free pricing, when firms face a sloping demand curve, their marginal Revenue is below their price. Then, to the degree that such imperfect competitors intelligently pursue their self-interest, they will not be led by Adam Smith’s Invisible Hand to perform the acts needed to promote the general interest.” \textit{ld. at 475.}

\textsuperscript{36} \textit{id. at 474.}

\textsuperscript{37} \textit{id. at 479-80.}

\textsuperscript{38} H. SPIEGEL, \textit{supra} note 23, at 641. Misallocation of resources in the transportation industry may be traced directly to indiscriminate regulation. One such example in railroad regulation has been explained by Professor Friedlaender:

Railroads are best suited to carrying high-density traffic with a minimum number of distribution points. The costs of service to relatively small, isolated communities with low traffic densities and inefficient means of distribution are substantially higher than the costs of service to communities with high traffic densities and efficient means of distribution. However, rates cannot generally reflect these cost differences.

The problem is compounded by the Commissions’s use of average costs in intermodal rate cases. Although efficient railroad operations may have a substantial cost advantage over trucks, the average cost data used by the Commission may not reflect it if the railroads perform a large amount of low-density service. Similarly, although trucking operations may have a substantial cost advantage over low-density rail service, the average cost data used by the Commission may not reflect it if the railroad performs a
ical incentives are great, it is important to critically examine not only the economic effects of regulation on a particular industry, but also to look at the motives, political or otherwise, that brought it about. The transportation industry is an excellent case study in this regard, for perhaps no other industry has been subjected to such indiscriminate and self-defeating reg-

substantial amount of high-density, efficient service. By considering only average costs, the Commission effectively prevents each mode from adopting rates that would reflect their true cost advantage.

An efficient traffic allocation would permit the railroads to perform a wholesaling service and specialize in handling high-density traffic between major centers. It would permit trucks to perform a retail or distribution service and specialize in handling relatively low-density traffic. Such specialization would lead to a diversion of large-volume trucking traffic to rails, a diversion of low-volume rail traffic to trucks, and lower transport costs. By refusing to let rates reflect relative costs, the Commission ensures a continued traffic misallocation and excessively high transport costs.


39. Regulatory legislation is the end product of a political process, which is sensitive to large power blocs and groups. See Olson & Trapani, Who Has Benefited From Regulation of the Airline Industry, 24 J.L. & ECON. 75 (1981). Jordan’s study of both the regulated and unregulated airline industry in California revealed that regulations resulted in excess capacity and thus benefited airplane manufacturers, employees and suppliers. W. JORDAN, AIRLINE REGULATION IN AMERICA 226-38 (1970), noted in Olson & Trapani, supra, at 75. For a discussion of union political incentives, and the effects of union power on regulation, see Hendricks, Fehille & Szerszen, Regulation, Deregulation, and Collective Bargaining in Airlines, 34 INDUS. & LAB. REL. REV. 67 (1980).

Stigler analyzes political power and regulation as follows:

When an industry receives a grant of power from the state, the benefit to the industry will fall short of the damage to the rest of the community. Even if there were no deadweight losses from acquired regulation, however, one might expect a democratic society to reject such industry requests unless the industry controlled a majority of the votes . . . .

Because the political decision is coercive, the decision process is fundamentally different from that of the market. If the public is asked to make a decision between two transportation means comparably to the individual’s decision on how to travel—say, whether airlines or railroads should receive a federal subsidy—the decision must be abided by everyone, travellers and non-travellers, travellers this year and travellers next year . . . .

The industry which seeks political power must go to the appropriate seller, the political party. The political party has costs of operation, costs of maintaining an organization and competing in elections. These costs of the political process are viewed excessively narrowly in the literature on the financing of elections: elections are to the political process what merchandising is to the process of producing a commodity, only an essential final step. The party maintains its organization and electoral appeal by the performance of costly services to the voter at all times, not just before elections. All of the costs of services and organization are borne by putting a party of the party’s workers on the public payroll. An opposition party however, is usually essential insurance for the voters to discipline a party in power, and the opposition party’s costs are not fully met by public funds.

The industry which seeks regulation must be prepared to do so with the two things a party needs: votes and resources.

ulation. The heavy-handed regulation of the railroads during the last three quarters of a century virtually brought that industry to its knees before recent legislation gave it one last chance, short of nationalization, to survive.

George Stigler, in his landmark article, *The Theory of Economic Regulation*, looks at two alternative views of regulation—regulation for the "benefit of the public" and regulation as the result of the political use of power by vested interest groups. In examining the second view, Stigler proposes the following general hypothesis: "[E]very industry or occupation that has enough political power to utilize the state will seek to control entry."\(^{40}\) Thus, other state powers sought by an industry will include those which affect substitutes and complements (thus butter producers will try to suppress margarine and encourage bread production; airlines will urge subsidies for airports).\(^{40a}\) Finally, an industry, through coercive use of government power, will seek to fix prices above the level which would be determined by supply and demand. Oligopoly profits can thus be achieved either by market concentration, or by use of political power. Ironically, regulation can actually serve as a substitute for naturally created oligopoly power. Stigler examines the nature of the political process in which an industry or interest group can employ political machinery which is beneficial to that industry but harmful to the public at large.

Once the political process of regulation is understood, its dangers can be appreciated. When evaluating regulation of an industry, five questions must be asked: first, does oligopoly power exist in the industry; second, what is the source of the oligopoly power (i.e., is the industry a "natural" monopoly);\(^{41}\) third, what is the extent of the oligopoly power, and to what degree does it result in distortion of market prices and the

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40a. *Id.*
41. Economists generally define "natural monopoly" as one where economies of scale are so great that only a single producer is viable in the industry." J. Hirshleifer, *supra* note 33, at 300. By the same reasoning, a "natural oligopoly" is where economies of scale are so great that only a limited number of producers are viable in the industry. The capital requirements of economies of scale are usually high, creating a "natural" barrier to entry. Thus, it is important to determine the barriers of entry to a particular industry before choosing a regulatory model. In theory, where barriers to entry are sufficiently high to result in the creation of a natural monopoly or oligopoly, some regulation may be necessary to neutralize the oligopoly power. Likewise, where barriers to entry are not so high and where many producers may therefore enter an industry, regulation becomes self-defeating, especially if regulation takes the form of limiting entry. In fact, regulation under these circumstances actually creates barriers where none existed before, taking the place of "natural" barriers. This is exactly what happened with airline regulation: artificial barriers to entry were created, thus actually creating an "artificial oligopoly." The airline industry is a classic example of such an artificially created oligopoly. When airline regulation began in 1938, there were 16 carriers, which gradually evolved into 10 domestic trunk lines. No new trunk lines were permitted entry prior to 1978. Harvard Project, *supra* note 3, at 5. The tragedy of this heavy-handed regulation was that such an oligopoly was totally unnecessary because of the relatively low economies of scale and barriers to entry in the industry.
misallocation of resources; fourth, will the benefits of regulation outweigh
the administrative and social costs; and finally, are there independent
political motives and incentives that may explain the nature of the regula-
tion ultimately enforced?

With regard to the transportation industry, these questions must be
asked in relation to each of its primary modes: railroad, motor carrier and
airline. The answers for each are different and will be considered sepa-
rately in evaluating the effects of deregulation.

III. SURFACE TRANSPORTATION REGULATION (1887-1976): PRODUCER
PROTECTION AND THE RISE OF THE ARTIFICIAL OLIGOPOLY

Critics of the recent revolution in deregulation point to the past few
years experience in airline deregulation to prove their point that deregula-
tion is a "dismal failure."42 (The fact that deregulation coincided with a
severe recession and skyrocketing fuel costs43 does not cloud these crit-
ics' vision, nor does the evidence of declining fares,44 better community
service,45 or even recent record industry profits.46) An evaluation of the
effects of regulation compared to the effects of deregulation is not possi-
ble. The evaluation of deregulation is based on the experience of a few
short years, while an evaluation of regulation is based on the experience
of forty years of regulation in the airline industry,47 forty five in the motor
carrier industry,48 and ninety three years in the railroad industry.49 Stud-
ies of that experience reveal what is now obvious to all but the die-hard
regulators: "There is a growing consensus that all of these regulatory
programs have been monumental failures, in some cases bordering on
disaster."50

Histories of the regulatory experience in transportation are numerons
and readily available,51 and no attempt will be made to repeat them in

42. Dempsey, supra note 5, at 386; W. Augello, The Deregulation Disaster 10 (1982) (un-
published monograph).
43. See supra note 4.
44. See supra note 3.
45. See supra note 7.
46. USA Today, supra note 6.
47. The period from 1938-1978. Although the Civil Aeronautics Act of 1938, ch. 601, 52
Stat. 973, marks the beginning of rigid entry control, previous acts actually began the regulatory
process: Contract Air Mail Act of 1925 (Kelley Act); Waters Act of 1930; Black-McKellar Act of
1934. For an excellent history of these early years of regulation, see HARVARD PROJECT, supra
note 3, at 13-37; Dempsey, supra note 7, at 95-107.
48. The period from 1935 to 1980. For a history of these years, see infra text accompanying
notes 79-126; Dempsey, supra note 1; Sloss, Regulation of Motor Freight Transportation: A
49. The period from 1887 to 1976.
50. Jones, supra note 18, at 316.
51. See supra notes 47-48.
detail here. Nevertheless, highlights of the regulatory experience are useful for purposes of comparison with, and evaluation of, the deregulatory experience.

A. THE POLITICS OF RAILROAD REGULATION: THE GREAT TRAIN ROBBERY

Railroads perhaps epitomize an illustration of Stigler's hypothesis: "[E]very industry or occupation that has enough political power to utilize the state will seek to control entry."52 Railroad regulation has its roots in the failure of early railroad robber barons to form their own cartels and "pools." The incentive to form such cartels and pools was high because of the fierce competition, which resulted in lower profits for the railroad magnates. In 1880, for example, shippers in Atlanta and St. Louis had twenty competitive routes between the cities to choose from. By 1900, there were 1224 operating railroads, and by 1907, there were 1564. By 1980, after ninety three years of regulation, the number of operating railroads had been reduced to but seven major carriers accounting for eighty five percent of traffic.53 Because of this drastic reduction, it is now fashionable to refer to the railroad industry as a "natural" monopoly. There was nothing very "natural" about the regulation from 1887 to 1980. It virtually created a transportation oligopoly.

In the competitive atmosphere of the 1870's and '80's many railroads offered substantial rebates to shippers. In hopes of increasing profits, many railroad barons began calling for "anti-rebate" laws, i.e., a legalization of price-fixing and "pooling," and other anti-trust exemptions. By 1887, the barons had succeeded in characterizing any discounts or rebates to shippers as "discriminatory." Facing the same problems as today's oil cartels, the barons' attempts to raise rates by pooling and price-fixing repeatedly failed because of the large number of competitors.54 In 1879, the head of the first government railroad statistics department recognized that pooling agreements would never work unless made enforceable by law.55 When national freight rates declined by twenty percent, men such as Henry Seligman noted that "[t]he merchants are securing the benefits of very low rates, to which I suppose they do not object.56 By 1884, such rail magnates as John P. Green were testifying to the House Committee on Commerce that "a large majority of the railroads in the United States would be delighted if a railroad commission or any other power could make rates upon their traffic which would insure

52. Stigler, supra note 39, at 5.
54. See id. at 10-11.
55. See id. at 26 (citing Apr. 15, 1899 memo by Joseph Nimmo, Jr.).
56. See id. at 30 (citing letter from Henry Seligman to Philip N. Lilienthal (Mar. 16, 1885)).
them six percent dividends." 57 Friedlaender has observed that the railroads during this period supported regulation in part to formalize a rate structure. 58 But perhaps the barons' greatest accomplishment was their

57. See id. at 35 (citing Hearings Before the House Comm. on Commerce, 48th Cong., 1st Sess. 1-2 (1884) (testimony by John P. Green)).

58. A. FRIEDLAENDER, supra note 1, at 2 (citing the following works supporting the view of railroad support of regulation: S. BUCK, THE GRANGER MOVEMENT, 1870-1880 (1913); L. BENSON, MERCHANTS, FARMERS AND RAILROADS: RAILROAD REGULATION AND NEW YORK POLITICS 1850-1887 (1955); I. TARBEH, THE HISTORY OF THE STANDARD OIL COMPANY (1904)).

There were a few Railroad men who did not welcome the 1887 Act. John Murray Forbes and William Bliss. See Letter from John Murray Forbes to John M. Endicott (Jan. 29, 1887); Letter from William Bliss to Chauncey Depew (Jan. 20, 1887), quoted in G. KULKO, supra note 53, at 45. For the most part, however, the Railroads openly welcomed regulation, as Kulko has observed:

It is not my contention, of course, that railroad leaders were the only group favoring the federal regulation of transportation. The mere fact that they did not always get their specific legislative demands indicates that not only were the railroads divided among themselves as to precisely what legislative measures they wanted passed, but that they faced opposition on many points from shipping groups who had their own goals and demands. Railroad interests differed from line to line, and the disagreements among the railroads were frequently as strong as the disagreements between the bulk of the railroads and many shippers. The crucial point is that the railroads, for the most part, consistently accepted the basic premises of federal regulation since only through the positive intervention of the national political structure could the destabilizing, costly effects of cutthroat competition, predatory speculators, and greedy shippers be overcome. Moreover, the railroads were a much more constant force for federal regulation than the shippers, and the deeper divisions within the ranks of shippers often meant that their agitation for regulation contributed to the interests of the railroads. Legislative proposals, to be successful, usually needed the support of both the railroads and important shipping groups, and throughout the period from 1877 to 1916 neither could obtain legislation without the support of the other for some general form of legislation.

Virtually all histories of railroad regulation have focused on the views and actions of politicians, farmers, or shippers. And while these groups played a crucial part, . . . the role of the railroads and the railroad men in the movement for federal regulation has largely been ignored, beyond the automatic assumption that they naturally opposed regulation. Such a perspective, . . . is like ignoring the role of the Confederates in the Battle of Gettysburg . . .

G. KOLKO, supra note 53, at 5-6.

Only the railroads were consistently interested in increasing federal regulation of the railroads throughout the 1890's. Neither merchants nor farmers offered significant opposition to their plans. Some merchants, especially in the East, actually aligned themselves with the railroads. It was clear to these merchants that rates were declining, and this alone took the impetus out of their earlier anti-railroad sentiment.

_id. at 78.

While the Railroads generally supported federal regulation, they had however, found state regulation difficult to control. When the states first began regulating the railroads in the late 1860's and early 1870's, the railroads challenged the state regulations, alleging that regulation of interstate commerce was within the exclusive power of the United States under Art. I, § 8 of the U.S. Constitution. Although state regulation was generally upheld, see Munn v. Illinois, 94 U.S. 113 (1876); Winona & St. P. Ry. v. Blake, 94 U.S. 180 (1876), it began to wane by the early 1880's, leaving the way open for federal regulation, culminating with the passage of the Interstate Commerce Act of 1887. For an excellent history of this early period, see Harris, supra note 1, at 4.

The Railroad's resistance to state regulation but support of federal regulation is consistent with Professor Thom's observation: "The railroads have been the most intensely regulated of the
political success in characterizing any competition as "chaotic." 59 Big oil producers even organized a letter writing campaign, which flooded Congress with petitions calling for "the passage of a law to regulate commerce." 60

There is no question that there were abuses in the railroad industry. The secrecy of many transactions, for example, resulted in widespread corruption and injustice. 61 But such abuses, created by the railroads themselves, were then used by them to justify not just remedial social legislation, but legislation to enforce higher rates across the board—something that attempts at illegal price-fixing had been unable to accomplish. But even the passage of the ICC Act 62 was not sufficient to satisfy the railroads' thirst for government-imposed oligopoly profits. Discounts and rebates persisted in reducing railroad profits. In 1899, Alexander Cassatt, president of the Pennsylvania Railroad, led the fight against rebating, 63 which finally resulted in the adoption by Congress of the Elkins Act 64 in 1903. The Hepburn Act of 1906 gave the railroads even more power to take the initiative in maintaining rates, prompting George Perkins to write to his superior, J.P. Morgan: "[T]he Hepburn bill is going to work out for the ultimate and great good of the railroads. There is no question but that rebating has been dealt a death blow." 65 The railroads had been


59. Harris, supra note 1, at 5.
60. See G. KOLKO, supra note 53, at 23.
61. Oren Harris described conditions:
There was the sale of worthless securities and the granting of public land and credit by public officials to railroad corporations for worthless schemes.
In regard to the frenzied speculation and manipulation that occurred, the Cullom report had this to say:
Railroad corporations have been organized and manipulated by speculators; rings within rings have controlled their operations and fattened on their revenues; "railroad wrecking" has become a fine art; values have been made to fluctuate wildly, without due cause; panics have been occasioned by the magnitude of these operations, and the whole railroad system, as well as the commerce of the country, will suffer for years from the effects of those eras of mad speculation which are yet fresh in the memory of all.

Harris, supra note 1, at 4 (emphasis added).
63. See generally Creelman, All is Not Damned, 15 PEARSON'S MAG. 543-54 (1906); Carnegie, My Experience with Railway Rates and Rebates, 75 CENTURY MAG. 722-28 (1906), cited in G. KOLKO, supra note 53, at 96.
65. Hepburn Act, ch. 3591, 34 Stat. 584 (codified as amended in scattered sections of 45 U.S.C.). This Act extended the provisions of the Elkins Amendment to cover express, sleeping
very careful not to voice their support of the Hepburn Act for fear of creating political liability for the bill’s congressional proponents; but by the time its passage was assured the railroads were openly expressing support. The New York press even declared that the railroads had written the whole bill and "[t]his explains why the railroad lobbies did not raise a note of public or private protest against the Hepburn bill in the house."66

The Hepburn Act’s solution to “discriminatory” pricing seemed to suit almost everyone, especially the railroads: simply make all pay the highest rate. Once again the railroads had managed to translate the obvious need for securities law and anti-trust reform into railroad protection legislation.

Regulation left the railroads unprepared to compete with an unregulated motor carrier industry.68 Indeed, the competitive advantage of an unregulated motor carrier industry was an important rationale for regulating motor carriers in 1935.69 Motor carrier competition and subsidies,

car and private car lines. Notice of rate charges was extended to 30 days from 10 days; it provided specific fines for rebating; and provided for a two year prison term for violations. Most important was Section 15, which provided that, upon complaint of a shipper or railroad, the ICC could determine “just and reasonable rates.” See G. KOLKO, supra note 53, at 144-45. The Progressives in the 1912 campaign portrayed the act as victory over the Railroads. Frank Dixon wrote in 1922: “It was in 1906 that the railroads fought their fight to the finish against federal regulation.” F. DIXON, RAILROADS AND GOVERNMENT 1910-1921, at 3 (1922). Such a portrayal was, of course, entirely satisfactory to the Railroads, since they realized that such a portrayal was politically necessary for passage. See supra note 58.

66. See G. KOLKO, supra note 53, at 139 (quoting N.Y. Press, Mar. 16, 1906). Rail Magnate Cassatt stated in 1906: “Let the Government regulate us. For my part and for my associates in the Pennsylvania Railroad Company, I am generally heartily in accord with the position taken by President Roosevelt, and we have been all along.” Creelman, supra note 63, at 551-52. The Railway World stated in 1906: “[N]otwithstanding the fears of many that railroads would be hurt by the operation of the law, no complaint has been heard from railroad men against its general provisions. On the contrary, the complaints are coming from the shippers, who were supposed to be the chief beneficiaries of the law.” G. KOLKO, supra note 53, at 150 (quoting RAILWAY WORLD, Aug. 24, 1906, at 729).

67. See Harris, supra note 1.

68. A study by Clifford Winston reveals that despite rail’s cost advantage over motor freight, it has been prevented from pursuing this advantage by regulation. Winston, The Welfare Effects of ICC Rate Regulation Revisited, 12 BELL J. ECON. & MGMT. SCI. 232, 233 (1981). Rail rate regulation affected the railroads in competing with exempt motor carriers. Since truckers could vary their rates to accommodate swiftly changing market conditions but railroads could not, the result was devastating for the railroads. See Thoms, supra note 58, at 194.

69. Nelson and Greiner, while acknowledging the pressures for motor carrier regulation brought by certain shippers, have observed that: “Control of truck competition through regulation may have held out the prospect of helping the railroads . . . .” A. FRIEDLAENDER, supra note 1, at 22. E. Anderson has summarized the logic of the legislative history of the Motor Carrier Act of 1935 as follows:

(1) railroads are regulated by the Interstate Commerce Commission;
(2) motor carriers are competing with railroads; therefore,
(3) motor carriers should be regulated by the Interstate Commerce Commission.

Anderson, supra note 19, at 28.
and the iron hand of the ICC, finished the job begun by the early regulators. By the 1970’s, the railroads were in a state of virtual collapse. A 1974 White House Paper on Regulatory Reform concluded: “Railroading is a troubled industry. Virtually every American suffers some consequence of the industry’s afflictions.”\(^{70}\) The study also found that half of all rail track was unfit for high speed operations, and that train speed limits of ten to twenty miles an hour were not uncommon. Accidents and derailments doubled from 1967-1974. A typical freight car moved only twenty three days a month.\(^{71}\) The report also found that “cumbersome regulatory procedures impede responses to competition and changes in market conditions and at times result in traffic being handled at noncompensatory rates. Those procedures also have created a serious impediment to needed restructuring.”\(^{72}\)

Professor Thoms has mused that Washingtonians like to boast about their three great museums: the Smithsonian, the National Archives and the ICC.\(^{73}\) According to Professor Thoms, by 1970 the effect of the latter’s “utility-type regulation upon the railroads had been amply documented. The industry everywhere was in decline, with higher fixed costs leading to a rate of return much lower than the cost of capital. Some railroads had disappeared, others were seeking salvation through merger with parallel lines . . . .”\(^{74}\) To make matters worse, although “[t]here had been some savings in labor costs through dieselization and consolidation of trains, . . . increased labor costs were still passed on to the public in general rate increases,”\(^{75}\) further eroding the railroads’ competitive position.

But by the mid-1970’s, the American public had had their fill of railroad regulation. The critics, who had for so long warned against the ICC’s capture by the industry it was supposed to regulate, were finally being believed.\(^{76}\) An article in Trains echoed the popular sentiment: “The ICC must go!”\(^{77}\) The stage was set for the nearest thing to a popular uprising since 1776: the first steps toward freeing the railroads (as well as other transportation industry modes) from the stranglehold of regulation.\(^{78}\) It was perhaps fitting that it occurred during the 200th anniver-

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71. *Id.* at 64-65.
72. *Id.* at 65.
73. Thoms, *supra* note 58, at 190.
74. *Id.* at 195 (footnote omitted).
75. *Id.*
sary of that earlier revolution.

B. ECONOMICS OF RAILROAD REGULATION: THE CRY FOR REFORM

The speedy political origins of regulation might be irrelevant were it not for the tragic economic results. The irony of course is that, in the long run, the regulation which resulted from the railroad's quest for oligopoly profits incurred to the detriment not only of the public, but of the railroads. It has been noted that after ninety three years of regulation, the number of railroads declined from 1564 in 1907 to seven major carriers (carrying eighty five percent of the traffic) in 1980. Service deteriorated, profits slumped, and bankruptcies were endemic. Regulation had reduced a proud, robust industry on the forefront of the industrial revolution to a lumbering, whimpering giant: a sad legacy from the regulators and a mockery indeed of the "public interest." But perhaps most sad is the fact that the results may be irreversible. High barriers\textsuperscript{79} to entry prevent a quick return to the days of competition; the nation is now saddled with what may be a permanent oligopoly. Thus, unlike the airline industry, steps towards railroad deregulation have been more tentative\textsuperscript{80} to allow a more gradual rise of the phoenix. Even those on the forefront of deregulation recognize that going "cold turkey" may not have the desired effect on a ninety three year old regulation addict.

The rationale for early regulation was "discriminatory pricing."\textsuperscript{81} It is true that the Interstate Commerce Act initially caused a reduction in price discrimination—"in large part to facilitate increases in the general rate level and to make cheating on the cartel agreement more costly."\textsuperscript{82} Arguments in favor of reducing price discrimination were seductive.\textsuperscript{83} In the long-run, however, they put the railroads at a competitive disadvantage from which they have not yet recovered.\textsuperscript{84}

\textsuperscript{31} (codified in scattered sections of 45, 49 U.S.C.). De facto deregulation of airlines is generally considered to have begun in 1976. See supra note 2.

\textsuperscript{79} Stephen Breyer has noted that "[v]irtually every form of classical regulation tends to raise barriers to entry into the regulated industry. Cost-of-service ratemaking is almost always accompanied by rules or laws that require a commission to allow new firms to enter the industry only if it serves the 'public convenience and necessity.' " S. Breyer, supra note 30, at 194 (emphasis in original).

\textsuperscript{80} See Thoms, supra note 58, at 212: "What emerged, of course, was compromise. Re-regulation rather than deregulation was the order of the day. It was hardly a consumer bill—it was addressed to the real problem of flagging rail revenues." Id. (footnote omitted). See also Birkholz, The Staggers Act of 1980, Deregulation and Regulation: A Railroad Perspective, 17 Forum 850 (1982); Abrams, Railroads and Deregulation, 17 Forum 844, 844 (1982) ("Let's begin by remembering that the ICC still regulates some rates . . . .")

\textsuperscript{81} Harris, supra note 1, at 4.

\textsuperscript{82} Jordan, supra note 17, at 168.

\textsuperscript{83} See S. REP. No. 46, 49th Cong., 1st Sess. (1886); see also supra note 61.

\textsuperscript{84} A. Friedlaender, supra note 1, at 63. As Friedlaender has pointed out:
A 1968 Presidential Task Force on Anti-Trust Policy stated that "price discrimination has an adverse effect on competition only in exceptional cases."\textsuperscript{85} and that in some cases "price discrimination improves the functioning of the competitive system."\textsuperscript{86} A 1969 Presidential Task Force on Productivity and Competition found that price-cutting, even in oligopolistic industries, led to general price reductions and thus benefited competition.\textsuperscript{87} It is now apparent that the price-discrimination provisions in the railroad regulatory legislation were primarily protectionist in scope and not for promotion of the general welfare.\textsuperscript{88}

But if the intent of regulation was really to prevent rate discrimination, it sorely missed the mark. While eliminating price discrimination that would have increased efficiency, the "enactment of the 1903, 1906, and 1910 laws...combined with the ICC's frequent suspension of the provisions of Section 4 [of the Interstate Commerce Act of 1887] resulted in a resurgence of locational discrimination."\textsuperscript{89} It has been observed that "over 100 years of development have resulted in a marvel of complicated discriminatory pricing."\textsuperscript{90} In fact, in 1970, it was reported that there were

Price discrimination is probably a necessary aspect of the transportation industry. Different shippers have different elasticities of demand and are faced with different marginal costs for their shipments. Railroads have large fixed costs relative to their variable and marginal costs. As long as substantial excess capacity prevails, the optimal use of capacity requires price discrimination.

The marginal shipper with a high elasticity of demand can be accommodated at close to marginal cost, while captive shippers with a low elasticity of demand can be used to cover the overhead and charged rates considerably above costs. Without price discrimination all shippers would be charged the same rate and less traffic would move. Thus price discrimination enables the railroads (or other modes) to capture the consumers' surplus of the low-elasticity shipper to enable them to carry the goods of the high-elasticity shipper. So long as the railroads are operating in the failing or constant portions of their cost curves, this leads to the maximum use of resources and thus is socially desirable.\textsuperscript{ld. at 63-64.}

\textsuperscript{85} WHITE HOUSE TASK FORCE ON ANTITRUST POLICY, ANTITRUST & TRADE REGULATION REPORT [NEAL REPORT] 3 (1968).

\textsuperscript{86} Id. at 10.


\textsuperscript{88} Weston, Rail-Barge Competition and Predatory Pricing: A Legal Perspective, in RAILROAD REVITALIZATION, supra note 70, at 147.

\textsuperscript{89} Jordan, supra note 17, at 168.

\textsuperscript{90} Id. The pricing is no less discriminatory and nightmarish in the trucking industry. Discrimination by class is incredibly complex. As Breyer explains:

The "class rate" lies at the heart of the system. The National Motor Freight Classification assigns approximately 25,000 commodities to 23 classes. The standards used for classifying include both cost- and demand-related factors. Each class is given an index number from 35 to 500, with 100 as the reference point. This number gives the class a constant relationship to all other classes. A tariff also develops a series of "rate-basis numbers"—basically a mileage scale occasionally modified to reflect spe-
over 43 trillion railroad rates on file with the ICC.\textsuperscript{91}

The complaints of a mounting chorus of economists\textsuperscript{92} and public leaders\textsuperscript{93} went largely unheeded until the mid-70's, when many railroad firms made it clear that the likely alternative to regulatory reform was massive government subsidy.\textsuperscript{94} Levine has observed:

As scholars examined the record of regulated industries, they found prices which were too high or too low, distorted allocations, mercantile protection, suppression of innovation, extension of regulation beyond the bounds of any known market failure, and protection of entrenched interests, corporate or geographic, from any change at all costs.\textsuperscript{95}

Economists have long argued against the ICC's use of "Value of Service" pricing.\textsuperscript{96} The basic economic rationale of regulation is to keep price at marginal cost or at least average cost.\textsuperscript{97} On the whole, however,

\begin{itemize}
  \item Special transportation characteristics such as mountainous terrain. A Shipper looks up a rate on a tariff table. He determines the class-rating number from the commodity classification table and the rate-basis number from a list of origin and destination points. He then refers to a table, or "class tariff," which has class ratings on one axis and rate-basis numbers on the others. The cell that he locates will have the rate in cents per hundredweight (it may have several rates, for different weight categories).
  \item S. Breyer, supra note 30, at 231.
  \item 2 I. Kahn, The Economics of Regulation: Principles and Institutions 26 (1970).
  \item See, e.g., A. Friedlander, supra note 1; Railroad Revitalization, supra note 70.
  \item See Levin, supra note 17.
  \item Levine, supra note 91, at 179.
  \item See Railroad Revitalization, supra note 70, at 14. See also 1 I. Kahn, The Economics of Regulation: Principles and Institutions (1970):
  \item The basic defeat of full cost distributions as the basis for pricing is, then, that they ignore the pervasive discrepancies between marginal and average cost. Those discrepancies may require prices that take into account not just the cost but also the elasticities of demand of the various categories of service if the company is to recover its total costs. Whenever there is some separable portion of the demand sufficiently elastic that a rate below fully-distributed costs for it would add more to total revenue than to total costs, any insistence that each service or group of patrons pay their fully allocated costs would be self-defeating. It would force the firm to charge a price that would result in its turning away business that would have covered its marginal costs—in other words, would prevent it from obtaining from customers with an elastic demand the maximum possible contribution to overheads. Thus, under the guise of ensuring a fair distribution of common costs and preventing undue discrimination, it would be serving the interests neither of the patrons who would be prepared to take additional quantities if prices were closer to marginal costs, nor of the customers with the more inelastic demands.
  \item Id. at 155.
  \item Samuelson explains that if an industry is to be regulated in order to wipe out its "excess profits," regulators should force the price to where it equals average cost [AC], "and price covers only normal costs." P. Samuelson, supra note 24, at 479. However, Samuelson advocates that: "Ideally, [price] should be forced all the way down to MC [marginal cost] . . . ." Id. The latter solution, however, usually requires a government subsidy since "with a decreasing cost situation . . . setting P = MC while AC is still falling will involve [t]he firm in a chronic loss." Id. In summary:
  \item Monopolistic deviation from \( P = MC \) means "exploitation" of labor (and other transfer-
regulated railroad rates have been kept artificially pegged above marginal costs—precisely the effect regulation was supposed to avoid. Thus, economists have long advocated the use of "variable cost" pricing. When federal regulation was first enforced in 1887, it rested on the assumption of decreasing costs. Economists have recognized, however, that "costs were in fact not decreasing." Unfortunately, what was obvious to the economists was not so to the regulators who experienced political and interest group pressures. Economists had long realized that "[v]alue of service pricing leads to misallocation of transport resources, misplaced locational decisions, and distortion of the entire structure of production and of consumption. The regulatory process itself tends to encourage excess capacity and stifle initiative." The literature is rich with economic analyses critical of regulation. The economic case against regulation may be summarized as follows:

1. **Traffic Misallocation:** Under regulation, many shipments did not go by the low-cost carrier. In the absence of rate competition, trucking attracted much traffic that could go

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able resources), in the sense that society's labor is misapplied as between goods and leisure or as between too-scarce monopolized goods in relation to too-plentiful competitive goods.

*Id.* at 480.

The problem, of course, is that economics is at best an inexact science, and even the best-intentioned regulators can not hope to fathom the various costs, marginal costs, and average costs of an industry, and even if they could, estimates of "a 'proper' rate of return carried out to one or two decimal places are unlikely to be worth the effort expended." S. Breyer, *supra* note 30, at 59. As Breyer explains:

The standard to which such efforts implicitly appeal is that of overcoming "distortions" produced by competitive market failure—the standard of trying to replicate what would occur without such a failure. Yet in trying to overcome such failures the regulatory process introduces so many distortions of its own, that one should be satisfied with gross estimates and not insist upon refined economic calculations. Second, insofar as cost-of-service ratemaking is advocated as a "cure" for market failure, one must believe that the unregulated market is functioning quite badly to warrant the introduction of classical regulation. That is to say, the regulatory process—even when it functions perfectly—cannot reproduce the price signals that a workably competitive marketplace would provide. Thus, only serious market failure will, even arguably, warrant the adoption of cost-of-service ratemaking as a cure.

*Id.* The irony, of course, is that so much expense and energy is expended by regulators to accomplish so imperfectly what is achieved virtually automatically by a free economy.


99. *Id.* While "variable cost" pricing may be better than value of service pricing, the fact remains that any external and coercive price mechanism related to costs will result in stifling incentives for cost reduction. As long as obtaining regulated rate hikes provides the path of least resistance, there will be no incentive for fighting intrinsic lost battles, since they are not necessary for survival. *Id.* at 108.


101. *Id.*

cheaper by rail. By 1969, the cost to society of such resource misallocation resulted in an annual cost of a half billion dollars.\textsuperscript{103}

2. \textit{Excess Capacity}: The ICC refusal to permit rates that reflected higher costs of irregular route and peak demand service, combined with the regular emphasis on "fair return on fair value," encouraged wasteful and destructive overcapacity.\textsuperscript{104}

3. \textit{Reduced Incentives for Technological Change and Innovat-

\textsuperscript{103} A. FRIELAENDER, supra note 1, at 98. As Friedlaender explains:

What then are the costs of the present regulatory policies? First is the misallocation of traffic resulting from the continuance of value-of-service pricing. Since railroads and trucks cannot compete for high-density traffic by cutting rates, an area in which railroads have the advantage, competition is concentrated on the service sphere, an area in which trucks have the advantage. Thus a considerable amount of high-density traffic goes by truck that could in fact go more cheaply by rail. Moreover, the use of uniform rate schedules prevents trucks from capturing a good deal of the low-density traffic that currently goes by rail. Because of this lack of rate competition, rates are higher than they would be in a competitive situation. The direct social losses resulting from this misallocation may run about $500 million per year.

\textit{id.} Professor Breyer puts the case somewhat differently:

In a competitive industry, firms are motivated to produce efficiently—to find ways to cut production costs—by the hope of increased profits and by the fear that failure to keep costs low will cause more efficient firms to capture their customers by lowering price. In a regulated industry, the stick is usually unavailable. The carrot has diminished influence, for, if ratemaking is based upon actual costs and is performed accurately and promptly, firms do not benefit by adopting cost-saving devices; the total saving produced by increased efficiency flows to the consumer.

S. BREYER, supra note 30, at 47.

\textsuperscript{104} In an unregulated industry, a firm’s insistence on costly excess capacity could be ruinous, and that firm would fail in the face of a competitor able to cut costs by reducing excess capacity. In a regulated industry, however, where firms do not have the option of open price competition, competition must be for service, i.e., providing transport even during peak periods (which of course means substantial over capacity in off-peak periods). Thus, whether a shipper wants to pay extra for the slightly greater convenience or not, he has to pay for it. Since a regulated firm can always get a rate hike based on costs (even costs of excess capacity), there is no incentive to cut down on excess capacity. Nor need a regulated firm fear a price reduction by a competing firm since: a) the competing firm’s price can be challenged in a long expensive hearing, and b) the competitor has the same incentives for passing on the costs of excess capacity in the form of rate hikes. The MacAvoy Study found in 1974:

In some parts of the country, there now is capacity to provide more rail service than is demanded at current rates. In this case, the elements that constitute variable costs are less inclusive than when additional capacity is demanded, because only those cost elements which are dependent on the volume of service are included. The reason for this is that variable costs must include only those elements which are required to provide, on a continuing basis, the demanded services. Since the level of service demanded falls short of the available capacity, no funds are required to expand or even, in the long run, to maintain the existing facilities. Indeed, it is desirable that the capacity shrink so that the resources can be redeployed. If monies are not provided for the replacement of fixed assets, there will be a gradual shrinkage of capacity to the level demanded.

Snow, The Ford Administration’s Proposal for Rail Regulatory Reform, in RAILROAD REVITALIZATION, supra note 70, at 78.
tion: "Since legalism rather than competition has been used to protect the public interest with regard to the railroads, little premium is placed on entrepreneurial aggressiveness and competitiveness." ¹⁰⁵

4. Reduced Incentives for Effective Management: Railroad management is usually made up of lawyers or bankers rather than engineers or scientists. An executive who can write a good tariff or get along better with regulatory authorities will rise faster than a good manager or innovator. ¹⁰⁶

The large amount of excess capacity existing in the transport industries is due to regulation. The concept of the common carrier has doubtless encouraged capacity expansion in the transport industry. Common carriers have a responsibility to the public to provide adequate transportation services, they must be available to carry goods to and from isolated locations; they must have sufficient capacity to meet the peak demands. These requirements would not necessarily lead to excessive capacity expansion if the carriers were permitted to charge rates that reflected the higher costs associated with irregular route or peak demand service. However, rate differentials of this type have traditionally been forbidden by the Commission. Since rationing the facilities through the price mechanism has been precluded, the carriers have found it profitable to maintain sufficient capacity to handle all irregular demands without prohibitive increases in costs.

A. FRIEDLAENDER, supra note 1, at 78-79.

¹⁰⁵. A. FRIEDLAENDER, supra note 1, at 92.

That the railroads spend relatively little on R&D and thus on potential innovations is clear . . . . All the available evidence suggests that the railroads have been particularly slow in adopting available innovations. For example, it took about 15 years for the diesel locomotive, 25 years for the mikado locomotive, 20 years for the four-wheel trucking locomotive, 25 years for centralized traffic control, and 30 years for retarders to be generally accepted.

. . . .

[T]he rate of innovation in the railroad industry has been stifled by the regulatory process.

. . . .

Moreover, even when railroad management wanted to exercise entrepreneurial initiative with regard to innovations, the Commission has often blocked the way. The experience of the Southern Railway System with its Big John cars provides a good case in point.

During the latter half of the 1950s, grain shipments to the southeastern portions of the United States rose from 3.6 million tons to 10 million tons . . . . The railroads did not share in this growing market, which was largely captured by barges . . . . or by truck . . . . Because the ICC does not generally permit major rate reductions without proof of concomitant cost reductions, the Southern Railway developed the large, lightweight, aluminum Big John cars in an effort to regain its share of this market. Each car is divided into four compartments and is easy to load and unload and to clean and maintain; its capacity of 110 tons is twice that of a traditional boxcar, while its weight is 13 tons less. Confident of the success of the cars, the Southern invested $14 million in them.

On August 10, 1961, the Southern announced that it was cutting rates up to 60 percent for minimum five-car shipments of 450 tons, with 90 tons to a car . . . . The economies that permitted these reductions were due to heavier loads per car, multiple-car shipments, and greater utilization, in which each Big John car was expected to travel up to 60,000 miles a year compared to the annual mileage of 16,425 miles for a typical boxcar. These rates were immediately challenged and suspended.

Id. at 91-93 (footnote omitted).

¹⁰⁶. Id. at 92.
5. Reduced Incentive for Cutting Costs: Since costs were considered in general rate increases, there was little incentive to cut costs or resist labor demands. It was far easier to request a rate increase. As Professor Thoms has noted: ""...increased labor costs were . . . passed on to the public in general rate increases.""\textsuperscript{107} In addition, regulation impedes the divestiture of wasteful, inefficient operations.\textsuperscript{108}

6. Uncompetitive Rates Due to Imposed Tariffs: The requirements of long cumbersome hearings for rate changes and reductions, the inability to adjust to market conditions, and the ease with which inefficiency is translated into high rates, account for rates which are up to nine to fifty percent higher than without regulation.\textsuperscript{109}

7. Reduced Incentives for Increasing Revenues: Regulations impede any revenue raising innovations which might adversely affect other carriers (such as soliciting business or adjusting rates on short notice to accommodate seasonal or cyclical demands).\textsuperscript{110} Railroads were also prohibited from diversifying into other forms of transportation.\textsuperscript{111}

8. Lack of Capital Investment incentives: With regulation dooming the railroads to low return on investment there was little incentive to invest funds necessary to modernize the industry.\textsuperscript{112}

9. Deterioration of Passenger Service: Encumbered by regulation, passenger service deteriorated. Thoms noted that ""[w]ith the exception of the heavily travelled Boston-Washington Corridor, service levels on American passenger

\textsuperscript{107} Thoms, supra note 58, at 195.
\textsuperscript{108} RAILROAD REVITALIZATION, supra note 70, at 86-91.
\textsuperscript{109} id. at 92.
\textsuperscript{110} In President Kennedy's 1962 Transportation Message, he emphasized ""the inability of carriers to make full use of their capacity by soliciting business or adjusting rates if such action would adversely affect other carriers."
\textsuperscript{111} A. FRIEDEKWARDT, supra note 1, at viii.
\textsuperscript{112} Thoms, supra note 58, at 196.

The ICC determined in 1978 that a return of 10.6% was needed just to cover capital costs. Adequacy of Railroad Revenue (1978 Determination), 361 I.C.C. 79 (1978). This figure was later increased to 11.22%. Adequacy of Railroad Revenue (1980 Determination), 364 I.C.C. 311 (1980). In 1978 the average rate of return was about 1%! Hearings on H.R. 4570 Before the Subcomm. on Transportation and Commerce of the House Comm. on Interstate and Foreign Commerce, 96th Cong. 1st Sess. 5 (1979) (statement of William H. Dempsey, President of the Association of American Railroads).

Obviously no astute investor will invest money at 1% when he can get 10% at the local savings & loan. Since one of the original rationales of railroad regulation was to prevent "monopoly profits," one wonders about a regulatory system that resulted in a return of 1%. If the road to Hell is paved with good intentions, the regulations should have a lot of pavement.
trains are the worst in the world."¹¹³ Often the deterioration was the result of purposely downgrading service in order to obtain regulatory concessions.¹¹⁴ If the above list is incomplete, it is only because the inefficiencies of regulation have so thoroughly pervaded the economic fabric of society.

The earliest efforts at reform,¹¹⁵ such as the Rail Passenger Service Act of 1970,¹¹⁶ have been characterized as railroad "euthanasia scheme[s]."¹¹⁷ It was not until the Railroad Revitalization and Regulatory Reform Act of 1976 (4R Act)¹¹⁸ that any significant regulatory relief was given to the railroads. This Act, while not changing the basic regulating scheme, nevertheless allowed the railroads some flexibility to raise and reduce rates, imposed restrictions on the ICC's power to suspend rate changes, relaxed time limits for ICC action, and adopted an intrastate rate-making provision.¹¹⁹ Finally, it introduced the concepts of "market dominance"¹²⁰ and "demand sensitive pricing."¹²¹

¹¹³ Thoms, supra note 58, at 196.
¹¹⁴ Id. at 197.
¹¹⁵ See generally Thoms, supra note 58, at 198 n.70.
¹¹⁷ Thoms, supra note 58, at 198.
¹²⁰ The Act purports to restrain rate flexibility where the railroad has "market dominance."
¹²¹ In light of the severe financial plight of the railroads, one wonders why even this restriction should apply. If the railroads can improve on their one parent return as capital in a market in which they are dominant, more power to them. As it turns out, however, "market dominance" for the railroads is almost totally illusory. As Jones noted:

The railroad's erstwhile dominant position in most transportation markets has been severely eroded. There is virtually no remaining market in which a railroad does not now face intermodal competition or in which such competition would not be promptly forthcoming in response to a railroad rate increase. Some of this competition comes from wholly unregulated carriers able to enter and leave markets at will and able to raise and lower prices in a matter of minutes in response to a competitor's action. The data also show that a wide range of options are open to shippers and consignees faced with railroad rate increases and that these options (seeking new markets or plant locations, changing inventory practices, and so forth) have been taken in the past in response to railroad rate increases.

Jones, The Meaning of Market Dominance, in RAILROAD REVITALIZATION, supra note 70, at 209. Jones concludes:

Rail carriers no longer enjoy the dominant role they once played in the national transportation system... intermodal competition pervades the transportation markets in which railroads participate. It is clear that exceptions to the competitive norm are less a consequence of technological or cost considerations than they are the result of past regulatory decisions by the ICC regarding the entry of new firms into transportation markets... Even in those instances where railroads enjoy a large share of a transportation market, they can no longer be complacent in the assurance that competition will not appear and erode their position. Potential competition from common carriers in other modes and from unregulated carriage faces the railroads in all markets...
The Staggers Rail Act of 1980\textsuperscript{122} further relaxed the regulatory reins. Among other provisions, the Act reduced certificate requirements for new line construction and eased exit and entry requirements.\textsuperscript{123} Also important were provisions allowing greater rate flexibility. Rate increases can become effective upon twenty days notice, with ten days notice required of decreases.\textsuperscript{124} Perhaps the most significant development was that railroads were relieved from the burden of subsidizing some freight with revenue from other traffic.\textsuperscript{125} Equally important, the railroads were finally permitted to enter into contracts with shippers,\textsuperscript{126} enabling them to obtain long-term commitments and revenues.

Neither the 4R Act nor the Staggers Act deregulated the railroad industry. Railroad lawyers must still battle the ICC and each other in lengthy, onerous battles over what is a “fair” rate. But the reins have been loosened and the railroads now have some freedom to regain financial stability. The railroads will have to wait several more years for results, unlike the airline industry where the tangible benefits of a more complete process of deregulation are now being felt. While deregulation initiatives have been predictably modest, so have the results. But even now the outlook is more promising. As one scholar has recently observed since passage of the Staggers Act: “[F]or the time being railroads are doing relatively well financially. And the railroads probably couldn’t do any worse under the Staggers Act and partial deregulation than they

\footnotesize{a consequence, rail market dominance can be considered the exception rather than the rule in virtually every market.}

\textit{Id. at 223.}

\textsuperscript{121} 49 U.S.C. § 10727 (1982). One student scholar has opined:

Demand sensitive pricing was premised on the assumption that transportation costs would be a primary factor in determining when grain would be shipped. However, that assumption was incorrect. Had Congress examined motor carrier price fluctuations, it would have realized the ineffectiveness of demand sensitive pricing. More importantly, the remedy did not address the underlying problem of competition with exempt motor carriers. During slack demand, grain transportation was provided by exempt motor carriers who effectively priced against the rail rate.

\textit{Note, supra note 119, at 306.}

\textsuperscript{122} Pub. L. No. 96-448, 94 Stat. 1895 (current version at 49 U.S.C. § 10101a (1982)).

\textsuperscript{123} \textit{Id.} § 10901(a). \textit{See generally} discussion in Note, \textit{supra} note 119, at 308-10.

\textsuperscript{124} 49 U.S.C. § 10762(c)(3).

\textsuperscript{125} The notion that railroads should be forced to subsidize some freight with revenue from other traffic was a favorite of the regulators. Although always based on a myopic view of the “public interest,” it was based on a common fallacy. The results, of course, were predictable: railroad rates were uncompetitive where the rates were too high, thus causing a loss of business and revenues. Where the rates were subsidized and too low, the railroads had a tremendous incentive to abandon the route. For a study of the tragedy of these abandonments, see \textit{RAILROAD REVITALIZATION, supra} note 70, at 86. As always, a policy by regulators to promote the “public interest” instead makes a mockery of it.

\textsuperscript{126} 49 U.S.C. § 10713. Even before enactment of this provision, the ICC had reviewed its administrative policy against contract rates. \textit{See Change of Policy, R.R. Contract Rates, 361 I.C.C. 205 (1979).}
did when every rate and schedule was subject to ICC scrutiny."'

IV. MOTOR CARRIER REGULATION: THE WRONG WAR AT THE WRONG TIME

The motor carrier industry superbly illustrates how regulation accomplishes the political transfer of wealth. The experience of trucking regulation also provides a striking example of the economic and social harm which results when classical regulation is imposed on a competitive industry. Unlike the railroad industry, where relatively high barriers to entry and industry concentration could be used to rationalize regulation, the trucking industry was an industry closely approaching true competition. At the time of the passage of the Motor Carrier Act of 1935, only 18,000 out of 90,000 motor carrier "grandfather" applications were granted. Entry control was further tightened, until by 1977 the number had been reduced to but 15,000. Regulation had done its work well. Even this latter figure is misleading, for under regulation, there had been tremendous concentration in the industry. In 1972 the top eight firms had seventeen percent of the trucking business, and a quarter of all income.

The railroads, of course, wholeheartedly supported regulation of the

127. Thoms, supra note 58, at 218.
128. Peltzman, supra note 17, at 215.
129. See Allen & Hymson, The Costs and Benefits of Surface Transport Regulation: Another View, in REGULATION OF ENTRY AND PRICING IN TRUCK TRANSPORTATION 93 (P. MacAvoy & J. Snow eds. 1977) [hereinafter cited as FORD PAPERS]. The study concludes that "the vast majority of economists who have looked at this issue have concluded that the net social cost of ICC regulation is truly substantial." Id. at 115. Professor Thomas G. Moore's estimates of ICC regulation, which showed an economic loss of between $6.5 billion and $15.2 billion, were critically examined by the ICC Bureau of Economics. The Bureau also estimated the social costs at no more than $1.7 billion. Bureau of Economics, ICC, A Cost and Benefit Evaluation of Surface Transport Regulation, in FORD PAPERS, supra, at 47. See also Winston, The Welfare Effects of ICC Rate Regulation Revisited, 12 BELL. J. ECON. & MGMT. SCI. 232 (1981); Davis, Surface Transportation Regulation—A Succinct Analysis, I.C.C. PRAC. J. 55, 62 (1979) (estimating costs of regulation in terms of resource misallocation as three billion dollars annually).
133. A. FRIEDLAEENDER, supra note 1, at 112.
134. Snow, supra note 132, at 19.
135. Id. at 20.
motor carriers. The ICC welcomed this support, finding that intermodal competition between the rail and motor carrier industries was being "conducted under conditions of inequality, particularly in regard to regulation." It apparently did not occur to the railroads and the ICC to simply loosen the regulatory stranglehold on rail. Rather, it was assumed that if the railroads had to suffer the incubus of regulation, the imposition of equal burdens on motor carriers would make intermodal competition more "fair."

Before regulation could begin, a rationale had to be found. Although the "natural monopoly" rationale obviously didn't apply in an industry where 90,000 carriers were clamoring for admittance, an early attempt was made to put forward this argument. Even the ICC had trouble swallowing this.

One 1934 study made the following observation:

There are thousands of little operators, with very few trucks or even a single truck . . . . As yet there are comparatively few well-organized, large scale operations, and these are small when judged by rail standards . . . . It has been and is easy to enter the business, especially on a contract or private business, and may require little expenditure elsewhere. Hardly a description from an Adam Smith handbook for a theoretical industry. This was the description of the actual state of trucking in 1934 by the same federal report which advocated regulation.

Obviously a rationale other than "monopoly regulation" had to be found in order to justify protectionism and entry control in the trucking industry. A rationale was finally found in what was euphemistically called "excess capacity." A 1928 ICC report expressed concern over carri-

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In 1935 the railroads were fully regulated and were recognized to be a sick industry. Many argued it was unfair to burden the railroads with comprehensive regulation while turning the trucks loose to take the cream of their commerce and then expect them to offer comparable service . . . . It was obviously unfair to continue to regulate rail carriers without enacting a similar system of regulation for motor carriers of passengers.  
Id. at 97.


138. Commissioner Woodlock's concurring opinion in Motor Bus and Motor Truck Operation, 140 I.C.C. 685 (1928) stated:  
Transportation by motor bus and motor truck does not necessarily depend upon monopolistic or semimonopolistic organization or performance. It is manifest that at the present time these services are much more largely of a competitive than of a monopolistic nature. For that reason the need for regulation, except in so far as concerns the public safety, is not wholly clear.  
Id. at 750.

139. REPORT, supra note 130, at 893.

140. Hearings on S. 1629, S. 1632, and S. 1635 before the Senate Comm. on Interstate Commerce, 74th Cong., 1 Sess. 78 (1935). Commissioner Eastman stated: "The most important thing . . . . is the prevention of an oversupply of transportation."  
Id.
ers which were cutting fares below compensatory levels and otherwise engaging in "reprehensible" practices. (After all, what could be more "reprehensible" than reducing rates to consumers and shippers? The report never explained, however, how all these undercapitalized carriers managed to survive so long while charging fares "below compensatory levels.) What they meant, of course, as did all advocates of the "excess capacity" theory, was that the rates of these "reprehensible" firms were lower than that of many of their competitors. The regulators' solution was as predictable as it was simple: exclude by law all those whose rates were, in the ICC's opinion, "noncompensatory." Thus, what the market inexplicably failed to do through business failures, regulation could accomplish by fiat—or so theory went. The shippers were even condemned for "contributing" to the carriers' reprehensible acts. The 1937 Report of the Federal Coordinator of Transportation noted with obvious disgust that some shippers had "done little to discourage, and much to encourage, the cutting of rates," and, with apparent horror, noted that some had even "shopped around."142 (Fortunately, consumers who "shopped around" were spared the immediate wrath of the report.)

Like the emperor's new clothes, most of the interest groups could not bring themselves to acknowledge the true motivation for deregulation: to control entry, and to eliminate competition for the benefit of those who, by political means, became one of the "elite"—those who would be permitted to enter the industry. Thus, those who had failed to successfully compete by economic efficiency were able to accomplish the same result by political means and the use of effective advocates before the ICC. There were a few, however, who saw the real purpose behind regulation of trucking. Congressman George Huddleston spoke for 115 members who voted against the Carrier Act: "The proponents of the bill admitted candidly that its main purpose was to give a monopoly, to eliminate competition."143 Senator Wheeling stated: [I]t will prevent that competition that brings lower rates and better service to the people."144

These protests, and those of consumer advocates' were ignored, despite the numerous economic studies which revealed the inequities and inefficiencies wrought by regulation.145 Meanwhile, those given entry privileges soon realized that their oligopoly rights had a tremendous windfall value. Indeed, the total value of operating "certificates" has been es-

141. See Motor Bus and Motor Truck Operation, supra note 137, at 702.
142. REPORT, supra note 130, at 893.
143. H.R. REP. No. 783, 71st Cong., 2nd Sess. 16-17 (1930).
144. Id. at 96.
timated to be on the order of three to four billion dollars.\textsuperscript{146} The windfall in certificate value reaped by those lucky enough to obtain oligopoly rights was at the expense of potential competitors who were denied entry, as well as at the expense of shippers and consumers.\textsuperscript{147}

The American Trucking Association has noted that "virtually the only way for (a relatively small carrier) to obtain additional operating authorities is to buy them from other motor carriers."\textsuperscript{148} Even more indicative of regulatory distortions of the market is the fact that amounts paid for operating authorities in 1972 were approximately fifteen to twenty percent of the annual revenues produced by those authorities, according to the ATA.\textsuperscript{149} Predictably, however, those who reaped such windfalls used other arguments to support regulation. Exhaustive studies have now revealed the inaccuracy and the hypocrisy of the myths perpetuated to oppose regulatory reform: that it would (a) cause "market chaos"; (b) lead to "monopoly"; (c) cause price discrimination and "predatory pricing"; (d) decrease service to small communities; and (e) adversely impact railroads.\textsuperscript{150}

It is often difficult to determine empirically what differences there would have been had there been no trucking regulation from 1935-1980. Fortunately, several controlled studies are available. During the 1950's, for example, fresh and frozen poultry were declared exempt under the Interstate Commerce Act. As a result, rates declined significantly more for fresh and frozen poultry than for frozen fruits and vegetables.\textsuperscript{151}

A study of trucking rates in countries with little or no regulation showed rates there to be 43\% lower than in regulated countries such as

\textsuperscript{147} As a 1976 study found:

The best evidence of the widespread existence of market power caused by the ICC's restrictive entry policy is that operating rights have market value. They only have value because they have been artificially restricted. The value of rights consists of the capitalized value of the excess over normal competitive returns... Thus the policy operates to the detriment of the public and to the benefit of the original holders of these rights.


\textsuperscript{148} \textit{id.} at 23. A good example of the injustice of the certificate system was seen in Shaffer Transp. Co. v. United States, 355 U.S. 83 (1957), discussed in C. Fulda, \textit{COMPETITION IN THE REGULATED INDUSTRIES: TRANSPORTATION} 73-79 (1961). The W.A. Shaffer Co. sought a certificate, offering to provide faster and cheaper service between South Dakota and points east. The ICC refused to grant the certificate on grounds that even though present service was slow and expensive, it was "adequate." Six years later, the courts reversed the ICC, but by that time Shaffer had gone out of business.


\textsuperscript{150} \textit{Snow}, in \textit{FORD PAPERS}, \textit{supra} note 129, at 35-43.

the U.S. and West Germany.\textsuperscript{152} A study by James Sloss showed that trucking rates in Canada were 9 to 12\% lower in provinces without regulation than in provinces with regulation.\textsuperscript{153} A recent study of Motor Carrier Deregulation in Florida, by Richard Beilock and James Freeman, revealed that most shippers felt that rates had been lowered due to deregulation of trucking in that state. As a result, only 10\% of the shippers and private carriers preferred regulation. This finding was expected since both shippers and consumers had benefited from the rate reductions. The startling finding of the study, however, was that only 47\% of the carriers preferred regulation. A large percentage of carriers felt they could operate just as well under deregulation as under regulation. Apparently for these shippers, the benefits of deregulation even outweighed the advantages of oligopoly rights.\textsuperscript{154}

The explanation for the higher rates under regulation is now clear: "Because of restrictions on entry and other regulatory controls, they regulate as a cartel, exacting monopoly profits from shippers."\textsuperscript{155} This is perhaps the supreme irony of regulation: a competitive industry has been transformed into a monopoly by the very regulation that was originally rationalized as a means of preventing monopoly. How can this be the case with thousands of carriers still operating? Even aside from the industry concentration in a few firms, the answer is simple: regulation permits all carriers to act in concert, to benefit and obtain oligopoly profits from a rate structure applicable to the industry as a whole rather than to a particular firm. The economic result is the same as if there were but one firm in the industry. It is not surprising, therefore, that operating oligopoly rights fetch such a high price, nor, as one scholar notes, that "the irrational nature of the regulatory scheme has spawned a vigorous illegal truck industry, able to maintain profitable operations against an inefficient and cartelized regulated truck industry."\textsuperscript{156}

In short, regulation has been the means for a political transfer of wealth from consumers, shippers and non-union workers to a cartel and to certain privileged workers. Cartel gains went to the Teamsters; the rate structure of the ICC reinforces this result.\textsuperscript{157} Professor Thoms has ob-

\begin{itemize}
\item \textsuperscript{152} T. Moore, TRUCKING REGULATION: LESSONS FROM EUROPE 141 (1976).
\item \textsuperscript{153} Sloss, Regulation of Motor Freight Transportation: A Quantitative Evaluation of Policy, 1 BELL J. ECON. & MGMT. SCI. 32 (1970). For an unbiased study, see Chow, Economic Regulation of Motor Freight in Foreign Countries, 47 I.C.C. PRAC. J. 44 (1979).
\item \textsuperscript{154} Beilock & Freeman, Motor Carrier Regulation in Florida, 14 GROWTH & CHANGE 30 (1983).
\item \textsuperscript{155} Jones, supra note 18, at 317.
\item \textsuperscript{156} Id.
\item \textsuperscript{157} As Moore explains:
Management will be less unwilling to agree to higher wages knowing that the ICC will not only permit higher rates but enforce them on any nonunionized competition. More-
\end{itemize}
served that "unions . . . prefer an oligopolistic industry with excess prof-
its which [can] be recaptured through collective bargaining."\textsuperscript{158}

The fault, however, does not lie with the unions, which seek legiti-
mate social redress for their workers and serve to counterbalance the
power of the artificially created trucking cartel. The fault is with the sys-
tem of regulation that, by granting rate increases, actually \textit{rewards} a firm
for its failure to hold down costs. A firm which \textit{can} cut costs is punished
by being forbidden from reaping a competitive advantage by lowering
rates. This perversion of normal market incentives explains the staggering
differences in efficiency in regulated and unregulated trucking indus-
tries. Since costs of individual firms differ, even the seductive notion of
"equal pricing" has perversely caused true discriminatory pricing, since
some shippers are charged more than the actual cost of the traffic, and
some are charged less.

It is beyond the scope of this article to set forth all the harm and
inefficiencies caused by trucking regulation; they may be summarized,
however, as follows:

1. Rates which are too high,\textsuperscript{159} irrational,\textsuperscript{160} and
discriminatory.\textsuperscript{161}

\begin{flushright}
\textit{Moore, The Beneficiaries of Trucking Regulation, 21 J.L. \\ 
& Econ. 327, 331 (1978).}
\end{flushright}

\textsuperscript{159} \textit{Snow, in Ford Papers, supra note 129, at 8. "Rates are too high partly because
unnecessary regulatory restrictions cause carriers to operate less efficiently than they would
without the restrictions. Regulation causes carriers to use circuitous routes . . . ." Id. See also S.
Breyer, \textit{supra} note 30, at 234 ("certificates may limit the commodities that a carrier can trans-
port between two points. This means that a truck must remain idle, rather than carry commodi-
ties for which it is not certificated."). (footnote omitted).}

\textsuperscript{160} \textit{Snow, in Ford Papers, supra note 129, at 14.}

Because rates, especially class rates, are not tied to the actual costs of the service
provided, rates are frequently irrational. . . . A study of rates in the Rocky Mountain
region found that rates for a given commodity class are often higher for shorter dis-
tances than they are for longer distances in the same direction or even traveling over
the same route. . . . [R]egulated rates are frequently irrational, capricious, and inconsist-
ent because they are determined by regulation, not by competition. . . . 
[C]ompetitive discipline would force rates into a more consistent and rational pattern.
\textit{Id.} at 14-15.

\textsuperscript{161} \textit{Id.} at 15-18. "[I]n many cases the costs are not the same. When costs differ, the princi-
ple of equal rates results in actual discrimination. Some shippers are charged more than the
cost of their traffic and some are charged less. The discrimination is irreproachable and it leads to
economic inefficiencies". \textit{Id.} at 15.
2. Social and economic inequities.\textsuperscript{162}
3. Inferior service to small communities.\textsuperscript{163}
4. Waste and inefficiency.\textsuperscript{164}

Reform, however, is being vigorously resisted by carriers, who see in deregulation the diminution in value of their inherited or purchased oligopoly rights. The result has been a compromise between those who favored deregulation as a means of improving efficiency and lowering rates for the consumer, and those opposed, fearful of losing protection and oligopoly rights. Thus the Motor Carrier Act, while correcting many of the grossest regulatory abuses, nevertheless extended the basic regulatory scheme.

On the one hand, the Act shifted the burden of proof of "useful public purpose" from the applicant to a protestant,\textsuperscript{165} allowed the issuance of new "master's certificates" in certain narrowly designated markets,\textsuperscript{166} expanded the number of commodities exempt from regulation,\textsuperscript{167} allowed carriers to give shippers credit for their own pickup without fear of being accused of "discriminatory pricing,"\textsuperscript{168} created a ten percent "zone of reasonableness" in setting rates,\textsuperscript{169} and curtailed "rate bureaus."\textsuperscript{170} On

\begin{figure}
\centering
\includegraphics[width=\textwidth]{figure1.png}
\caption{Graphical representation of the text content.}
\end{figure}

Where rate distortions of this sort occur, shippers make adjustments which are often uneconomic.\ldots For high valued, high rated items, it may in fact be cheaper to switch to the traditionally more expensive alternatives such as air freight.\ldots Where these decisions are made simply because rates are distorted, and not for service reasons, shippers, motor common carriers, and ultimately consumers are needlessly harmed.

\textit{Id.} at 18.

\textsuperscript{162} "The restrictions on entry into the regulated motor carrier industry inevitably result in gross inequities.\ldots Persons who happened to be in the motor carrier business in the mid-1930s have been awarded, free of charge, valuable property rights.\ldots"\textit{ Id.} at 23. Other individuals, no less capable, have been prevented from engaging in the business or occupation of their choice.

\textsuperscript{163} \textit{Id.} at 27.

The DOT has analyzed the rural service issue and has concluded that, far from providing a justification for the current restrictive regulatory policy, the present system has impaired rural motor carrier service. Rural towns would be much better served by a regulatory program which placed greater reliance on competitive market forces and which eliminated unnecessary and wasteful operating restrictions.

\textit{Id.}

\textsuperscript{164} See A. FRIEDLAENDER, \textit{supra} note 1, at 74-75. ("[T]he total welfare loss arising from value of service pricing can be estimated at approximately $300 to $400 million annually."). See also Jones, supra note 26:

The nature of both the exemptions and the regulatory requirements has created a level of inefficiency condemned by numerous observers. The motor vehicle—which has as its major virtue an intrinsic capacity for flexibility—is locked into narrowly defined routes, carrying restricted commodities, and often operating empty or at less than full capacity.

\textit{Id.} at 317 (footnotes omitted).

\textsuperscript{165} 49 U.S.C. § 10922(b)(1) (1982); Thoms, \textit{supra} note 158, at 76.
\textsuperscript{166} Thoms, \textit{supra} note 158, at 76.
\textsuperscript{167} \textit{Id.} at 77; 49 U.S.C. § 10526(a) (1982).
\textsuperscript{169} Thoms, \textit{supra} note 158, at 77; 49 U.S.C. § 10708(d) (1982).
the other hand, new applicants must still submit to a cumbersome hearing process before being allowed entry or the right to charge rates outside the ten percent "zone of reasonableness." Nevertheless, the Act is a step in the right direction, and it is probably only a matter of time before the interests of consumers and the public force a further loosening of the regulatory grip on what is potentially the most competitive mode of transportation.

V. AIRLINE DEREGULATION: CASE STUDY IN REFORM

A. UNFRIENDLY SKIES—"YE SHALL NOT ENTER HERE": HISTORICAL PERSPECTIVES ON AIRLINE REGULATION (1938-1976)

Under legal precedents established since the early days of railroad regulation, regulations became applicable in industries affecting the "public interests." As long as airplanes were rickety, unreliable, gas-wheezing flying machines, they were not thought of in the context of the "public interest." As early as 1916, however, funds were appropriated for airmail service. U.S. Mail Service came under Post Office control in 1918. The Contract Air Mail Act of 1925 was the first major legislation affecting airlines. Other legislation followed, further refining the air service system. An amendment to the Black-McKellan Act of 1934 removed responsibility for airmail contract rate setting to the ICC.

The age of airline regulation began in earnest in 1938 with the Civil Aeronautics Act. From the beginning, regulation was rigid. The Act gave the Civil Aeronautics Board (CAB) the power to control entry by allowing it to issue certificates of "public convenience or necessity," and suspending or establishing "just and reasonable" rates. For the next forty years, the CAB wielded its power with a heavy hand: its chief accomplishment seems to have been preventing a single major trunk carrier from entering the industry during its reign. Professor Dempsey has observed: "[T]he excessively rigid regulatory scheme established by the Civil Aeronautics Board . . . between 1938 and 1975, allowed the creation of an effective oligopoly composed of the five largest trunk line carriers."  

173. See id.
174. See id. at 14.
176. Ch. 601, 52 Stat. 973 (1938); see generally Dempsey, supra note 4, at 91.
177. See Dempsey, supra note 4, at 93.
178. Dempsey, supra note 2, at 2 n.1.
Between 1950 and 1974, seventy nine firms sought entry. Not one received it. As Dempsey has noted: "As a result of these policies, the big four in 1938—United, American, Eastern, and Trans World Airlines—are the big four today." This fact is even more startling when one realizes that the industry itself has expanded by 23,800 percentage points during the same period.

The political and economic motives for an industry seeking regulation have been documented in the railroad and motor carrier industries. The advantages of artificial barriers to entry were no less for the original trunk carriers in 1938. It was not until the late 1950's that the "public interest" mythology began to be critically reexamined. Between 1960 and 1975, "[t]he scholarly view of the regulatory process changed from one of control of private behavior for the public benefit to one of use of governmental powers for private or sectional gain."

In 1976, Roger Noll described public interest theories as "traditional," and "no longer widely shared." Jean Luc Migué in 1977 postulated: "It seems fair to say that among economists the most widely accepted theory of government regulation is that, as a rule, regulation is acquired by the industry regulated and is designed and operated primarily for its benefit." A. Downs had revealed, as early as 1957, a government run by individuals trying to maximize a private, rather than public, utility function.

The "public interest" mythology fell hard, however. By the time of the first attempts at reform, the special interest groups, which had bene-

179. Dempsey, supra note 4, at 115.
180. Id.
181. S. Breyer, supra note 30, at 206.
182. Levine, supra note 92, at 180. Levine continues:
This pattern emerges frequently enough to inspire speculation about the "true" sources of regulation and about the "true" motives of regulators. While no single explanation gained unanimous acceptance, a kind of "cluster consensus" appeared. This consensus characterized regulation as a device used by relatively small subgroups of the general population, either private corporations or geographic or occupational groups, to produce results favorable to them which would not be produced by the market. The regulatory services provided were variously described as organization of a cartel, wealth transfers as a form of "taxation," enshrinement of capitalistic class interests, or preservation of congressional and bureaucratic power. Of course, all gains, whether from regulation or the market, are in a sense realized by private human beings. The operational significance of this view of regulation is that government processes are used by organized subgroups of the population to enforce inefficient arrangements which transfer wealth or power to them.

Id.
185. See generally A. DOWNS, AN ECONOMIC THEORY OF DEMOCRACY (1975).
fited from the airlines' oligopoly power created by regulation, posited every reason to resist reform, predicting that deregulation would bring industry ill-health, deterioration of service to small communities, reduction of safety, and even, without shame, the danger of industry concentration.\textsuperscript{186} So far these prognosticators are batting .000: not one prediction has come true.\textsuperscript{187} Fortunately, scholarly criticism was soon translated into political reform. Thirteen years after President Kennedy called for "greater reliance on the forces of competition,"\textsuperscript{188} the U.S. Senate Judiciary Subcommittee on the CAB (The Kennedy Hearings) began oversight hearings. At the hearings, the tragedy of thirty five years of regulation was exposed to public view: studies revealed that fares were 40-100\% higher than would have been the case under deregulation.\textsuperscript{189} It was revealed that airfares in intrastate areas not regulated by the CAB were 50-70\% of the CAB regulated fares for the same distances.\textsuperscript{190} In response to a 1975 Presidential call for regulatory reform in the airline industry, an exhaustive study of the history of airline regulation summed up the fiasco of airline regulation.\textsuperscript{191}

To its credit, the CAB in 1976-77 took the initiative in airline deregulation, easing entry and rate requirements. Breaking a tradition of bureau-

\textsuperscript{186} See, e.g., TRANSPORTATION LAWYERS ASSOCIATION, STATE REGULATORY COMMITTEE REPORT (1983); Forest, supra note 19; Duffy (President of Airline Pilots Association), Airline Deregulation: More Harm Than Good, Denver Post, Dec. 31, 1983, at B2, col. 2.

\textsuperscript{187} See supra notes 3 and 4.

\textsuperscript{188} See supra note 1.


\textsuperscript{190} STAFF OF SENATE SUBCOMM. ON ADMINISTRATIVE PRACTICE AND PROCEDURE OF THE SENATE COMM. ON THE JUDICIARY, 94TH CONG., 1ST SESS., REPORT ON CAB PRACTICES AND PROCEDURES 41 (Comm. Print 1975).

\textsuperscript{191} The present system of airline regulation is seriously deficient. Its most serious deficiency is that it causes air fares to be considerably higher than they would be otherwise. It also results in a serious misallocation of resources, discourages innovations in service, denies consumers the range of price and service options which they would prefer, and creates a chronic tendency towards excess capacity in the industry.

The Civil Aeronautics Board (CAB) has historically used its broad powers to forbid competitive pricing and lower fares. Unable to compete on the basis of price, carriers have been forced into costly service competition, and the costs of these services have been passed on to the consumer. On review of the evidence, one is forced to conclude that the present regulatory system is hindering, not advancing, the original statutory objectives of "adequate, economical and efficient service by air carriers at reasonable charges." The present regulatory system has become a major obstacle to the provision of air service at the lowest cost consistent with the furnishing of such service. Ironically, airline profit levels are not increased by this regulatory system, and they may indeed be made more volatile than otherwise.

cratic inflexibility and inertia,\textsuperscript{192} the Board paved the way for the Airline Deregulation Act of 1978.\textsuperscript{193} This new Act, which placed "maximum reliance on competitive market forces,"\textsuperscript{194} further eased entry restrictions, even allowing for some automatic entry, and established a means for unregulated price adjustments.\textsuperscript{195} For the first time in forty years, the success or failure of an airline would depend upon its ability to provide the best service at the best price to consumers—not on its political influence or legal expertise before CAB.

\textbf{B. \textit{Industry Health—Turning the Tide}}

In the years after regulation, the airline industry proved to be less profitable than firms in the unregulated economy.\textsuperscript{196} On the eve of deregulation, former CAB Chairman John Bobson observed that "[o]nly three times in the past 26 years, and never in the past decade, has the industry earned the . . . allowable return on investment."\textsuperscript{197} Although there were brief periods of profitability immediately after the introduction of new technologies,\textsuperscript{198} the long periods of low profitability came despite the fact that regulation had given the airlines virtually everything they had asked for.\textsuperscript{199}

Under CAB policy, a few carriers who were awarded lucrative routes, prospered, while inefficient carriers were kept afloat by enforcement of rates based on the average costs of the industry.\textsuperscript{200} With absolute security, the privileged trunks had no incentive to be efficient and were content with their oligopoly profits. With no incentive to reduce costs the airlines engaged in wasteful and extravagant service competition, offering such frills as gourmet meals and Polynesian pubs,\textsuperscript{201} and culminating in the

\begin{itemize}
\item \textsuperscript{192} See, e.g., Dempsey, supra note 4, at 123 nn.135-39, 123-24.
\item \textsuperscript{194} P. Biederman, supra note 172, at 80.
\item \textsuperscript{195} Id. at 81.
\item \textsuperscript{196} Office of Economic Analysis, Civil Aeronautics Board, Competition and the Airlines: An Evaluation of Deregulation 8 (1982) [hereinafter cited as CAB Report].
\item \textsuperscript{197} Traffic World, July 18, 1977, at 14.
\item \textsuperscript{198} CAB Report, supra note 196, at 8.
\item \textsuperscript{199} See C. Kelly, The Sky’s the Limit: The History of the Airlines (1963).
\item The Civil Aeronautics Act of 1938 gave the airlines almost all that they desired. The routes of the then existing . . . airlines were protected, and the outside competition was practically eliminated. Furthermore, a generous subsidy was provided, in effect a blank check . . . . Unless a carrier could be shown to be willfully fraudulent or inefficient in his management, he no longer had to fear losses. The government stood ready not only to make up any deficit, but also to insure a return on his investment. All in all, the . . . Act seemed to be a bonanza for the airlines, and the major figures in the industry greeted its passage enthusiastically.
\item Id. at 102.
\item \textsuperscript{200} See M. Lazarus, Airline Pricing Deregulation and United’s Fare Policies (1983).
\item \textsuperscript{201} S. Breyer, supra note 30, at 200.
\end{itemize}
so-called "liquor wars" in which airlines competed by offering free liquor to customers. Deprived of the right to compete by price, some airlines were reduced to competing by offering more flights than were actually dictated by market demand, resulting in costly excess capacity.\textsuperscript{202} Since the costs of such extravagances as liquor wars and Polynesian pubs were nevertheless considered in determining "average costs," and thus a factor in fixing industry-wide fares, there was every incentive to be extravagant rather than efficient. With nothing to fear from a competitor who might compete by reducing price, the airlines grew fat in their protected environment. Thus, despite studies showing that whenever passengers had the choice of fuller planes at lower prices, or better schedules but more expensive flights, they chose the former, the passenger was not given this choice.\textsuperscript{203}

Nevertheless, the airlines had ample opportunity to bring their profits up to manufacturing industry standards. In 1938, passenger fares were set at approximately the rates for pullman travel on the trains.\textsuperscript{204} After World War II, however, the industry introduced the DC-6 and Lockheed Constellation, which had drastically greater load capacity and cruising speeds. In a competitive environment such opportunities to cut costs would have resulted in drastically lower fares. With no price competition to fear, however, average fares declined far less than the reduction in costs.\textsuperscript{205}

An even more dramatic opportunity to reduce costs per passenger mile came in the late 1950's and 1960's with the introduction of jets, which were far more efficient than the older propeller driven planes. Again, the CAB refused to allow a proportionate realignment of fares to reflect the lower costs, although a few discount fares were finally permitted.\textsuperscript{206} Between 1960 and 1969, the trunks' cost per seat mile was reduced by 21%; average fares, however, declined only 7%.\textsuperscript{207} Such a result would have been impossible in a competitive market, since any carrier reducing the fares by over 7% would have taken business from the other carriers, consequently forcing all fares down.

Since technological breakthroughs were so drastically reducing costs, while prices were kept artificially high by CAB price fixing policies, the question arises as to why the airlines did not reap a bonanza of prof-

\textsuperscript{202} Id.
\textsuperscript{203} S. Breyer, supra note 30, at 205. One economist has calculated that fare/service combination was suitable only for travelers whose time was worth over $60,000 per year. Travelers therefore paid half a billion dollars more than necessary in 1969 alone. Prior to 1975, overcharges ranged up to $3.5 billion annually. Id.
\textsuperscript{204} CAB Report, supra note 196, at 65.
\textsuperscript{205} Id.
\textsuperscript{206} Id. at 66.
\textsuperscript{207} Id. at 67.
its. There are several answers: 1) CAB policy encouraged the dissipation of revenue by service competition (e.g., "liquor wars");\textsuperscript{208} 2) the airlines had no incentive to take advantage of their opportunities to reduce costs, since increased efficiency would only make their case more difficult when seeking fare increases from the CAB; 3) the CAB did not allow airlines to take advantage of their greater load capacity by use of peak load fares;\textsuperscript{209} 4) CAB policy created an environment in which submission to union pay demands was a path of less resistance than fighting for lower consumer fares.\textsuperscript{210}

The latter-most factor became a dominant one during regulation. Pilots' pay was originally based on a formula incorporating an hourly rate and a mileage rate.\textsuperscript{211} When the Strato-liner increased productivity substantially, however, the hourly rate was increased. This change "established a precedent: as faster aircraft were introduced, pilots' hourly rates [were] increased."\textsuperscript{212} When jets were introduced, productivity gains were again translated into higher hourly rates and reduced flying time. Average flying hours per month declined 8 hours during the 1950's, from 65 in 1955 to 50 hours in 1975. Since there were no competitive pressures on airlines to resist such pay increases and flight hour reductions, the net result was that airline employees were paid substantially more than their counterparts in deregulated industries. For example, typists were paid 41% more than their counterparts in deregulated industries, computer operators 38%, air freight agents 58%, and even janitors received 82% more than their deregulated counterparts.\textsuperscript{213}

The fault for this injustice lies not with the unions, of course, which only seek to protect the interests of its workers, but with the system which provides the wrong incentives. Under deregulation, airlines with strong unions find they must compete with airlines which pay competitive wages. Workers previously excluded from airline employment can finally find work at market wages in a deregulated industry. The previous power structure is being drastically altered as airlines such as Continental are forced to reduce labor costs in order to compete with airlines paying fair market wages.\textsuperscript{214}

While these developments under deregulation obviously affect the power of unions to reap the benefits of productivity increases, it also has

\begin{footnotes}
\item[208] See M. Lazarus, supra note 200.
\item[209] CAB Report, supra note 196, at 69.
\item[211] CAB Report, supra note 196, at 114.
\item[212] Id. at 114.
\item[213] Id. at 117-23.
\end{footnotes}
advantages for the unions. Far from creating an environment for "union-busting," deregulation creates unique opportunities for unions to obtain a voice in management and in their own future. In the deregulatory scheme of things, union and worker ownership and responsibility is a healthy trend. In such an environment, the interests of the firm and the workers coincide rather than clash, inuring to the benefit of both the public and the industry.

In light of the mediocre airline profit history under regulation, it was not surprising that in the very first year of deregulation, operating profits of the airline industry increased fifty percent over the previous year. Air fares declined for the first time in twelve years and air traffic in revenue passenger miles expanded faster than it had in ten years. Load factors in 1978 jumped five points and exceeded sixty percent for the first time since 1959.215

The recession which began in 1979 affected the airline industry in the same manner it affected all industries. Fuel prices increased by 105% in one twelve month period alone (1979).216 The PATCO strike further curtailed operations and slowed the progress of deregulation.217 While airline profits slumped during the recession, as did other industries in the economy, fares increased at a rate lower than the inflation rate.218 Fuel cost increases, rather than being automatically passed on in fare increases, were absorbed by a newly emerging competitive industry. By 1983, as the recession ended, the airlines began to show record profits.

In early 1984, the Air Transport Association’s chief economist estimated a half billion dollar operating industry profit for 1983, including a fourth quarter profit of between $300 and 400 million.219 Passenger traffic in 1983 came close to the record of 317 million passengers set in 1979.220

Although few had doubted the consumer benefits of deregulation, 1983 industry profits showed that the industry also benefited. Even during the depth of the recession, when unemployment increased in other sectors of the economy, employment increased dramatically in the airline industry. From 1977 to 1979, the number of employees increased from 265,777 to 294,930, with a 7.7% increase in employment in 1979 alone. The most dramatic increase in employment occurred in the local service industry, where employment increased 11.7% in 1978 and 16.3% in

216. HARVARD PROJECT, supra note 3, at 163.
218. Id. at 73.
220. USA Today, Jan. 9, 1984, at B-1.
1979. From 1977 to 1982, local service employment increased from 31,402 to 44,559.221 Thus, the explosion in passenger miles stimulated by deregulation was also serving the interests of the working person. What the economists and theoreticians had predicted for so long was now happening.

C. INDUSTRY CONCENTRATION

It has been argued that airline deregulation will result in industry concentration. In 1982, one commentator predicted that "within five to seven years you will have no more than five . . . trunk airlines."222 The theory behind such predictions is usually simplistic: in a competitive industry, the more efficient airlines will take advantage of their efficiency and economies of scale, and engage in "predatory" pricing in the manner of a Standard Oil under John D. Rockefeller. The inefficient airlines will then cease to exist, and a substantial monopoly will result which can then reap oligopoly profits. These predictions, however, originate not from economists but from those who have an axe to grind,223 and are clearly misdirected. Exhaustive studies have revealed that it was regulation which provided the only hope for creation of an oligopolistic industry.224

These predictions reveal how quickly memories fade. (The feared scenario of five major trunk carriers was one which actually existed under regulation.) However, the predictions also rest on two false assumptions: 1) barriers to entry are relatively high, and 2) there are significant economies of scale and decreasing costs. Economic barriers to entry are relatively low in the airline industry.225 The most important barriers have been legal barriers enforced by the CAB. Economic barriers pale by comparison. Even such upstarts as People's Express have no trouble leasing jumbo 747's to start up operations.226 The explosion in the number of new airlines since deregulation reveals the economic ease of entry. By September of 1981, eleven newly formed airlines providing jet service had entered the industry.227 In addition, former intrastate and regional airlines such as Pacific Southwest Airline (PSA), Air California, and South-

221. CAB REPORT, supra note 196, at 35 (Table 1.4).
223. One notable doomsayer was Howard Putnam, Braniff's Chief Executive Officer, who probably qualified for a sour-grapes award in predicting a drastic reduction in the number of carriers in the industry. See Dempsey, supra note 5, at 345 n.52.
224. Snow, in FORD PAPERS, supra note 129, at 28.
225. See Bailey & Panzar, The Contestability of Airline Markets During the Transition to De-Regulation, LAW & CONTEMP. PROBS., Winter 1981, at 125, 129.
226. For a comprehensive review of the lower costs of such up and coming airlines as Muse, Southwest, People's Express, Capital and World, see CAB REPORT, supra note 196, at 103.
227. Id. at 125.
west Airlines have greatly expanded their operations.\footnote{id. at 124.}

Without high barriers to entry, "predatory pricing" does not become a factor. Such pricing is used when a large firm attempts to use its economies of scale to lower prices which it can absorb, but which bankrupts competitors. After the competitors go bankrupt, the large firm exercises monopoly power. Predatory pricing is irrational in an industry where exit and entry is easy. A firm hoping to practice predatory pricing must be prepared to absorb huge losses in the speculative hope of future high profits. Where firms can enter or exit the industry quickly there is little incentive to absorb huge losses. Even if a competitor or two is driven from the industry, the same or another competitor can reappear at a later time. In fact, in the present competitive environment, it is usually the predator rather than the prey that fails (e.g., Braniff Airlines). Breyer has observed that unless a predator firm is both insured of its own ability to absorb ruinous losses and protected by substantial barriers to reentry by competitors, "it is irrational for it to attempt predatory pricing."\footnote{id. at 61 (emph. added) (footnotes omitted).}

Economies of scale are relatively low in the airline industry;\footnote{id. at 61 (emph. added) (footnotes omitted).} in fact, there are significant diseconomies of scale. Small, lean airlines can often reap cost advantages unobtainable for the larger airlines.\footnote{[E]conomists have come to accept the conclusion that there are no significant economies of scale in air transport." Bailey & Panzar, supra note 225, at 126.} Economies of scale are more related to the efficiency of particular aircraft in a particular market than on total number of aircraft. In addition, small lines like People's Express can cut costs by having ticket sellers perform baggage handling chores. And, of course, small airlines are less likely to be saddled with oppressive labor contracts. For example, Southwest's pilots fly

\footnote{228. id. at 124.}
\footnote{229. S. BREYER, supra note 30, at 61.}
\footnote{In fact, \textit{regulation can make predatory pricing easier}, since it often provides the barriers to entry necessary for a potential predatory price to succeed. Furthermore, the antitrust laws make predatory pricing unlawful. Those firms suffering its consequences can bring antitrust suits and appeal to enforcement agencies.}
\footnote{Unfortunately, ordinary price competition is easily confused with predatory pricing. The former generally involves low-cost firms charging lower prices that take business from higher-cost firms; the latter involves short-term prices well below costs, set with the object of destroying competition and later recouping losses through prices well above cost. Those advocating regulation on these grounds in the transportation field may well have confused the two.}
\footnote{230. "[E]conomists have come to accept the conclusion that there are no significant economies of scale in air transport." Bailey & Panzar, supra note 225, at 126.}
\footnote{231. CAB REPORT, supra note 196, at 101. [The new airline's] lower costs are partly explained by the simplicity of their operations, partly by their lower input costs, especially wages; and partly by their no-frills service policies. In most cases, they set fares lower than the prevailing fares prior to their entry, and as a consequence, their share of industry traffic has grown to more than 8.5%. Because of their rapid growth, the influence on industry behavior goes well beyond what their market share would suggest.}
\footnote{id.}
73 hours per month compared to 43 hours for United.232 Such factors explain why in 1983, a smaller, leaner airline like US AIR could increase its revenue passenger miles by 19.2%, while an older trunk airline like United was only able to increase by 11.8%; Delta increased by 9.6%, Eastern by 8.4%, Western by 6.0%.233 These factors also explain an unmistakable trend since deregulation—the market share of the four largest trunk airlines has steadily declined, from 58.7% in 1978 to 55.8% in 1983.234 Moreover, the trend is accelerating as new competitors enter the industry. Deregulation has also resulted in the market share of all the trunk airlines declining from 97.3% in 1978 to 92% in 1983, while that of new entrants and locals more than tripled, from a total market share of 2.7% in 1978 to 8% in 1983.235 A recent study summarized the effects of deregulation on industry concentration as a replacement of the old route network by a new one arising from competitive market forces.236 It is hard to imagine industry concentration being any worse than that suffered by the industry during the days of regulation.

D. DEREGULATION AND FARES

A comparative analysis of pricing in the airline industry is difficult because of the number of independent economic factors that must be taken into account. A few such factors are the general inflation rate, particular rates of inflation (such as fuel), recessionary pressures, and technological advances. Most studies examining all these factors have concluded that regulation caused artificially high fares. Keeler’s 1972 study of coach fares revealed that fares were 45 to 84 percent higher than what the unregulated competitive fares would be.237 The 1975 Kennedy Hearings revealed that regulated fares were 40 to 100% too high, and that excess fares amounted to up to $3.5 billion.238

Comparisons of fares before and after deregulation do not tell the whole story; they are, however, a starting point. A May 1983 Air Trans-

232. id. at 10 n.9.
234. Staff of the Civil Aeronautics Board, CAB Draft Report 13 (Table 1.2) (1984) [hereinafter cited as 1984 CAB Draft Report].
235. id.
236. The market share of the trunk airlines—the group most favored by CAB regulation—has fallen rapidly since 1978. What has happened is that the air service network has become better integrated, as the airlines have moved rapidly to develop route networks that match traffic patterns. The old route network created by the CAB is unraveling, and a new network structured by competitive market forces is coming into being. Graham and Kaplan, Airline Deregulation is Working, AEI J. Gov’t & Soc., May-June 1982, at 26, 27.
238. See Kennedy Hearings, supra note 189.
port Association report revealed that the CAB Standard Industry Fare allowed for fare increases of 67% between 1978 and 1982.239 In light of staggering fuel price increases of 105% between March 1979 and March 1980 alone,240 fares would doubtless have increased dramatically during this period under regulation. Actually, fares decreased in real terms on an overall basis.241 In 1982, 80% of all coach travel was on discount fares compared with 48% in 1978.242 A 1984 CAB Draft Report states that fare increases between 1976 and June 1983 were less than both increases in the CPI and increases in carrier costs.243 Thus, while average seat costs increased by 71%, fares during this seven year period increased by only 45%.244 The decline in real average fares came about despite staggering fuel cost increases. (One shudders to think what fares would have been under a CAB "cost of service" policy of setting fares.) Moreover, the downward trend in prices is accelerating.

The cause of decline in real fares is attributable not only to economic incentives engendered by free entry and competition, but also to a relaxation of route and fare regulations. Thus, the airlines have been able to take advantage of higher load factors by offering special discounts, filling seats which would otherwise go empty. A wide variety of pricing strategies enabled the airline industry in 1983 to achieve record load factors.245 Planes which went empty in off-peak hours during regulation now go packed with customers on special discount fares,246 thus increasing maximum utilization of aircraft. Cheaper fares for "no frills" flights allow the consumer a choice not available under regulation, taking advantage of the high elasticity of demand for air travel.247 No longer must a consumer pay for the wasteful "liquor wars" so prevalent during the "service

240. HARVARD PROJECT, supra note 3, at 103.
241. Hearings, supra note 239 at 10.
242. Id.
244. Id.
245. Id. at 21, fig. 2.2 (supra note 243). Load factors increased from 55% in 1977 to 64% in 1979. Even during the depths of the recession in 1982, load factors were at 60%, substantially higher than under regulation.
246. Id. at 20.
247. Id. The use of peak-load pricing promotes a more efficient use of the airline industry's resources. If airlines were to use their stock of aircraft intensively, and all passengers were charged the same fare regardless of when they traveled, load factors on different flights would vary considerably; they would be quite high at peak travel times and quite low on less popular flights. This is the type of pattern that regulation encouraged. The use of peak-load pricing encourages travel at less popular times, and therefore enables
competition" era of regulation. An investigation of intrastate airline fares in California in 1975 revealed that passengers, when given a choice, chose lower fares, even at the risk of fuller planes and inconvenient schedules. The high elasticity of demand for air travel was revealed by a study which looked at the experience of Southwest Airlines. Even if demand had been less elastic, however, it was noted that travelers' choices were not reflected by the price/service tradeoff.\textsuperscript{248}

Under deregulation, the market was permitted to accomplish what all the "capacity reduction" fiats of the regulators had been unable to do: reduce excess capacity. Decreases in real fares since deregulation are obviously due to both competitive pressures and to relaxation of regulations which prevented market determination of fare equilibrium so as to maximize use of airline capacity.

\section*{E. Subsidies and Service to Small Communities}

It is true, as some critics have charged, that fare reductions have been greater in some markets than in others under deregulation. These critics cannot understand why it should be cheaper per passenger mile to transport 400 persons on a Boeing 747 jumbo jet between New York and Los Angeles than to transport twenty people on a Boeing 737 between two small communities in Nevada. In a free economy, prices reflect costs. If inefficiency and the distortion of market forces is to be justified by reference to such "social benefits" as providing cheap service to high cost markets, the cost of providing such benefits should be borne fairly by society at large, and not by an unfortunate group of consumers in high density markets who otherwise are forced to "cross-subsidize" fares in high cost markets. The unfairness of forcing one group of consumers to subsidize another becomes apparent when one realizes that the cross-subsidies come from higher fares on the non-subsidized routes, thereby

\begin{itemize}
\item carriers to serve more passengers with a smaller stock of aircraft. \textit{It thereby reduces the average cost of air service.}
\item \textit{id. at 18 (emphasis added)}.
\end{itemize}

\textsuperscript{248} Southwest Airlines, an intrastate carrier unregulated by the CAB, entered the market with fares about 50 percent below those of its competitors; total air traffic on those routes increased 100-150 percent between 1971 and 1975 . . . .

The price/service tradeoff did not reflect what most travelers wanted. One economist calculated that in 1969 the fare/service combination suited only those whose waiting time was particularly valuable—such as business travelers whose time was worth $60,000 per year or more. Assuming that waiting time was worth $10 per hour (an assumption used by the industry trade association) travelers paid about half a billion dollars more than necessary in 1969. Moreover, whenever passengers had the choice of lower fares and fuller planes or better schedules but more expensive flights, they tended to choose the former. In California, PSA (which offered low-fare, full-place service) prospered, while its competitors went bankrupt.

\textsuperscript{S. BREYER, supra note 30, at 205.}
precluding many consumers from flying the nonsubsidized routes who would otherwise do so.\textsuperscript{249} The regulators prefer this hidden "cross-subsidization" over open subsidy since it is less visible and creates fewer obstacles to the political transfer of wealth. Unfortunately, it results in severe misallocation of resources.\textsuperscript{250} For example, the cost of transporting food to Hawaii no doubt increases the cost of food to Hawaiian residents, but so far no one has advocated that food consumers in Nebraska pay the difference in transportation costs to the residents of Hawaii. Only a "regulator" would say that it is unfair that Hawaiians pay a higher price for food. (Apparently, however, food is less of a "social benefit" than air travel.)

Hidden cross-subsidization, despite its wasteful misallocation of resources, might be tolerable if it only worked. Unfortunately, the CAB's policy of cross-subsidization resulted in the abandonment of service to 173 communities in the eighteen years before deregulation, devastating those small communities.\textsuperscript{251} In addition, departures at cities served were cut back substantially. Between 1970 and 1975, airlines cut small community flights by twenty five percent.\textsuperscript{252} The reason, of course, was simple: the CAB used routes as favors, handing them out to selected carriers, using them as bargaining chips to achieve cross subsidization, and even giving them out to reward airlines who had demonstrated a high level of mismanagement and inefficiency. In such an environment, the energies and resources of the airlines were directed not towards cutting costs but towards convincing the CAB to allow them to abandon routes which did not cover their costs. The results made a mockery of even the "social benefit" rationale used to justify the resource misallocation caused by cross-subsidization. A simple example illustrates the point. In

\textsuperscript{249} Note, supra note 175, at 1417, 1428.
\textsuperscript{250} Levine has described the misallocation of resources resulting from cross subsidization as follows:

Non-economic justifications of subsidy are, ex hypothesi, beyond economic argument. But a subsidy provided on non-economic grounds ought to be designed to do as little economic harm as possible. By this standard public subsidy from general revenue is preferable to private transfer payments. It makes little economic sense to charge one group of consumers a higher-than-competitive price in order to provide similar but economically unrelated services to another group of consumers. Artificially high prices for main-line transportation decrease demand for such services, injuring those who could have profitably used the service at its true cost. Subsidizing in this way creates an allocation of resources which does not maximize output of goods and services in the economy as a whole. An efficient allocation is achieved only by employing resources where they can be most profitably used.

\textit{Id.} at 1428.


\textsuperscript{252} CAB REPORT, supra note 196, at 135.
1978, before deregulation, Hot Springs, Arkansas was served by 26 DC-9 and 14 Convair flights a week, consuming 2.5 million gallons of fuel. In 1980, after deregulation, service tripled, using 96 metro flights, but consuming only 600,000 gallons and saving consumers 1.9 million dollars.253

In 1983, after five years of deregulation, there were more city-pair markets receiving non-stop service than in 1978. Small communities received more service to cargo hubs in 1983 than in 1978. Non-hub small communities which lost trunk service after deregulation experienced a dramatic gain in departures, from an average of 17 a week in 1978 to 20 a week in 1983.254 Communities eligible for local service subsidy experienced a 27% increase, and even unsubsidized communities had a 26% increase. Points retaining trunk or local service after deregulation experienced a gain from 11,146 to 11,172 departures.255 Service also increased. In 1978, 40% of those passengers that had to change airplanes made interline connections. By 1983 this had declined to less than 15%.256 Looking at small communities as a whole, an exhaustive independent study concluded that “as a group, small communities (both small hubs and nonhubs) were receiving more scheduled airline service after deregulation than before.”257

More important to the taxpayer, however, was the fact that the better service to small communities was accomplished at lower subsidy levels. The number of subsidized communities declined from 392 in 1978 to 145 in 1984.258 The average subsidy per point in 1978 was $355,000 compared to $292,000 in 1984.259 While Section 419 subsidies (promulgated under the Deregulation Act to ensure service to small communities) increased from $380,000 in 1979 to $18 million in 1982, Section 406 subsidies declined from $79 million in 1977 to $45 million in 1982, for a net savings to the American taxpayer of approximately 16 million dollars.260 Such results were accomplished in the deregulatory climate by encouragement of efficient carriers and a policy of preference for airlines requiring low subsidies. A recent study summarized the effect of deregulation on service to small communities, noting that some communities had gained service, while others had lost it; it concluded that “on balance, every class of city is benefitting from the better-integrated service network,

254. 1984 CAB Draft Report, supra note 234, at 36 (Table 3.6).
255. CAB REPORT, supra note 196, at 148 (Table 5.3).
256. 1984 CAB Draft Report, supra note 234, at 34.
257. HARVARD PROJECT, supra note 3, at 156.
258. 1984 CAB Draft Report, supra note 234, at 50.
259. Id.
260. CAB REPORT, supra note 196, at 146 (Table 5.2).
either through increased flights or more direct service to major cities, and the beneficiaries include the smaller communities (which were considered vulnerable to service losses from deregulation)."261 Overall, deregulation has resulted in more "social benefits" to small communities than all the hordes of CAB bureaucrats did in all their years of trying to create an oligopoly for the privileged trunk carriers.

F. SAFETY

Safety standards have improved considerably during deregulation. Air Transport Association262 and National Transportation Safety Board Statistics reveal that fatal crashes per 100,000 takeoffs declined from .10 in 1978 to .08 in 1982.263 Even more important, the FAA reports that "performance indicators" (accidents, injuries, FAA violation) have improved by thirty percent in the past few years.264 Airlines have found that maintaining high safety standards can cut maintenance costs. Seth Oberg, a senior vice-president for Western Airlines, has explained that "[w]e have found by maintaining a margin above what the FAA requires, we save money in the long run"—such as maintenance costs on older aircraft.265

Unlike the days under regulation, when an airline's security was always ensured by benevolent bureaucrats, airlines must now take extra care to ensure safety. As Jim Ashlock, a spokesman for Eastern Airlines, has explained, now "you've got to be awfully careful when you start taking those shortcuts," because if you lose "public trust" in an airline's safety, "you're out of business."266

Nevertheless, interest groups desperate to regain economic power lost by deregulation often confuse economic regulation with safety regulation.267 Responsibility for regulation of safety lies with the FAA,268 which is empowered to withhold air carrier operating certificates from airlines lacking sufficient resources to maintain FAA standards.269 Even during

264. See id.
265. See id.
266. See id.
267. The attempt to link safety to economic deregulation is often deliberate, but rarely supported by facts. Despite clear government statistics showing that safety has improved under deregulation, interest groups persist in trying to link safety and economic deregulation. See, e.g., Henry A. Duffy (President of ALPA), Speech Before the Transportation Research Board (Jan. 17, 1984) ("That margin of safety is being steadily eroded by deregulation, and by Continental's brand of union-busting.")
268. See S. BREYER, supra note 30, at 199.
the days of regulation it was understood that the CAB was responsible for economic regulation and the FAA was responsible for safety regulation. The success of economic deregulation, however, has reduced critics of deregulation to blaming the CAB for what they perceive to be a decline in safety standards.270

Critics look to the expansion of commuter airlines servicing small communities to support their argument that safety has suffered under deregulation. They point to statistics which show that commuter airlines have a lower safety record than the trunk airlines. It is true that the trunks are safer when measured by fatalities per hundred thousand passenger miles; however, use of such statistics in comparing trunk and commuter safety records is somewhat misleading. For example, a trunk 747 jumbo flying coast-to-coast gets credit for 948,000 passenger miles per take-off and landing, while a commuter aircraft flying 120 miles must make 465 take-offs and landings to equal the passenger miles of the jumbo. A recent study has suggested that a more appropriate standard would be based on fatalities per take-off. By such a measure the commuter airlines had a better safety record than the trunks in three of the five years between 1974 and 1978.271

There are legitimate concerns, however, about FAA safety regulations. The authorized force of FAA inspectors has been reduced by twenty three percent since 1981, although the authorization was increased in early 1984 by the Department of Transportation. The FAA is approving a large number of "deviations" from FAA standards.272 The near miss of two jumbo jets off the coast of Florida in January of 1984 raised fears that the air-traffic control system has not fully recovered from the effects of the PATCO strike; nor has the FAA been immune from political pressures. Consumer opposition to such proposed safety measures as backward seating, shoulder harnesses, and elimination of smoking and alcohol has obviously affected FAA policy.273

Cost considerations have played an important role in decisions on collision avoidance devices and life vest storage. However, the Airline Pilots Association (ALPA) has played an important role in safety, and for this they deserve credit for saving many lives. Criticism of safety standards and their enforcement should be directed to the FAA. If 100 hours of flight time is too many from a safety standpoint, as ALPA claims, the regulation should be changed. The FAA should then strictly enforce its regulations across the board.274

273. Id.
274. Levine has examined the argument that safety depends upon economic regulations:
Market entry controlled by FAA safety regulation enforcement is not inconsistent with economic deregulation of the industry. Indeed, airline safety today would be far higher if even half the money appropriated for wasteful economic regulation in the past had been spent instead on safety regulation and enforcement.

VI. CONCLUSION

The history of transportation regulation in the United States proves not only the truth of Stigler’s hypothesis,275 but of a far older one as well: the road to Hell is paved with good intentions. Indeed, it is only recently that the bankruptcy of the “public interest” hypothesis has been exposed—first by scholars, then by President Kennedy in 1962, and by the Kennedy Hearings in 1975. In the double-speak of regulation, competitive fare reductions are “cut-throat” pricing; market dynamics are “chaotic”; price-fixing, criminal in any other sphere when done by industrial robber barons, has become “fare stabilization”; and protective entry control is known as “reducing excess capacity.” According to the die-hards, all twenty nine of the thirty members of the American Transport Association who support deregulation don’t know what is good for them; the new, lean and more efficient firms which have entered the market, reducing the old trunk’s market share, don’t deserve to exist; consumers should be limited to choosing an airline based on who wins a “liquor war” or provides a Polynesian pub, rather than on what consumers care about most, namely price; and certain unfortunate consumers should be asked to pay the fares of other consumers who would rather not pay the cost of their own ticket. (Who does?)

The regulators had ninety three years to impose their ideology on the railroads, forty five years to oligopolize the competitive trucking industry, and forty years to accomplish in the airline industry what even John D. Rockefeller failed to do in oil: prevent even a single competitor from entering the industry. Deregulation was given its sternest test by being asked to reverse the slide of three industries in the midst of the worst recession since the Great Depression. In a few short years, deregulation

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275. See supra text accompanying note 40.
has accomplished virtually everything the economists had predicted for so long: reduced fares; more efficient allocation of resources; greater service to small communities; a reduction in subsidies, both by government and consumers; increased safety, and deconcentration of power in the industry. In light of its accomplishments and in the face of all the odds, deregulation certainly deserves the same chance the regulators had. Based on the experience of the past few years, deregulation shows every sign of giving the transportation industry a better opportunity to serve the real needs of the consumer, the industry and its employees.
HAROLD A. SHERTZ ESSAY

The Shipping Act of 1984:
A Return to Antitrust Immunity

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I. INTRODUCTION

Few people realize the importance of international maritime shipping. It is not only a major vehicle for trade in a world where countries are becoming increasingly economically interdependent, but also provides an ever-ready reserve naval fleet in the interest of national defense. Early in the 20th century, Congress recognized this importance and passed the Shipping Act of 1916,¹ which provided the shipping conferences with protection from the antitrust regulations sweeping the business world. This protection, however, has been significantly eroded by the federal judiciary during the ensuing decades.

As a result, the U.S. Federal Maritime Policy has been, in effect, a policy in disarray. The shipping industry has been operating in an unstable environment; lawyers cannot advise their clients with any degree of certainty as to which of the conferences' activities are subject to the antitrust laws and which are subject to protection under the Shipping Act. This confusion has forced the United States shipping conferences to operate at a severe disadvantage in the international maritime community, and has wholly frustrated maritime commerce from reaping the benefits intended them by Congress.

Lately, there has been a flurry of Congressional activity designed to remedy the ocean shipping dilemma. The Shipping Act of 1984² is by far the best effort, with unsurpassed potential to stabilize the regulatory environment and reinstate the original intention of the 1916 Congress. This article will examine the specific problems which led to the need for such a bill, how and why the case law developed as it did, the changes this Act will make in the regulatory scheme, and the effectiveness of the Shipping Act of 1984 in curing the ills of United States maritime policy.

II. LEGISLATIVE HISTORY

A. PRE-TWENTIETH CENTURY

In order to understand contemporary U.S. maritime policy, it is necessary to review pre-twentieth century policy.³ The colonists came to North America with strong maritime backgrounds, which were reflected by the government of the infant nation. The first enactment of the first Congress in April 1789 produced a tariff system designed to protect U.S. shipping. In 1817, Congress also secured cabotage⁴ protection for

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¹ Ch. 451, 3a Stat. 728 (codified as amended at 46 U.S.C. §§ 801-42 (1982)).
⁴ S. ABRAHAMSSON, INTERNATIONAL OCEAN SHIPPING: CURRENT CONCEPTS AND PRINCI-
ocean shipping. Supported by these policies, the U.S. shipping industry prospered to the point 92.5% of foreign shipments were carried in U.S. ships.\(^5\) Between 1930 and the Civil War, the United States was a leader in the shipbuilding industry, producing wooden clipper ships widely considered to be the best sailing vessels in the world at that time.\(^6\) The American shipwrights, however, were hesitant to abandon their wooden sailing vessels for the more modern steel ships being produced in Europe. "When the United States opted to protect its youthful steel industry by a protective tariff, the Morrill Act of 1864, American steel ships were non-competitive in price."\(^7\)

Another adverse factor was the Civil War, which seriously depleted the U.S. fleet. Further, U.S. vessels that had fled to foreign registry to escape confederate privateers were not allowed to return to U.S. registry. By 1900 the U.S. fleet consisted of but 816,795 tons: less than that of the 1810 fleet. Moreover, the U.S. share of its foreign waterborne commerce was a meager 9.3 percent.\(^8\)

B. EARLY TWENTIETH CENTURY

In 1904, after becoming aware of the tremendous weakness of its merchant marine, the United States promulgated its first "cargo preference law"; American military shipments were required to be carried in U.S. vessels. This did little to improve the lagging U.S. shipping industry. It was not until World War I that substantially increased aid to the merchant marine was realized.\(^9\)

1. THE SHIPPING ACT OF 1916

At the onset of the first World War, the United States, though neutral at the time, suffered from a severe shipping deficiency. Congress’ solution to this dilemma was the Shipping Act of 1916 which remains current law in the U.S. shipping industry.\(^10\) This was the first piece of comprehensive maritime legislation of the 20th century. Its promulgation was not the result of any desire to regulate the then infant shipping industry, but was a response to the war raging in Europe. The Act provided for antitrust immunity by permitting carriers to openly organize shipping conferences, established a U.S. Shipping Board (which later became the Fed-

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6. id.
7. id. at 5.
8. id.
9. See id.
eral Maritime Commission), prohibited discriminatory practices and required the filing and publication of tariffs with the FMC. In this respect, the Act was both regulatory and innovative, providing incentive for the production of ships in the event of military engagement. By the time the Act was implemented, however, the United States was already at war.

2. **The Conference System**

The combination of shipowners' propensities to price at destructive levels and the existence of surplus shipping capacity resulted in rate wars during the nineteenth century, and culminated in the creation of conferences at the turn of the century. Through agreements enforced among its members, the conference system attempted to combat the tendency toward destructive pricing, and to prevent wasteful over-tonnaging and loss of the huge investments in fleets and equipment. One of the major governmental investigations subsequently undertaken was the House Committee on Merchant Marine and Fisheries inquiry into shipping combinations, conducted from 1912 to 1914. The Alexander Committee (named for Representative Joshua M. Alexander, then Chairman), whose conclusions helped establish the basis for United States shipping policy, found that there were basically two types of conference agreements. The first were used to restrain competition among the conference members and included agreements for ratefixing, sailing rationalization, apportioning traffic by allotting the number of movements for each line, and various pooling agreements for revenues and cargoes. The second were used to restrain non-conference competition. These included deferred rebates and preferential contracts with shippers which persuasively attached them to the conference.

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14. The deferred rebate system gives shippers who agree to exclusive use of the conference lines in a given trade a rebate of a certain percentage of their payments. The rebate is computed for a designated period but is not paid for several months. During the contract period and the additional months, the shipper must continue the exclusive use of the conference lines to earn the rebate. This system was found to be the most effective device for control of a trade. *HOUSE COMM. ON MERCHANT MARINE AND FISHERIES, REPORT ON STEAMSHIP AGREEMENTS AND AFFILIATIONS IN THE AMERICAN FOREIGN AND DOMESTIC TRADE, H.R. Doc. No. 805, 63rd Cong., 2d Sess. 287* (1914) [hereinafter cited as ALEXANDER REPORT].

15. The Alexander Committee found both advantages and disadvantages in conference
Fearing that removal of the conference system would produce either rate wars or mergers, the Alexander Committee did not recommend prohibiting the conference system entirely. The Committee feared that the U.S. market might become monopolized by either of these possibilities.\(^{16}\)

Nor did the Alexander Committee recommend preserving the status quo, because the potential for abuse in the conference system was inherent and required some control. The solution the Alexander Committee proposed, was supervisory control over the U.S. trades by a government agency. The shipowners’ reaction to the committee’s recommendations was so hostile that no action was taken on the investigatory report until 1916, when the Shipping Act was passed embodying the Alexander Committee’s recommendations.\(^{17}\)

The Shipping Act of 1916 specifically addressed the conference system and laid down the rules from which case law later departed. The primary purpose of the Act, detailed in section 15, required all conference agreements to be filed with the FMC (and subject to approval by FMC in order to be exempt from antitrust laws). The FMC is required to disapprove, after notice and hearing, any agreement it finds:

1. to be unjustly discriminatory or unfair,
2. to operate to the detriment of the commerce of the United States,
3. to be contrary to the public interest, or
4. to violate the Shipping Act.\(^{18}\)

Agreements that create closed conferences and those which do not provide a right of independent action for the participants are automatically vetoed.\(^{19}\)

3. **Development of the Conference System**

The conference system . . . had developed in response to the fact that the ocean liner industry is highly capital intensive, leading individual liners to attempt to fill their vessels through intensive competition, which, if not controlled, would result in excessive and destructive competitive practices. The

\(^{16}\) Note, supra note 12, at 642-43.

\(^{17}\) Id.


\(^{19}\) The Act provides:

No such [conference] agreement shall be approved, nor shall continued approval be permitted for any agreement . . . which fails to provide reasonable and equal terms and conditions for admission and re-admission to conference membership of other qualified carriers in the trade, or fails to provide that any member may withdraw from membership upon reasonable notice without penalty for such withdrawal.
shipping conference, itself, is a voluntary association of ocean carriers operating on a particular trade route between two or more countries. The purpose of a shipping conference is the self-regulation of price competition, primarily through the establishment of uniform freight rates and terms and conditions of service between the member shipping lines.\(^{20}\)

Conferences are comprised of two types of membership, open or closed. In the open system, any carrier can be admitted to membership if he has the intent and ability to offer liner service and agrees to the terms of the conference agreement. Closed conferences are distinctly different in that the acceptance of a new member is subject to concurrence of the already existing members. Closed conferences, by thus limiting service, act as a restraint on supply by limiting empty cargo space and "thus provide a curb against uneconomic sailings which in turn can result in overall lower-cost shipping."\(^{21}\) By functioning in this manner conference members seek protection from the predatory practices and rate wars which would otherwise result. As a defense mechanism against the competitive practices of non-members, and to assure members adequate return on their investment, conferences will use shipper loyalty devices, such as dual rates\(^{22}\) or deferred rebates, which provide adequate incentive for shippers to continue to employ conference members.

This discount/rebate system has come under attack in recent years, particularly from the federal judiciary. This has been a drastic step away from the conclusions and recommendations of the Alexander Committee. In essence, the Committee concluded that the conference system could not successfully function without immunity from U.S. antitrust laws.\(^{23}\) The Committee did not feel that the shipping industry should arbitrarily be given exemption from the antitrust laws, but in light of the elements of an international shipping market, the Committee did feel a certain amount of immunity from antitrust should be allowed.\(^{24}\) The Committee in its report of 1914 stated:

To terminate existing agreements would necessarily bring about one of two results: the lines would either engage in rate wars which would mean the elimination of the weak and the survival of the strong, or, to avoid a costly struggle, they would consolidate through common ownership. Neither result can be prevented by legislation, and either would mean a monopoly fully as effective, and it is believed more so, than can exist by virtue of an


\(^{21}\) Id.

\(^{22}\) "Under the dual rate system, a shipper agrees to give all or some fixed portion of its patronage to the contracting conference carriers, in return for . . . percentage discount, commonly fifteen percent, from the rates applicable to those shippers which do not enter into such an agreement." Fawcett & Nolan, supra note 13, at 539-40.

\(^{23}\) S. REP., supra note 20, at 3.

\(^{24}\) Id.
agreement.25

Currently, there are few who would argue with the importance of the shipping conference system as a stabilizing factor in the U.S. shipping industry. Experts believe that the conference system "is a prerequisite for stable liner services, operates in the interests of shippers and consumers, and should not be prohibited or otherwise inhibited from performing its normal commercial functions by legislative interference."26 Today, proponents of the conference system continue to argue that if a trade is overtonnaged and the conference is not strengthened, destructive competition will again ensue because of the individual shipowner’s cost structure and pricing policy.

The overall level of rates is at best only marginally adequate to finance replacement of equipment and improvement of services . . . . The system’s supporters further contend that any weakening of the conference system will lead to violently oscillating tariffs, which in the long run will prove more expensive to shippers than the present system.27

4. THE SHIPPING ACT OF 1920

After World War I the government had the dual problem of disposing of surplus vessels and implementing an innovative peacetime shipping policy. The legislative solution took shape in the Merchant Marine Act of 1920.28 The new Act mandated that the United States require, for national defense, international relations and trade, an adequately equipped merchant marine.29 While the goals of the Act were well directed, its effectiveness was somewhat lacking. Surplus ships were sold to the private sector at prices below cost. Even so, the government could not rid itself of all of them.30

25. Id.
27. S. Lawrence, United States Merchant Shipping Policies and Politics 14-15 (1966); Note, supra note 12, at 643-44.
29. "[i]t is necessary for the national defense and domestic commerce that the United States shall have a merchant marine of the best equipped and most suitable types of vessels sufficient to carry the greater portion of its commerce and serve as a naval reserve or military auxiliary in time of war or national emergency, ultimately to be owned and operated privately by citizens of the United States and it is hereby declared to be the policy of the United States to do whatever may be necessary and to develop and encourage the maintenance of such a merchant marine, and, insofar as may not be inconsistent with the express provisions of this Act, the United States Shipping Board shall be in the disposition of vessels and shipping property as hereinafter provided, in the making of rules and regulations, and in the administration of the shipping laws keep always in view this purpose and object as the primary end to be obtained.
30. Id. See also Bess & Farris, supra note 3, at 5.
5. **THE MERCHANT MARINE ACT OF 1928**

The ineffectiveness of the Shipping Act of 1920 in stabilizing the U.S. shipping industry resulted in passage of the Merchant Marine Act of 1928.31 By 1928, the state of the fleet was rapidly deteriorating and new legislation was required. “It reaffirmed the 1920 Act’s statement of policy, set up direct mail subsidies to promote trade, and established a construction loan fund to promote replacement of reconditioning of the aging wartime fleet.”32

The Shipping Act of 1920 and the Merchant Marine Act of 1928 were two of the very few legislative enactments which attempted to modify the Shipping Act of 1916. The primary modification of the 1916 Act, however, did not occur until enactment of the Merchant Marine Act of 1936.

6. **THE MERCHANT MARINE ACT OF 1936**

The Merchant Marine Act of 193633 set the congressional foundation on which modern-day maritime policy rests and was the first attempt to set down a comprehensive maritime policy in the post-1916 Act period. The act itself was a legislative monument, as it enacted the first specific peacetime promotion of America’s maritime program. The program was revolutionary because never before had the U.S. merchant fleet been directly subsidized. Prior to this, Congress consistently refused to consider the necessity of government aid to the maritime industry.34 It can even be argued that Congress contributed to the decline of the fleet by failing to address fundamental shipping industry problems.35 By the year of enactment, U.S. flagships were carrying only 29.7% of U.S. trade. Concern over the declining merchant marine and the failure of the 1928 Act to attain its goal led to the eventual enactment of this pivotal piece of legislation.36

**C. MID-TWENTIETH CENTURY**

From 1936 to 1970, the U.S. fleet fluctuated in size in response to national defense demands. By the late 1960’s, the shipbuilding and operating industries were on an apparently irreversible downward trend.37 The response manifested itself in the Merchant Marine Act of 1970.38 The Act sought to: (1) broaden the firms eligible for direct subsidy, and (2)

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32. Bess & Farris, supra note 3, at 5-6.
34. S. LAWRENCE, supra note 27, at 55.
35. Bess & Farris, supra note 3, at 6.
36. Id.
37. Id.
increase efficiency by encouraging more forward planning and by limiting certain types of subsidy-eligible cost increases.\textsuperscript{39} It is generally accepted that, though some parts of the Act were relatively successful, the 1970 Act was indeed a failure.\textsuperscript{40}

It is well documented that legislation promulgated subsequent to the Shipping Act of 1916 has been less than effective in stabilizing the United States shipping industry. The major factor in the current strife ridden industry, however, is the gradual erosion of the antitrust exemption which has occurred as a result of numerous decisions and rulings by the federal judiciary.

III. PROBLEMS IN U.S. MARITIME POLICY

A. EROSION OF CARRIER ANTITRUST IMMUNITY

It is no secret that the carriers, under current U.S. maritime policy, are suffering. To date, the intentions of Congress in passing the Shipping Act of 1916 have not been realized. Carriers are, in many cases, unable to secure timely approval for conference activity and tying arrangements which give them their economic durability.\textsuperscript{41} Such agreements are generally in the form of ratemaking agreements, intermodal arrangements, pooling agreements, joint service ventures, rationalization agreements, discussion agreements, and inter-conference agreements. "Even when approval by the FMC is secured, there remain wild fears of prosecution under the antitrust laws should the parties' conduct subsequently be found to exceed the permissible bounds of the agreement or to be otherwise in violation of the Shipping Act of 1916."\textsuperscript{42} Under the Shipping Act, carriers were, in essence, encouraged to act in concert, but often encountered problems complying with the antitrust laws.\textsuperscript{43} This has consistently occurred despite Congress' intent to treat foreign waterborne commerce of the United States differently from those forms of commerce and industries subject to the antitrust laws. Currently "there is a compelling need to clarify that ocean common carriers be exempt from the antitrust laws and that this exemption should be clearly written into the Shipping Act."\textsuperscript{44}

The Shipping Act of 1916 was, indeed, clear on its face. In short, it mandated that Shipping Act remedies pre-empted antitrust remedies.\textsuperscript{45} "However, there can be no doubt that the antitrust immunity provisions of

\begin{itemize}
\item \textsuperscript{39} Bess & Farris, supra note 3, at 7.
\item \textsuperscript{40} Id. at 8.
\item \textsuperscript{41} S. Rep., supra note 20, at 4.
\item \textsuperscript{42} Id.
\item \textsuperscript{43} AST&T Report, supra note 11, at 200.
\item \textsuperscript{44} Id.
\item \textsuperscript{45} See Note, supra note 12, at 648-49.
\end{itemize}
current law have caused carriers to be uncertain as to which of their activities are truly covered by immunities and which are not.\textsuperscript{46} Since 1961, conference immunity from antitrust laws has been continually eroded by the federal courts and the Department of Justice.\textsuperscript{47} Early court decisions on this issue did establish that the antitrust statutes were unable to proscribe agreements of shipping conferences and that remedies for violations of the 1916 Act were found within the act itself.\textsuperscript{48} This uncertainty about the applicability of the antitrust laws is a severe disadvantage to U.S. carriers in the face of international competition.

\section*{B. \textit{Case Law Development}}

The first major litigation concerning section 15 of the Shipping Act reached the Supreme Court in the early 1930's. In \textit{United States Navigation Co. v. Cunard Steamship Co.},\textsuperscript{49} the U.S. Navigation Company sought injunctive relief against the Cunard Steamship Company and its fellow conference members. In disregard of the legislative intent to provide antitrust immunity, it was charged that the conference, through exclusive patronage or dual rate agreements, had violated the Sherman and Clayton antitrust Acts. It was also alleged that the conference activities had never been approved by the Shipping Board, which later became the FMC. The Court held that:

In any event, it reasonably cannot be thought that Congress intended to strip the board of its primary original jurisdiction to consider such an agreement and “disapprove, cancel or modify” it, because of a failure to file it as \S\ 15 requires. A contention to that effect is clearly out of harmony with the fundamental purposes of the act and specifically with the provision of \S\ 22 authorizing the board to investigate any violation of the act upon complaint, or upon its own notion and make such order as it deems proper. And whatever may be the form of the agreement, and whether it be lawful or unlawful upon its face, Congress undoubtedly intended that the board should possess the authority primarily to hear and adjudge the matter. For the courts to take jurisdiction in advance of such hearing and determination would be to usurp that authority. Moreover, having regard to the peculiar nature of ocean traffic, it is not impossible that, although an agreement be apparently bad on its face, it properly might, upon a full consideration of all the attending circumstances, be approved or allowed to stand with modifications.\textsuperscript{50}

As to the availability of a private right to sue under \S\ 16 of the Clayton


\textsuperscript{47} \textit{AST&T Report}, \textit{supra} note 11, at 189.

\textsuperscript{48} \textit{See Note, supra} note 12, at 648.

\textsuperscript{49} 39 F.2d 204 (S.D.N.Y. 1929) \textit{aff'd}, 50 F.2d 83 (2d Cir. 1931), \textit{aff'd}, 284 U.S. 474 (1932).

\textsuperscript{50} \textit{Id.}, 284 U.S. at 487 (emphasis in original).
Act, the Court ruled such a right did not exist.\textsuperscript{51}

Exactly twenty years after \textit{Cunard}, the Supreme Court was presented with the issue of whether the United States could do what a civil litigant could not, that is, enjoin conference agreements which had not been approved by, or even submitted to, the Federal Maritime Board. In \textit{Far East Conference v. United States},\textsuperscript{52} the Supreme Court, in a majority opinion authored by Justice Frankfurter, held that the government’s plea for injunctive relief fared no better than a civil litigant’s and that any such action under the antitrust statutes was barred under the rationale of \textit{Cunard}.\textsuperscript{53} The United States could not enjoin, under the antitrust laws, conference agreements that had not been submitted to the Federal Maritime Board for approval.\textsuperscript{54} Thus, it was clearly settled that the antitrust laws were not controlling where the actions alleged fell within the jurisdiction of the Shipping Act, and remedies for violating section 15 were within the provisions of the Act.\textsuperscript{55}

For more than a decade afterward, the lower federal courts followed \textit{Cunard} and \textit{Far East}, consistently ruling that shipping conferences fell outside of the antitrust statute, and that the remedies for unapproved conference activities under section 15 of the Shipping Act of 1916 must be found within the provisions of the Act itself.\textsuperscript{56} \textit{Federal Maritime Board v. Isbrandtsen}\textsuperscript{57} was the first Supreme Court case involving the Federal Maritime Board’s approval of a conference using exclusive patronage contracts with shippers. Isbrandtsen was an independent carrier serving the Japan-Atlantic trade in direct competition with the Japan-Atlantic and Gulf Freight conference. By consistently undercutting the conference rates, Isbrandtsen captured thirty percent of the trade.\textsuperscript{58} The conference was forced to retaliate. Initially the conference cut its rates to meet those of Isbrandtsen, but Isbrandtsen only undercut the conference rate, maintaining its price advantage.\textsuperscript{59} The conference then promulgated a dual rate contract which would push the shippers toward the conference carri-

\begin{footnotesize}
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\item id. at 486.
\item 342 U.S. 570 (1952).
\item id. at 573.
\item id.
\item id. In a later case it was held that although the Commission can approve prospective operations under agreements which have been implemented without approval, the Commission has no power to validate preapproval implementation of such agreements. Therefore, \textit{Far East} and \textit{Cunard} principles only preclude courts from awarding treble damages when the defendant's conduct is arguably lawful under the Shipping Act. \textit{Carnation Co. v. Pacific Westbound Conference}, 383 U.S. 213, 222 (1966).
\item Fawcett & Nolan, supra note 13, at 546.
\item 356 U.S. 481 (1958).
\item id. at 485.
\item id. at 486.
\end{enumerate}
\end{footnotesize}
ers. Isbrandtsen was forced to challenge the pseudo-monopolistic agreement proposed by the conference.

In *Isbrandtsen*, the U.S. Supreme Court, in a split decision, affirmed the Court of Appeals but ambiguously skirted the lower court’s per se holding. Rather, the Court ruled that under section 14’s prohibition against “discriminating or unfair methods” the Maritime Board had no authority to rule on the dual-rate system at issue.\(^\text{60}\) This landmark decision made three important contributions to judicial review of Maritime Commission decision making:

1. It clearly established that the purpose of the Shipping Act was to prevent monopolistic practices, not sanctify them;
2. That to accomplish this purpose the courts can redefine the governing statute by reasoning from the statute and its legislative history; and
3. That the antimonopolistic intent of the Act served to protect independent nonconference carriers, as well as shippers, from the abuses of the conference system.\(^\text{61}\)

In so deciding, the Court overturned the Maritime Board’s approval of the conference’s dual rate agreement by citing anticompetitive motive.\(^\text{62}\) The purpose of the Shipping Act, the Court reasoned, was not only to permit conference agreements, but to eliminate conference abuses as well.\(^\text{63}\) By holding that the Act was designed to eliminate anticompetitive activities and discrimination by the conferences, the Court re-established the guidelines of the Shipping Act. Protection against such unfair business practices was to be afforded independent as well as conference shippers. “The Court suffered little embarrassment in augmenting the Act to preclude dual rate contracts, a device which Congress itself had not expressly prohibited.”\(^\text{64}\)

In essence, the Supreme Court outlawed exclusive patronage contracts, ruling that the language of section 14 of the Shipping Act, which prohibited “resort to other discriminating or unfair methods” to hinder outside competition, permitted an antitrust exemption only for expressly

\(^{60}\) Fawcett & Nolan, *supra* note 13, at 547. The Court stated:

Since the board found that the dual-rate contract of the Conference was “a necessary competitive measure to offset the effect of non-conference competition” required to meet the competition of Isbrandtsen in order to obtain for its members a greater participation in the cargo moving in this trade, it follows that the contract was a “resort to other discriminatory or unfair methods” to stifle outside competition in violation of § 14


\(^{62}\) 356 U.S. at 493; Pansius, *supra* note 71, at 341.

\(^{63}\) 356 U.S. at 488-93.

\(^{64}\) Pansius, *supra* note 71, at 342-43.
enumerated practices.\textsuperscript{65} Congress later circumvented \textit{Isbrandtsen} by once again exempting the activities at issue from the antitrust laws,\textsuperscript{66} at the same time providing that conference agreements could be approved by the FMC only if it was determined that they were not inconsistent with the "public interest."\textsuperscript{67}

In overturning \textit{Isbrandtsen}, however, Congress did not reject the procompetitive policies upon which the Court had relied in barring dual rate contracts. To date, this procompetitive policy is still available to the courts for once again redefining the Shipping Act.\textsuperscript{68}

Following the Supreme Court's decisions in \textit{Cunard} and \textit{Far East}, the law appeared settled that the antitrust statutes were inapplicable to agreements of shipping conferences within the purview of the Shipping Act, whether approved or not, and that the remedies for violating section 15 of the Shipping Act were to be found within the provisions of that Act itself. In distinguishing \textit{Cunard} and \textit{Far East}, the Supreme Court broadened the authority of the federal courts beyond what Congress intended by mandating to the FMC exclusive jurisdiction only where such is necessary to avoid conflict between the two factions.\textsuperscript{69} This legal presumption was quickly exploded by the Supreme Court's decision in \textit{Carnation Co. v. Pacific Westbound Conference}.\textsuperscript{70}

\textit{Carnation} resulted from a conflict between a shipper of dairy products and two steamship conferences, both of which were serving the Philippine Islands market. Carnation challenged the legality of an agreement between the two conferences and alleged that as a result of a clandestine rate-fixing agreement between the two, its rate requests had been improperly refused.\textsuperscript{71}

The federal district court dismissed the complaint on the grounds that it was without jurisdiction to entertain the suit because the Shipping Act provided the exclusive remedy for the wrongs alleged. On appeal by Carnation, the Ninth Circuit Court of Appeals affirmed the lower court.\textsuperscript{72} The

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\textsuperscript{65} 356 U.S. at 493-95.
\textsuperscript{67}  Id.; Hanson, \textit{Regulation of the Shipping Industry: An Economic Analysis of the Need For Reform}, 12 L. & POL'Y INT'L Bus. 973, 983-84 (1980).
\textsuperscript{68}  \textit{See} Pansius, \textit{supra} note 71, at 340, 343.
\textsuperscript{69}  \textit{See} S. REP., \textit{supra} note 20.
\textsuperscript{70}  383 U.S. 213 (1966).
\textsuperscript{71}  Id.
\textsuperscript{72}  336 F.2d 650 (1964). The court held, \textit{inter alia}:
\end{flushleft}

In dismissing the action, the court below relied on the decision in the cases of \textit{U.S. Navigation Co. v. Cunard Steamship Co.} and \textit{Far East Conference v. United States}. It seems plain to us that both of these decisions support and require the action of the court below . . . . [W]e think that appellant's efforts to assert the lack of the continuing authority of \textit{Cunard} and \textit{Far East} is entirely fallacious and altogether unsupportable.
Supreme Court, however, was far more sympathetic than the lower courts had been. In issuing the opinion of the Court, Chief Justice Earl Warren struck down fifty years of legal precedent. Warren held that because the FMC was directed by the Shipping Act of 1916 not to approve agreements which would violate the Act, conference action found to be in violation thereof could not receive section 15 exemption from antitrust laws. Carnation, in one fell judicial swoop, thus revoked the antitrust immunity Congress had intended for shipping conferences under the 1916 Act, and ignored the rule preventing treble damage actions against regulated conferences. Carnation thereby placed antitrust penalty exposure on top of the Shipping Act penalty exposure.

Under Carnation, a shipper may therefore sue for treble damages when a conference agreement violates antitrust laws and is implemented without FMC approval. Prior approval by the FMC is necessary for antitrust immunity. The Carnation rationale permits a court to impose antitrust sanctions when the defendant's conduct clearly violates the Shipping Act. However, where a presumption of legality exists, the court must suspend any adjudication on the antitrust claim until the close of the FMC's investigation. Carnation, in short, not only drastically reduced antitrust protection but subjected the regulated conference carriers to treble damage liability under the antitrust statutes.

The decision in FMC v. Aktiebolaget Svenska Amerika Linien represents the most severe restriction on conference immunity from antitrust regulation. Svenska's lengthy litigation began when the FMC, after receiving a complaint from the American Society of Travel Agents, began an investigation into previously submitted and approved conference agreements. The case involved two passenger steamship conferences whose members served the passenger market of the Atlantic. The Supreme Court upheld the FMC's consideration that the "public interest" standard created the presumption that a conference restraint which interferes with the policies of antitrust laws is "contrary to the public interest"

Id. at 653, 657.

73. Fawcett & Nolan, supra note 13, at 553.

74. 383 U.S. at 219-20. The Court distinguished Far East and Cunard, and stated that "those cases merely hold that courts must refrain from imposing antitrust sanctions for activities of debatable legality under the Shipping Act in order to avoid the possibility of conflict between the courts and the Commission." 383 U.S. at 220. "In light of the language used in Cunard and Far East and of the dissent's exception to the majority's holding in Far East, it is clear that Carnation created a distinction where none existed before." Fawcett & Nolan, supra note 13, at 649.

75. Fawcett & Nolan, supra note 13, at 554.

76. Note, supra note 12, at 649.

77. Id.


79. Note, supra note 12, at 651.
and, therefore, invalid. The Court ruled that such a conference agreement would be approved only if the members could rebut the presumption by making a prima facie showing that the restraint is required by "a serious transportation need, necessary to secure important public benefits, or in furtherance of a valid regulatory purpose of the Shipping Act."80 This presumption greatly altered antitrust considerations in section 15 proceedings by attaching to them a substantial degree of significance.81

In so ruling, the Supreme Court shifted the burden of proof to the conferences in determining whether FMC reliance on antitrust policy as justification for disapproving conference agreements was proper. The Court found that the 1961 amendment82 expanded FMC authority to disapprove agreements.83 The "Svenska presumption" has become a balancing test, with the degree to which the conference agreements impede free trade tipping the scales against the benefits.84 This has the effect of not only limiting antitrust exemption, but also serves to postpone FMC action by creating a standard which has become the basis for frequent intervention by the Department of Justice in FMC review proceedings.85

Although in deciding Svenska the Supreme Court granted FMC power to consider antitrust implications of an agreement, it later qualified that language by stating that the FMC was required to do so. The Carnation (Sabre) rationale on antitrust penalties and the Svenska interpretation of "the public interest" have operated to reduce the one-time congressional mandate for antitrust immunity to a forgotten promise.86

Two years later, Sabre Shipping Corp. v. American President Line, Ltd.87 expanded the effect of the antitrust regulations on the supposedly exempt ocean shipping conferences. In Sabre, the FMC determined that the rates of the conferences had a predatory effect on the independent

80. 390 U.S. at 243.
81. S. Rep., supra note 20, at 6. See also Hanson, supra note 77, at 984.
82. The 1961 amendments to the Shipping Act added a fourth test to section 15, requiring that an agreement be disapproved where it was found to be "contrary to the public interest." See S. Rep., supra note 20, at 6.
83. Note, supra note 12, at 650.
84. Hanson, supra note 77, at 984.
85. See id. In addition to the Svenska requirement of considering the anticompetitive effect of an agreement, the FMC is obligated to go beyond notice and comment when a competitor raises antitrust issues in objecting to a filed agreement. In Marine Space Enclosure, Inc. v. Federal Maritime Comm'n, 420 F.2d 577 (D.C. Cir. 1969), the court held that § 15 requires the FMC to provide a hearing unless the FMC has already determined that the agreement is routine or that the impact on commerce is de minimis. 420 F.2d at 584. The FMC continues to operate under the structures imposed by this case. Closed Conferences and Shippers' Councils in the U.S. Liner Trades: Hearings on H.R. 11422 Before the Subcomm. on Merchant Marine of the House Comm. On Merchant Marine and Fisheries, 95th Cong., 2d Sess. 29-32 (1978) (statement of Ky. P. Ewing, Jr., Deputy Att'y Gen., Antitrust Division, Dep't of Justice).
86. Note, supra note 12, at 651; Fawcett & Nolan, supra note 13, at 563-64.
carrier, Sabre Line, and the conference rates were therefore "so unreasonably low as to be detrimental to the commerce of the United States" within the meaning of section 18(b)(5) of the Shipping Act. Sabre sued for treble damages under the antitrust laws. The court applied the rationale that even though the rates of the defendant conferences were FMC approved, the anti-Shipping Act practices violation stripped the conferences, ex post facto, of section 15 antitrust immunity for those "unlawful" activities. As a result, the treble damage claim was valid.88

To summarize these holdings, notwithstanding the clear intention of Congress in enacting the Shipping Act of 1916, subsequent case law has effectively pulled the full antitrust exemption out from under the shipping conferences. Carnation was the first case to decisively strip away the defense of exemption from the antitrust laws. Later, Svenska placed the burden of proof of a conference acting within the provisions of the 1916 Act on the conferences themselves if their agreements or actions were challenged. Finally, Sabre completed the erosion by holding that even though an agreement may have been approved by the FMC, the finding of a violation would strip the conference of their approved immunity. It is this erosion of antitrust immunity which established the need for strong legislation reaffirming the antitrust environment initially established in 1916.

C. CONSEQUENCES OF ANTITRUST IMMUNITY EROSION

Carriers have been forced to operate in the dark, suspended between congressionally enacted antitrust immunity and judicially applied antitrust exposure. From the development of federal case law, the conferences must now prove their practices will not be in violation of the very antitrust laws from which they have been given immunity. In addition, they have become targets of a "Catch-22" situation for Shipping Act violations; civil penalties, criminal sanctions, and private treble damage actions.89

Although the original goal of the 1916 Act was to grant the conference system ultimate legality and protect it from the antitrust laws of the United States, this has become a mere apparition due to destructive case law. Today, conferences are forced to act at their own risk when functioning within the very guidelines established for them by Congress in the Act of 1916 (legislation of a type not since duplicated). Even the FMC now views such practices as anticompetitive and dangerous to trade and the public.90

The present situation has resulted in major regulatory problems: de-

88. See generally Note, supra note 12, at 649-50.
89. S. REP., supra note 20, at 13.
90. Id. at 6.
lay in the FMC's approval process for section 15 agreements stretching on for years, application of vague standards for approval of section 15 agreements, and resultant loss of predictability in regulatory decision making. Conflicting views of executive branch agencies regarding acceptable conference practices, and shifting decisions by the FMC and courts, have created confusion over the guidelines within which the conferences may operate and the government's regulation of conference activities. This has had a chilling effect on carriers attempting to cooperate in formulating constructive commercial arrangements to improve U.S. participation in the ocean shipping industry, increase operational efficiency, and promote comity with foreign trading partners. These efforts have exposed all parties to the threat of prosecution under the U.S. antitrust laws.91

Absent the security of antitrust exemption, carriers will have no incentive to enter into any conference agreement. As established by the Alexander Committee, such a situation will lead to price wars, and ultimately, to monopoly control by the survivors.92

IV. SHIPPING ACT OF 1984

A. NEED FOR LEGISLATION

The need for new legislation which will reemphasize the guidelines within which the U.S. shipping industry must operate is manifest. The development of case law affecting antitrust immunity has caused the ocean carriers severe problems. Subjection to antitrust laws, coupled with the burden of justification before the FMC and courts, have deprived U.S. ocean carriers from realizing optimal price and cost benefits that could be achieved through the economics of rationalized or joint services.93 Unlike other transportation modes, the demand for international ocean carriage is an inelastic one. Therefore, the lower prices which competition might ordinarily foster will not generate more cargo in this area.94

In a report to the Senate Subcommittee on Commerce, Science and Transportation, it was pointed out that "this uncertainty regarding antitrust immunity inhibits conferences in U.S. trades from agreeing among themselves on the charge to quote shippers . . . for the inland leg of a foreign door-to-door movement and it clearly frustrates the growth of an innovative, efficient, and economical transportation service."95 This has been a recurring problem since the very first chipping away of antitrust immunity.

91. Id. at 6-7.
92. Note, supra note 12, at 652.
93. S. REP., supra note 20, at 8.
94. Id.
95. Id. at 10.
The need for Shipping Act reform is undiminished. Several problems currently inherent in the industry cry for renewed legislative assistance. Overtonnaging, and the needs for greater efficiency through rationalization and intermodalism, for certainty as to the applicable law, and for speedy federal Maritime Commission decisions on proposed carrier agreements, are several of the more important issues requiring timely attention. A new statutory framework, outlining a new regulatory philosophy, must be established if carriers and shippers are to conduct international trade in a stable, efficient, and fair manner. Domestic rules of competition may be successful in such an environment; however, they have been proven not to work in international liner shipping. Although American-flag carriers have been among the most innovative in the world, they and their customers have often been unable to fully reap the benefits of their progressive operations. Few, if any, maritime nations have anti-trust laws which apply to shipping. When such laws do exist they are not enforced on carriers in the same manner as in this country. This lack of uniformity in philosophy has disadvantaged our carriers and our shippers. We are alone in the world in imposing such a burden on flag companies.

B. PURPOSE

When considering maritime reform, the major goal is a balance between carriers and shippers for the improvement of U.S. flag carriers and shippers in foreign commerce. The need for Shipping Act reform is well documented and undisputed. The Shipping Act of 1984 revises the Shipping Act of 1916 to provide an updated, simplified, more efficient, responsive, and effective regulatory scheme for international liner shipping. The paramount objective of this regulatory scheme is to develop and maintain an efficient and flexible ocean transportation system through commercial means, with minimum government involvement. Congress has gone to great lengths to empower the Shipping Act of 1984 to resolve such problem areas as the inefficiency of current U.S. regulation procedures, the disadvantage U.S. carriers are forced to operate under in contrast to their trading partners abroad, the disparity between the treatment of U.S. flag carriers, and foreign flag carriers at the hands of the U.S. government,

98. See Hearings, supra note 96, at 105 (statement of Albert E. May, V.P., Council of American Flag Ship Operators).
providing all shippers with a viable common carrier service, and maintaining a flexible system with respect to intermodal transportation advancements.\textsuperscript{100} The overall purpose of the Shipping Act of 1984 is to improve the international ocean commerce transportation system of the United States.

\textbf{C. Predecessor Bills}

The Shipping Act of 1984 is the most recent attempt to improve U.S. maritime shipping policy and the ocean liner shipping industry. The Act has its birthright in legislation pondered, reported and debated in Congress for the past five years. The proposed reforms have included formally acknowledging closed conferences and shippers' councils, revising the right of civil litigants to a federal judicial forum, strengthening legal tying arrangements, exempting conference intermodal rates from antitrust restrictions, and promoting basic policy revisions.\textsuperscript{101}

The bills to be considered here are the Ocean Shipping Act of 1980 (Inouye bill),\textsuperscript{102} the Omnibus Maritime Regulatory Reform, Revitalization and Reorganization Act of 1980 (Murphy bill),\textsuperscript{103} the Shipping Act of 1981 (Gorton bill),\textsuperscript{104} and the Biaggi bill.\textsuperscript{105} The approach of the four bills is similar; each expressly granted antitrust exemption to shippers' councils.

In 1980, S. 2585 unanimously passed the Senate. Similar efforts in the House (H.R. 4769 and H.R. 6899) failed to reach a floor vote during the 96th Congress. The following year, H.R. 4374 was introduced along with a comparable Senate bill, S. 1593. If passed, this legislation would have largely rewritten the 1916 Shipping Act.\textsuperscript{106} The House passed H.R. 4374. This act "was the result of a balancing of all interests, the compromise efforts of carriers; the shipping public, the administration and the cooperation of the Merchant Marine and Fisheries Committee and the Judiciary Committee."\textsuperscript{107} Also in the 97th Congress was the first concerted effort to produce an effective piece of legislation by adjusting the differ-

\begin{thebibliography}{99}
\item 100. \textit{Id.} at 1-2.
\item 101. \textit{See Note, supra note 12, at 657.}
\item 102. S. 125, 97th Cong., 1st Sess. (1981); this bill is almost identical to S.2585, 96th Cong., 2d Sess. (1980), which also was introduced by Senator Inouye.
\item 104. S. 1593, 97th Cong., 1st Sess. (1981). The Gorton bill, unlike the other bills considered here, is restricted to activities of ocean common carriers, without providing for non-vessel-operating common carriers. A nonvessel operating common carrier is a middleman who acts as a carrier by arranging for the consolidation of goods to fill a container. In essence, it is a freight forwarder service. \textit{See Note, supra note 12.}
\item 106. \textit{See AST&T Report, supra note 11, at 188.}
\item 107. \textit{See Hearings, supra note 106, at 105} (statement of Peter M. Klein, V.P. and General Counsel of Sea-Land Industries Investments, Inc.).
\end{thebibliography}
ences between H.R. 4374 and S. 1593, introduced by Senators Gorton, Packwood, Stevens, Kasten and Inouye. A compromise agreement of all U.S. flag carriers and major shippers sought to clarify several sections of the Senate bill, primarily those concerning independent action, loyalty and service contracts. These were incorporated into S. 1593 before the bill was reported out of the Senate Committee on Commerce, Science and Transportation. Unfortunately, however, the legislation never reached the full Senate for its consideration prior to adjournment of the 97th Congress.

The Murphy (H.R. 6899), Gorton (S.1593), and Biaggi (H.R. 4374) bills authorized closed conferences. These three bills were intended to permit a broad range of conference activity with little governmental interference, and ultimately to create the kind of conference structure that operates in foreign nations.

The Inouye bill (S. 125) was more limited in its approach than the other three. It sought to shift the burden of proof for only four classes of conference agreements: those that implement intergovernment maritime agreements, conference agreements that allow a right of independent action, agreements that are endorsed favorably by shippers' councils in the relevant trade, and agreements that relate to technical matters. This bill also would have given the FMC the power to grant temporary approval of an agreement without holding a hearing, but only in extraordinary situations. The bill, in addition, stated that failure of the FMC to approve, disapprove, or modify any agreement within eight months of the date of filing would result in automatic approval.

In contrast, the Gorton bill required the FMC to issue a decision within 180 days after filing. If not issued within this time period, the agreement would go into effect as proposed. The bill also shifted the burden of proof to the opponent of the agreement. Similarly, the Biaggi bill shifted the burden of proof to the opponent of the agreement. In addition, the Biaggi bill required the FMC to take action on any proceeding 30 days after the filing of the agreement and issue a final order 180 days thereafter, much the same as the Gorton bill. Unlike the other bills, however, the Biaggi bill did not provide for automatic approval in the event of FMC delay. Therefore, under Biaggi an agreement would not be lawful after the 180 days had run. In this manner, the Biaggi bill was self-contra-

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109. Id.
111. Note, supra note 12 at 658.
112. Id. at 670.
113. Id. at 670-71.
dicting. It placed the burden of proof on the opponent, yet provided that if the FMC failed to take action within the requisite time period the agreement would be unlawful.\textsuperscript{115}

Another paramount concern in the process of validating conference agreements has been the requirement that the FMC consider the competitive effect before granting approval, a requirement imposed by \textit{Svenska}. The Murphy bill eliminated the public interest test required by \textit{Svenska} and substituted a different set of criteria. The test would require an agreement to be consistent with the mandated policy objectives of promoting U.S. foreign commerce, assuring competitive rates in the international market, and realigning U.S. shipping practices with those of foreign nations.\textsuperscript{116} The Gorton and Inouye bills provided for many of the same policy objectives as the Murphy bill. However, like the Murphy bill, neither proposal spoke to the paramount concern for the competitive impact of an agreement, but merely provided for a full exemption from the antitrust laws.\textsuperscript{117} Unlike the others, however, the Inouye bill retains the \textit{Svenska} public interest test,\textsuperscript{118} but because the majority of the agreements would be exempt from the antitrust laws, this test should not result in the interpretational difficulties experiences under \textit{Svenska}.\textsuperscript{119}

Nevertheless, it is generally felt that the Murphy bill was superior to the other bills. By eliminating the public interest standard and granting across the board antitrust exemption, the bill avoids judicial rescission of the exemption. Should the public interest standard be retained, a complainant could be awarded a judgment against a conference carrier for violating the Shipping Act by arguing that the Act incorporated antitrust standards. Taken to its logical conclusion, a complainant could nullify a prior FMC approval.\textsuperscript{120} In contrast, the Biaggi bill included concern for the anti-competitive effect of an agreement. Combined with the tenuous limitation of antitrust immunity, this bill would not have been effective in developing and maintaining an efficient, innovative, and economically sound ocean transportation system.\textsuperscript{121}

\textbf{D. Enactment}

At the onset of the 98th Congress, two things occurred which pro-
duced an optimistic outlook for much needed new legislation: the Senate passed S. 47 and the House Subcommittee on Merchant Marine began considering H.R. 1878. Senators Gorton, Packwood, Stevens, and Inouye introduced S. 47, with Senators Kasten and Trible joining as co-sponsors. As introduced, S. 47 was modeled after S. 1593, but did include provisions which addressed antitrust concerns which had not been incorporated into its predecessor.\(^\text{122}\)

A hearing on S. 47 was called in early February, 1983 by the Senate Committee on Commerce, Science, and Transportation. Testifying before the Committee were proponents of the legislation, which included prominent members of the administration, the FMC, and representatives of small and large shippers and carriers. Issues addressed by the witnesses covered a panorama of potential shipping conference problems: the impact of the legislation on competition in general, ports, small shippers, jobs, balance-of-trade, ocean rate levels, and the adequacy of Federal Maritime Commission regulation and enforcement. Opponents of the bill had claimed that its enactment would raise shipping rates by as much as twenty percent. This figure was never substantiated. On the contrary, the Committee received testimony from shippers who would actually have had to pay the tariffs that enactment of S. 47 could well reduce ocean shipping rates.\(^\text{123}\) In spite of testimony that the bill might work to the detriment of small shippers, several small shippers testified to their own advantages under S. 47.\(^\text{124}\) In support of this, a paper by a representative of American ports refuted claims "that the bill was inimical to ports' interests."\(^\text{125}\) Additionally, there was testimony indicating that penalties under the Shipping Act were substantially less and far more equitable than antitrust treble damage penalties. This appeared to be a point in conflict, as subsequent testimony indicated that potential penalties under the antitrust laws were significantly lower than penalties which could be assessed by the FMC under S. 47.\(^\text{126}\)

**E. Problems With the Act**

Interested parties testifying before the committees expressed concern over the provisions granting carte blanche antitrust immunity to the activities and agreements of carriers, while at the same shifting the burden of proof to those challenging the agreements which, absent the immunity, would violate the antitrust laws or the Shipping Act. The consensus of those testifying to this maintained that entities seeking carte

\(^{122}\) S. Rep., supra note 20, at 14.

\(^{123}\) Id.

\(^{124}\) Id.

\(^{125}\) Id.

\(^{126}\) Id. at 14-15.
blanche immunity from the antitrust laws should at the very least shoulder the burden of justifying their actions and agreements. 127

The testimony indicated that the burden of proof should remain with the carriers seeking exemption, as "they have the primary knowledge concerning the ocean transportation problem which the carrier proponents of agreements contend requires resolution by such exemption." 128 However, lobbyist representatives of the carriers argued strongly in favor of the Committee placing the burden of proof in a proceeding on the party opposing the agreement, including the Commission." 129 In response to the support this proposed change received, the final draft of H.R. 1878 was modified to read exactly as desired by the conferences in the report to the full House (and consistently with S. 47). 130

Aside from reaffirming the conference antitrust provisions of the 1916 Act and establishing judicial guidelines within which the shipping conference may operate, the 1983 Act provides for numerous substantial changes to existing law. It places regulation of international liner shipping under a single law, functioning under a clearly established trade policy administered by a single agency. The Act also:

clarifies and reaffirms the complete antitrust immunity of ocean liner shipping operators engaged in specified collective activities; clarifies authority for conferences of carriers to establish intermodal rates and services and authorizes shippers to form shippers' councils to consult and confer with ocean carriers on general rate levels, rules, practices, or services. Regarding shipping conferences, the Act eliminates preimplementation approval of agreements required to be filed with the FMC. It provides for suspension of agreements, prior to their taking effect, pending review; streamlines procedures for review of agreements. Further, it replaces vague standards of review with a precise list of prohibited acts; sets statutory time limits on Commission action; and places the burden of proof squarely on opponents. In addition, the bill clarifies the authority of carriers to discount rates for shippers moving a specified volume of cargo over a specified period of time and to enter contracts for rates and services subject to common carrier obligations of the Act; and it prohibits certain practices of conferences designed to drive independent carriers from their trades. 131

F. EFFECTIVENESS

The prospects for the Shipping Act of 1984 are optimistic. The Act,

128. Id. at 3.
129. Id.
131. S. REP., supra note 20, at 15-16.
like its predecessor bills, attempts to define those activities which many feel deserve antitrust exemption. It also eliminates the ambiguous approval standards of section 15 which currently exist in the 1916 Shipping Act. Additionally, it replaces current approval procedures with specifically prohibited acts, affirmatively preventing anti-competitive practices. The Federal Maritime Commission has openly supported the prohibitions contained in the 1983 Act as being "realistic assessments of harm which might result from abusive collective activity by competing ocean carriers."  

V. CONCLUSION

Under the Shipping Act of 1916, collective ratemaking and trade practices of carriers were given legal validity, but today such activities encounter problems with antitrust laws. The Shipping Act of 1984 re-establishes the antitrust exemption of ocean carriers. This was manifested by the necessity for a return to legal certainty and permissible operational guidelines. For too long, the shipping industry, and conferences in particular, have been forced to operate in an environment which has been eroding at an accelerated rate. The U.S. shipping industry has been at an uncompromising disadvantage vis-a-vis its foreign counterparts. In order that it might, once again, establish a viable and competitive service the antitrust exemption must be firmly reinstated. The current administration, consistent with its policy of a laissez faire government, is striving to reduce government involvement in the maritime industry. It desires to reduce antitrust limitations in order to bring America's international trade "more in line with the rest of the world."  

Currently, there exists no better means for providing for stability and desired competition in ocean liner shipping than the open conference system. Congress must firmly and expressly sanction adequate protection for this institution through the Shipping Act of 1984, as this is the single most important piece of legislation for the maritime industries of the United States that Congress will deal with for years to come. The proposal is not intended, in one fell swoop, to completely alter the U.S. system. Rather, it is a procedural Act, designed to allow carriers to operate in the manner originally intended by Congress as far back as 1916. Numerous court decisions have limited the functional efficiency of the en-

133. Id.
134. See AST&T Report, supra note 11, at 196.
135. Id. at 191.
136. See Hearings, supra note 127, at 224 (statement of Rep. Edwin B. Forsythe (R-N.J.)).
acted regulatory program by imposing costly hearing requirements, both in terms of economics and timeliness. The FMC's attempts to resolve this dilemma have been sorely lacking. 137 Enactment of the Shipping Act of 1984 should realistically remedy the problem of carrier uncertainty with respect to antitrust immunity and laws, and ultimately, serve to balance the U.S. maritime shipping policy against its foreign competitors.

JOHN GIDUCK

137. See Hearings, supra note 96, at 105 (statement of Albert E. May, V.P., Council of American Flag-Ship Operators).
The Bus Regulatory Reform Act of 1982 and Federal Preemption of Intrastate Regulation of the Intercity Bus Industry; Where Has It Come From? Where Will It Lead?

JEREMY KAHN*

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Thomas Jefferson is generally credited as the author of the phrase that "government is best which governs least." The authors of the Bus Regulatory Reform Act of 1982 [BRRA], at least insofar as the issue of joint Federal-state regulation of the intercity bus industry is concerned, probably had that phrase in mind when they drafted the Federal preemption provisions of the Act. There can be little question that the Interstate

1. The phrase is attributed to Jefferson, but it has never been found in his writings. It is placed in quotations and referred to as a "motto" H. THOREAU, CIVIL DISOBEDIENCE (1849).
Commerce Commission [ICC] in its interpretation and implementation of the Act must have had Jefferson's phrase foremost in its thoughts.

Whatever Congressional intention may have been when it included the several Federal preemption provisions in the BRRA, the implementation of the Act by the Commission has effectively eradicated former state responsibility for the regulation of intrastate regular route bus service, historically one of the more important of the state regulatory functions.

Congressional authorization of the preemption of intrastate regulation by the ICC is based upon well established legal concepts. Though the Federal right to preempt state regulation is nothing new, the actual implementation of the Federal preemption provisions in the BRRA by the Commission is cause for serious questioning by all observers of the bus industry. The extent to which the ICC has used this law effectively to deregulate the intercity bus industry has gone far beyond the hopes and/or fears of those who observed the enactment of this legislation. To the extent that the implementation of such Federal preemption provisions is a presage for future Congressional and Commission action, it is as well a matter of concern for all interested in any form of motor carrier transportation.

I. PREEMPTION PROVISIONS IN THE BUS ACT

To some extent, the BRRA was the bus industry's own version of the earlier Motor Carrier Act of 1980,\(^3\) which Act had altered significantly historic strict Federal regulation of the trucking industry by replacing restrictive regulation with a new emphasis upon increased competition, expansion by existing carriers, and entry by new carriers.\(^4\) The major difference between these two examples of regulatory reform legislation is to be found not in the provisions governing transportation regulation by the ICC—the BRRA carries forward most of the free entry and promotion of competition policies of the MCA—but rather in the explicit recognition that state regulation of intrastate bus service imposed unreasonable burdens upon interstate carriers who also operated intrastate service, and, therefore, state authority to regulate those carriers should be replaced by more "enlightened" Federal regulation.

To reach such a conclusion, one need go no further than Section 3 of

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\(^4\) One of the many cases involving a review of ICC action under the MCA included the observation that:

The principal goals of the legislation . . . are to promote greater competition by allowing easier carrier entry, to simplify and expedite the certification process, and to lessen restrictions on motor carrier operation. Gamble v. ICC, 636 F.2d 1101, 1103 (5th Cir. 1981).
the BRRA which is entitled "Congressional Findings," and which includes within it the observation that:

[H]istorically the existing Federal and State regulatory structure has tended in certain circumstances to inhibit market entry, carrier growth, maximum utilization of equipment and energy resources and opportunities for minorities and others to enter the motor bus industry: [and] that State regulation of the motor bus industry has, in certain circumstances, unreasonably burdened interstate commerce.5

Those Congressional findings led to the decision to carve out a separate portion of the National Transportation Policy, redefined in Section 5 of the BRRA to address the problem that would be solved through the solution of Federal preemption of state regulation. In addition to the platitudes which constitute most of the National Transportation Policy, Congress inserted a new section dealing strictly with passenger transportation:

[I]n regulating transportation by motor carrier of passengers (A) to cooperate with the states on transportation matters for the purpose of encouraging the States to exercise intrastate regulatory jurisdiction in accordance with the objectives of this subtitle; (B) to provide Federal procedures which ensure that intrastate regulation is exercised in accordance with this subtitle; and (C) to ensure that Federal reform initiative enacted by the Bus Regulatory Reform Act of 1982 are not nullified by State regulatory action.6

The Federal-state "cooperation" promised in Part (A) to "encourage" the states to follow the Federal lead is revealed in Part (B) and especially in Part (C) to be little more than a cudgel to bring into line those states which for reasons of their own otherwise would not have seen the wisdom of the Federal deregulation scheme and welcomed it with open arms.

Rather than treat each of the Federal preemption provisions in the BRRA in the order that they have been placed in the Act itself, it is illustrative to begin with Section 17 of the Act. Section 17 is entitled "Discriminatory State Regulation of Rates and Practices," and as the title indicates this section and its specific provisions illustrate much of the Federal philosophy of preemption. Section 17(d) of the BRRA states in no uncertain terms:

It is the sense of Congress that each state should revise its standards and procedures (including timing requirements) for rates, rules, and practices applicable to intrastate transportation provided by motor common carriers of passengers so as to conform to such standards and procedures for rates, rules and practices as are applicable to interstate transportation provided by such motor carriers of passengers not later than 2 years after the effective

5. BRRA, supra note 2, § 3.
6. BRRA, supra note 2, § 5 (codified at 49 U.S.C. § 10101(a)(3) (1982)). That portion of the National Transportation Policy dealing with motor carrier transportation in general, in subsection (a)(2), was also modified to include reference to "passengers" and "consumers" in addition to the former reference to "shippers" and "receivers".
date of this section.\textsuperscript{7}

Section 17 establishes specific provisions limiting the right and the
ability of states to continue to regulate the central element of intrastate
bus transportation “by a motor carrier of passengers providing transport-
ation subject to the jurisdiction of the Commission.”\textsuperscript{8} Under the estab-
lished procedures, an intrastate carrier with some claim to status as an
interstate carrier\textsuperscript{9} does have the obligation to make a request concerning
any rate, rule, or practice first to the appropriate state regulatory agency.
If the state agency “has not acted finally (in whole or in part)” within 120
days of the filing, the carrier can (and in practice usually does) immedi-
ately turn to the ICC to appeal the state action or inaction. The ICC must
take “final action” on any such request not later than 60 days after the
filing\textsuperscript{10}, in effect creating a 180 day period within which the carrier is as-
sured of a final decision regarding its request.

That decision, under the presumptions imposed by the BRRA, is gen-
erally favorable.\textsuperscript{11} It is presumed that the challenged state practice im-
poses an unreasonable burden upon interstate commerce if the ICC finds
that:

\begin{enumerate}
\item [T]he carrier will be charging a lower rate for intrastate transportation
than that for interstate transportation;
\item the carrier does not receive revenues exceeding variable costs for pro-
viding such transportation;
\end{enumerate}

\begin{flushleft}
\textsuperscript{7} BRRA, supra note 2, \S 17(d), not codified, note following 49 U.S.C. \S 11501 (1982). In
Section 19 of the MCA, supra note 3, under the title “Uniform State Regulations,” the sense of
Congress was expressed as follows:
Congress hereby declares and finds that the individual State regulations and require-
ments imposed upon interstate motor carriers regarding licensing, registration, and fil-
ings are in many instances confusing, lacking in uniformity, unnecessarily duplicative,
and burdensome, and that it is in the national interest to minimize the burden of such
regulations while at the same time preserving the legitimate interest of the State in such
regulation. (emphasis added).
The BRRA does not express the same concern for the rights of the states.
\textsuperscript{8} BRRA, supra note 2, \S 17 (codified at 49 U.S.C. \S 11501(e) (1982)). Regulations imple-
menting this Section appear at 49 C.F.R. \S 1143 (1983). See also Procedures For Review of
Intrastate Bus Rates, 133 M.C.C. 10 (1982) and Procedures for Review of Intrastate Bus Rates,
133 M.C.C. 47 (1983).
\textsuperscript{9} There may be some question as to who is and who is not a qualifying carrier. For
example, must the intrastate and interstate routes be identical for this section to apply? See text
accompanying note 59, infra.
\textsuperscript{10} BRRA, supra note 2, \S 17 (codified at 49 U.S.C. \S 11501(e)(3)(A) (1982)).
\textsuperscript{11} This writer is unaware of any cases in which the petitioning carrier has been unable to
receive permission from the ICC to achieve the desired results on the merits of its case. Nume-
rous examples are cited in the text. One close observer of the bus industry found that as of
October 14, 1985, carriers had filed 62 such petitions. Sixty were approved; two were denied on
procedural grounds; one was pending. Testimony of Norman Sherlock, President, American
Bus Association, before the Surface Transportation Subcommittee, House Committee on Public
Works and Transportation, U.S. House of Representatives, October 22, 1985. The few “unfavor-
able” ICC decisions were rendered on procedural grounds. See note 52, infra.
\end{flushleft}
(3) the state agency hasn’t acted (in whole or in part) within 120 days of the carrier’s request;
(4) the carrier’s intrastate rates are less than those of other interstate carriers operating within that state, despite the application of recent general rate increases.\textsuperscript{12}

Although the foregoing presumptions are described by Congress as "rebuttable," no state has yet been successful in challenging such presumptions, regardless of the evidence that it has amassed and presented.

Also included in Section 17 is a provision that specifically prohibits states or political subdivisions from imposing any rules or regulations pertaining to scheduling or fare reductions on intrastate service over interstate routes (excluding commuter operations).\textsuperscript{13}

Of equal importance to the bus industry is Section 16 of the BRRA, which established a new section of law, 49 U.S.C. § 10935. This Section imposes a significant burden upon those seeking to block a discontinuance or reduction of regularly scheduled service. A request for a discontinuance will not be granted if evidence is presented which shows "that such discontinuance or reduction is not consistent with the public interest or that continuing the transportation, without the proposed discontinuance or reduction, will not constitute an unreasonable burden on interstate commerce" for interstate route authority awarded prior to the BRRA. For those carriers awarded regular route authority following the enactment of the BRRA, objectors to the discontinuance must show that "continuance of the transportation would not constitute an unreasonable burden on interstate commerce." This objector’s burden can be met "only if discontinuance or reduction of such transportation is not consistent with the public interest and the interstate and intrastate revenues from such service under reasonable pricing practices are not less than the variable costs of providing the transportation proposed to be discontinued or reduced."\textsuperscript{14}

This portion of the law also includes a time frame within which the ICC must issue a final decision.\textsuperscript{15} Section 16 includes a prohibition di-

\textsuperscript{12} BRRRA, supra note 2, § 17 (codified at 49 U.S.C. § 11501(e)(2) (1982)). This section has been interpreted most thoroughly in Commissioner of Transp. v. United States, 750 F.2d 163 (2d Cir. 1984), cert. denied, 105 S. Ct. 2019 (1985). See text accompanying note 34, infra.

\textsuperscript{13} BRRRA, supra note 2, § 17 (codified at 49 U.S.C. § 11501(e)(5) (1982)).


\textsuperscript{15} Under this section, the state is permitted 120 days within which to act. If it does not act and the carrier petitions the ICC, the Commission must issue a final decision within 90 days. In any event, for a discontinuance or reduction in service, the ICC may order the carrier to continue intrastate transportation for a period not to exceed 165 days, beginning on the date the carrier files its petition with the ICC.
rected to states and political subdivisions against instituting discriminatory regulations similar to those mentioned in Section 17 of the Act.\textsuperscript{16}

The other major preemption provision appears in Section 6, the "entry" section of the BRRA. Here, the ICC may issue a certificate authorizing the provision of regular route transportation entirely in one state where the applicant has held interstate authority over the same route at the time of the enactment of the BRRA.\textsuperscript{17} The ICC may also issue a certificate if such interstate authority is to be issued following the effective date of the BRRA.\textsuperscript{18}

Additional provisions of Section 6 address the carrier's obligations under intrastate authority issued by the ICC. Generally, such transportation "shall be deemed to be transportation subject to the jurisdiction of the ICC," although the carrier must also comply with various state requirements.\textsuperscript{19} A carrier has an opportunity for relief from requirements when they become an "undue burden on interstate commerce."

The "restriction removal" section of the BRRA\textsuperscript{20} does not explicitly remove restrictions from intrastate regular route certificates by removing intermediate point restrictions from interstate certificates. The BRRA does nonetheless effectively eliminate the "closed door" problem identified by Congress.\textsuperscript{21}

The foregoing provides a backdrop to the BRRA's operation. The BRRA allows Federal preemption of state regulation while providing an opportunity for the states to refute the presumptions appearing in the Bus

\textsuperscript{16} BRRA, supra note 2, § 16 (codified at 49 U.S.C. § 10935(h) (1982)).

\textsuperscript{17} BRRA, supra note 2, § 6 (codified at 49 U.S.C. § 10922(c)(2)(A) (1982)). Regulations implementing this Section appear at 49 C.F.R. § 1168 (1982). See also, Applications for Operating Authority—Motor Passenger Carriers, 133 M.C.C. 62 (1982). The breadth of this Section was interpreted by the ICC in Funbus Systems, Inc.—Intrastate Operations—Petition for Declaratory Order No., MC-C-10917 (i.c.c. served Jan. 8, 1985).

\textsuperscript{18} BRRA, supra note 2, § 6 (codified at 49 U.S.C. § 10922(c)(2)(B) (1982)). Regulations implementing this Section appear at 49 C.F.R. § 1160.70 et seq. See also, Applications for Operating Authority, supra note 17.

\textsuperscript{19} BRRA, supra note 2, § 6 (codified at 49 U.S.C. § 10922(c)(2)(D), (E), (F) (1982). The carrier first establishes "initial rates, rules, and practices" applicable to the intrastate transportation under ICC standards. No later than 30 days after the carrier begins to provide intrastate transportation, it must "take all action necessary to establish under the laws of such State rates, rules, and practices applicable to such (intrastate) transportation."

\textsuperscript{20} BRRA, supra note 2, § 7 (codified at 49 U.S.C. § 10922(i)(4) (1982)). Regulations implementing this Section appear at 49 C.F.R. 1165. See also, Removal of Restrictions from Authorities of Motor Carriers of Passengers—Intermediate Points, 133 M.C.C. 35 (1982).

\textsuperscript{21} S. Rep. No. 411, 97th Cong., 2d Sess. 9 (1982) reprinted in 1982 U.S. Code Cong. & Ad. News. [hereinafter cited as Senate Report]. An additional State barrier causing economic difficulties for carriers has been the "closed door" policy. Frequently, carriers operating under interstate certificates have been denied authority to pick up or drop off passengers traveling between intrastate points over the carrier's interstate route.
Act. Challenge of the rebuttable presumptions thereby allows the states to maintain a semblance of state regulation. The backdrop before which all of this is to take place is none too subtle; in the terms of the statute, the "action of the Commission under this section [ICC authority over intrastate transportation] supercedes State law or action taken under State law in conflict with the action of the Commission." Assuming, at first, that the ICC’s regulatory powers under the BRRA are exercised reasonably, the most interesting question raised regarding Congressional delegation of such broad powers over intrastate regulation to the ICC seems to be "Can they do that?"

II. CONGRESSIONAL POWER TO PREEMPT CERTAIN STATE REGULATION OF INTRASTATE TRANSPORTATION

Congressional power to delegate authority to the Interstate Commerce Commission so as to allow the ICC to preempt state regulation of intrastate activities is vast and well grounded in precedent. The only remaining issue of interest in this area is the definition of the outer limits of that power. Congressional power under the Commerce Clause of the Constitution knows very few limits.

The Federal preemption provisions of the BRRA have seemingly been drawn with great care to stay well within the permissible limits of Congressional delegation of such power. As the past is generally prologue, so is the history of Federal preemption of state regulation of intrastate transportation prologue to the provisions of the BRRA.

To approach this issue from an historical perspective one must begin with the Shreveport Rate Case of 1914. In Shreveport, the Supreme

22. For rate preemption under § 17 of the BRRA, "the State could, however, protest at the ICC and argue that the State action was reasonable." Senate Report, supra note 21, at 28.


24. It is well known that the reasonable exercise of discretion by an agency interpretation of facts under the appropriate enabling statutes will not be upset by judicial review. See generally, 5 B. MEZINES, J. STEIN, J. GRUFF, ADMINISTRATIVE LAW, ch. 51 (1984). The Commission's exercise of its powers under the BRRA is described in Section III infra. In the eyes of almost all courts called upon to review the ICC's actions, the ICC has exercised the powers bestowed upon it in a reasonable manner.

25. This question is borrowed from the title of a well known ICC publication of an earlier era of regulation, "Hot or Exempt, Can They Do that?" (On file in office of the Transportation Law Journal)

26. U.S. Const. art. I, § 8 cl. 3, provides Congress shall have the power "to regulate commerce with the foreign nations and among the several States . . . ." The limits of the vast Congressional power to preempt state regulation of intrastate commerce are explored in this section of the article.

Court dealt with a rail rate case prior to any statutory basis for ICC pre-emption of state regulation. The only intrusion into state regulation that existed at the time was a general prohibition in the Interstate Commerce Act [ICA] against unjust and unreasonable rates. The argument was raised by the challenging party "that Congress is impotent to control the intrastate charges of an interstate carrier even to the extent necessary to prevent injurious discrimination against interstate traffic." 28

The Court's resolution of the issue flowed from an identification of "the complete and paramount character of the power conferred on Congress to regulate commerce among the several states," a power so great that "It is of the essence of this power that, where it exists, it dominates." 29

Congressional power to regulate intrastate commerce, according to the 1914 pronouncement by the Court, was vast. 30 Wherever the interstate and intrastate transactions of carriers are so related that the government of the one involves the control of the other, it is Congress and not the state that is entitled to prescribe the final and dominant rule, for otherwise Congress would be denied the exercises of its constitutional authority, and the state, and not the nation, would be supreme within the national field... 31 This is not to say that Congress possesses the authority to regulate the internal commerce of a state, as such, but that it does possess the power to foster and protect interstate commerce, and to take all measures necessary or appropriate to that end, although intrastate transactions of interstate carriers may thereby be controlled. 32

The language of Shreveport is quite compelling, particularly where the intrastate activity has an apparent effect on interstate commerce. 33

28. Id. at 350.
29. Id. at 350. "[C]ongress, in the exercise of its paramount power, may prevent the common instrumentalities of interstate and intrastate commercial intercourse from being used in their intrastate operations to the injury of interstate commerce."
30. Id. at 351.
31. Id. at 351-52.
32. Id. at 353.
33. Not everyone necessarily agrees. In challenging ICC decisions under the BRRA, several states have conceded that the ICC has jurisdiction, although they argue on the basis of the doctrine of North Carolina v. United States, 325 U.S. 507, 511 (1945), in which it was stated that Congress can preempt state regulation, but the justification for the use of federal power "must
When *Shreveport* is considered in light of one of the more recent appellate court decisions in the area, that of *Texas v. United States*\textsuperscript{34} it appears that *Shreveport* was only the tip of the iceberg. The *Texas v. United States* case deals with a new challenge to the Staggers Rail Act of 1980\textsuperscript{35} which, according to the reviewing court, instituted "a major reallocation of regulatory authority between the Federal and State governments."\textsuperscript{36} This major reallocation whose propriety was strongly affirmed by the court is significant in that it constituted a departure from the previous "division of regulatory jurisdiction between the ICC and the states [in which] the ICC exercised the role of limited review over intrastate rate-setting."\textsuperscript{37} Prior to Staggers, ICC jurisdiction over intrastate rates was called into play only where "a rate, classification, rule or practice established by a state regulatory agency caused unreasonable discrimination against or an unreasonable burden on interstate or foreign commerce," or when a rail carrier had filed for an intrastate rail increase and the state authority did not act on the proposal within 120 days of the filing.\textsuperscript{38}

The *Texas v. United States* case before the 5th Circuit Court involved the Staggers Act preemption concept which effectively completely eliminated state regulation of intrastate rail service where interstate transportation is by any stretch of the imagination involved, unless the state agreed (and the Commission believed it) to regulate intrastate rail rates and practices according to ICC policies. The analysis used by the Court in upholding this far-reaching Federal preemption provision illustrates on just how strong a footing the Bus Act preemption provisions rest.

Where Congress acts under the Commerce Clause a reviewing court has a limited role. Under the accepted analysis, "the court must defer to a Congressional finding that a regulated activity substantially affects inter-

\textsuperscript{34} State of Texas v. United States, 730 F.2d 339 (5th Cir. 1984), cert. denied 105 S. Ct. 267 (1984).


\textsuperscript{36} *Texas v. United States*, 730 F.2d at 345.

\textsuperscript{37} *Texas v. United States*, 730 F.2d at 348.

\textsuperscript{38} *Id.* The statutory provisions in the Interstate Commerce Act formerly appeared at 49 U.S.C. § 11501(b)(1) (1982) before they were amended by the Staggers Act. The "unreasonable discrimination" and "unreasonable burden" terminology is, in effect, a codification of *Shreveport*, supra note 28.
state commerce as long as there is any rational basis for such a finding.\textsuperscript{39}

The \textit{Texas v. United States} court was aided in its identification of the necessary "rational basis" by finding that the information presented to Congress during the formulation of the Staggers Act warranted the pre-emption policy that was adopted, and further, there was clearly "a reasonable connection between the regulatory means chosen—preemption of independent state regulation—and the asserted objective."\textsuperscript{40}

With respect to the BRRA, Congress had before it specific examples of overburdensome state regulation. Specific examples of this included: unopposed intrastate rate increase proceedings which were held without hearings (one hearing lasted 245 days and another lasted 359 days); taking 4 years to unsuccessfully prosecute an intrastate application to remove a "closed door" restriction; and evidence of a general level of intrastate rates that were 30\% to 40\% below that of comparable interstate rates.\textsuperscript{41} The means of achieving the desired results—regulation of intrastate carriers which already held interstate authority—was clearly a logical one, and one thoroughly established in the philosophy of transportation regulation. Moreover, the means used were those in which the "rational basis" for finding an effect on interstate commerce was readily satisfied by virtue of the existence of an interstate certificate.

Following the court's analysis in \textit{Texas v. United States} would logically result in virtually an automatic affirmation of the Congressional delegation of power for intrastate regulation under the BRRA, on the basis of the \textit{Shreveport} analysis. Such a result follows, since the choice of regulating only that portion of intrastate transportation over an interstate route, which effectively gives states the right of first refusal to regulate in an enlightened manner, seems to satisfy all of the \textit{Shreveport} requirements. However, the BRRA preemption is on even stronger footing. The \textit{Shreveport} analysis is far too narrow when read in terms of a modern analysis of the Commerce Clause. In the words of the 5th Circuit, "For over forty years now, the Supreme Court has held that a purely intrastate activity may be regulated by Congress as long as the cumulative effect of the activity substantially affects interstate commerce."\textsuperscript{42}

In response to the petitioner's argument seeking to limit the reach of the Staggers Act, the \textit{Texas v. United States} Court concluded, "It is sim-

\textsuperscript{39} Id. at 340.
\textsuperscript{40} The Staggers Act, as enacted, has been termed a "compromise," in which Congress rejected an initial attempt to oust states from any regulatory role. \textit{Utah Power & Light}, 747 F.2d 721, 733. Congress has yet to see just how far it might reach under the "rational basis" test.
\textsuperscript{41} Senate Report, \textit{supra} note 2, at 8-10.
\textsuperscript{42} \textit{Texas v. United States}, 730 F.2d at 349. (Citing 
Hodel v. Virginia Surface Mining and Reclamation Ass'n., 452 U.S. 264, 276-77 (1981)).
ply not true that Congress can regulate intrastate commerce only to pro-
tect interstate commerce from unreasonable burdens."43 Congress can,
if it so desires, regulate any transportation activity remotely connected
with interstate commerce.44

The remainder of the Texas v. United States case dealt with the imag-
inative arguments used by the plaintiffs to attack the expanded preemp-
tion provisions of the Staggers Act. Such "new" preemption provisions
are a departure from the earlier, accepted provisions.45 The earlier pro-
visions are analogous to the provisions that were carried forward into the
BRRA. Thus, there seems to be little doubt that Congress can delegate
power to the ICC to regulate intrastate transportation in some instances.

A carrier seeking to take advantage of ICC procedures must comply
with certain requirements before it can come before the ICC. The carrier
must comply with the following: it must be an interstate carrier; must first
go to the state regulatory agency governing the intrastate transportation
to be performed; and must provide an opportunity for the state regulatory
agency to oppose the relief requested by the carrier from the ICC. All of
these provisions are such important safeguards under this type of Federal
preemption statute that they certainly would preclude a challenge to the
claim of improper Congressional delegation of power.46 Further, the
Texas v. United States court concluded:

[Under the Commerce Clause], Congress exercises a power that "is com-
plete in itself, may be exercised to its utmost extent, and acknowledges no
limitations, other than are prescribed in the Constitution." Gibbons v.
Ogden, 1824 22 U.S. (9 Wheat.) 1, 196, 6 L. Ed. 23. Because of the plenary
nature of the commerce power and because of the primacy accorded federal
law by the supremacy clause, the balance of interests between the federal
and state governments is an inappropriate consideration in determining
whether a federal act is a valid exercise of the commerce power.47

Congress, has the power to delegate; it has seemingly delegated
power to the ICC with deference to the legitimate interests of the states in
regulating purely intrastate transportation which has no effect on interstate
commerce. Under the appropriate delegation, how has the Commission
implemented its preemption powers under that legislation?

43. Texas v. United States, 730 F.2d at 350.
44. Id. at 350 n. 19. "The only activities that are beyond the reach of Congress are, those
which are completely within a particular state which do not affect other states, and with which it is
not necessary to interfere, for the purpose of executing some of the general powers of the
government."
45. See text accompanying note 38, infra.
46. Id.
47. Texas v. United States, 730 F.2d at 351.
III. ICC PREEMPTION IN THE INTRASTATE RATE AREA

The greatest number of petitions to the Interstate Commerce Commission arising out of the Federal preemption provisions contained in the BRRA are those concerning requests to raise intrastate rates. This is not altogether surprising given the litany of problems that carriers experienced when they sought to raise intrastate rates under the prior dichotomy that characterized Federal-state regulations. According to the Senate report accompanying the BRRA, major passenger carriers (Greyhound in particular) continued to apply for intrastate rate increases despite significant delays encountered in the prosecution of such requests. At the same time, some of the smaller carriers experienced a "chilling effect," deciding that the voluminous data and great expenditures of time required successfully to prosecute an intrastate rate increase coupled with the likelihood of achieving only limited relief was a greater cost than the benefit of ultimately raising intrastate rates. Presented with the apparent invitation to raise intrastate rates to the level of or close to those of interstate rates, a number of carriers first submitted their application to the regulatory agency of the state in which intrastate operations were being conducted and then immediately petitioned to the ICC to seek some parity between intrastate and interstate rates.

Section 17 of the BRRA established the procedure for raising intrastate fares without regard for the recalcitrance traditionally exhibited by many states regulatory agencies. Although the statute seems to include a number of limitations and at least suggests that the results of a carrier's appeal of a state action to the ICC is not a foregone conclusion, to the best of this writer's knowledge, no request for the ICC to raise intrastate rates under 49 U.S.C. § 11501(e) has been denied. What appeared in

48. By October 1985, 46 interstate exit petitions had been filed, compared to 62 intrastate rate petitions, supra note 11.
50. Senate Report, supra note 21, at 10. One study found that on a per mile basis intrastate fares were at least 30% lower than comparable interstate fares. "An Analysis of Intercity Bus Fares Under Varying Competitive Conditions" U.S. Department Research and Special Programs Administration, Transportation Systems Center.
51. BRRA, supra note 2, pertinent provisions enacted as 49 U.S.C. § 11501(e) (1982). It might be said more accurately that these procedures were enacted with full regard for the recalcitrance historically exhibited by the states.
52. In at least one instance, a carrier's petition for review was dismissed for being premature. The carrier's initial request to the state resulted in the issuance of a final action at least 3 months prior to the effectiveness of the BRRA. Peter Pan Bus Lines—Massachusetts Dept. of Pub. Util., No. MC-C-10848 (I.C.C. served May 12, 1983) [hereinafter cited as Peter Pan—Massachusetts]. Peter Pan ultimately returned to the ICC and was awarded the intrastate increase it sought. Peter Pan Bus Lines Review of a Decision of the—Massachusetts Dept. of Pub. Util. No. MC-C-10908 (I.C.C. served June 5, 1984). In another instance, a request was denied for lack of jurisdiction, because the carrier didn't provide the minimum information required under the
the statute to be limitations upon the preemptive power of the ICC under this section of the law has in practice proven to be non-existent.

A random sampling of ICC decisions dealing with intrastate rate appeals highlights some of the issues being considered by the ICC when such appeals first came before that agency. A threshold jurisdictional issue is a determination of those carriers who can take advantage of the invitation to appeal an unfavorable state decision to the ICC. The statute provides that this relief is available to any "motor common carrier of passengers providing transportation subject to the jurisdiction of the Commission under subchapter II of chapter 105 of this title." It would certainly seem that this relief is limited only to those carriers conducting regular route transportation subject to ICC jurisdiction, although this issue does not seem to have been raised. It is clear that despite the extent of the supplicant's interstate activities, even the most minimal interstate service over an intrastate route will result in the ICC's taking jurisdiction of the matter. In one case seeking review where the evidence established that state's rules for filing a rate increase, Greyhound Lines—Missouri Pub. Serv. Comm'n, No. MC-C-10851 (I.C.C. served May 26, 1983) [hereinafter cited as Greyhound—Missouri]. The decision was ultimately vacated and the matter dismissed pursuant to court remand in Greyhound Lines, Inc. v. United States, No. 83-7704, (9th Cir. entered April 10, 1984), (decision of ICC served May 31, 1984). See also, American Bus Association Statistics, supra note 11.


54. In an extreme case for example, a carrier which had provided local intrastate regular route service may provide interstate charter and tour service. The jurisdictional threshold of the ICC would presumably have been satisfied, although comparing intrastate regular route rates with interstate charter rates might prove to be an insurmountable burden. Given the ICC's receptivity to granting relief, filing such a petition might be worth the effort. In fact the ICC ultimately granted an increase in intrastate charter rates to carriers conducting interstate regular route (and charter) operations. Greyhound Lines—Railroad Comm'n. of Texas, No. MC-C-10893 (I.C.C. served February 21, 1984) [hereinafter cited as Greyhound—Texas] and Trailways Lines—Railroad Comm'n. of Texas, No. MC-C-10891 (I.C.C. served January 31, 1984) [hereinafter cited as Trailways—Texas]. These awards of intrastate charter authority were affirmed in Texas v. United States, 761 F.2d 211 (5th Cir. 1985).

55. The statutes providing for the ICC's award of intrastate regular route authority over interstate routes speak in terms of "authority" and not in terms of service. 49 U.S.C. § 10922(c)(2)(A)(B). Since a carrier is required to publish the rates it charges over its authorized routes, 49 U.S.C. § 10761(a), and since the ICC has held "that published tariff rates afford an appropriate basis for an effective rate comparison as contemplated by subsection 11501(e)(2)(A)(i)." Kerrville Bus. Co.—Railroad Comm'n of Texas, No. MC-C-10909 at 4 (I.C.C. served November 28, 1984) [hereinafter cited as Kerrville—Texas] the argument is compelling that bare ICC authority, without the performance of interstate service, nonetheless confers ICC jurisdiction over intrastate rates. However, in a recent decision, the ICC claimed a lack of jurisdiction to review a state's denial of a request for an intrastate rate increase. The ICC found that the carrier "makes reference to being an intrastate carrier, but makes no reference to any continuing interstate service or any interstate authority it holds," and concluded that the carrier "is solely an intrastate carrier of passengers [and] therefore, State ratemaking authority over the intrastate rates of this carrier was not affected by the Bus Act." Bloom Bus Lines—Massachusetts Dept. of Pub. Util., No. MC-C-10979 at 2 (I.C.C. served November 21, 1985). This may well be an isolated instance which arose only because an affiliate carrier, not petitioner, was
perhaps as much as 90% or more of the petitioning carrier’s revenues were the result of intrastate commuter operations, (and in fact, all interstate route operations were conducted wholly within that state) the Commission observed:

There is nothing in the statute or legislative history to indicate that Congress intended any different treatment under 49 U.S.C. 11501(e)(1) for interstate carriers who are also engaged in intrastate commuter operations than for interstate carriers who are engaged in non-commuter intrastate operation. Accordingly, the fact that petitioner may be engaged in substantial commuter operations is irrelevant here.56

Another significant issue raised by the terms of the statute itself is a determination of what is “comparable interstate transportation” as compared to the intrastate transportation which is the subject of the rate increase. The most frequently used (and the one beyond which the ICC has not proceeded in granting all petitions submitted to it) of the rebuttable presumptions in the statute is that intrastate rates are lower than the rate the carrier charges for comparable interstate transportation.57 The ICC has gone to great lengths to include most regular route transportation as “comparable” to interstate transportation for purposes of the rebuttable presumption. This is not altogether surprising since the Senate report cited a number of comparisons of the disparity between interstate and intrastate fares, many of which were based on comparable distances rather than identical routes.58

In practice, the concept of “comparable” interstate routes has been quite broadly defined by the Commission, which has not limited the com-

performing interstate services. An interesting twist illustrating the extent of the ICC’s perceived jurisdiction occurred in Greyhound Lines—Nebraska Pub. Serv. Comm’n.—Proposed Intrastate Newspaper Rate Increase, No. MC-C-10933 (I.C.C. served September 4, 1984). The ICC’s jurisdiction over this petition was never questioned, apparently because 49 U.S.C. § 10922(e)(4) (1982) provides, in part, [that] “A certificate of a motor common carrier to transport passengers shall be deemed to include permissive authority to transport newspapers, . . . .” The request to raise intrastate newspaper rates was granted. Requests by Greyhound and Trailways to increase intrastate package express rates were also approved readily by the ICC. See Greyhound—Texas and Trailways—Texas, supra note 54, and affirmed by the Court in Texas v. United States, 761 F.2d at 211. The jurisdiction issue was never raised in these cases either.

56. Plymouth & Brockton St. Ry. Co.—Massachusetts Dept. of Pub. Util., No. MC-C-10887 at 4-5, (I.C.C. served December 27, 1983) [hereinafter cited as Plymouth & Brockton—Massachusetts]. This case is also illustrative as one of the few self-imposed limits on ICC jurisdiction. The local Massachusetts Bay Transit Authority [MBTA] initially claimed jurisdiction over a portion of the intrastate route and applicable rates. The ICC decision denied the requested relief “to the extent such [proposed] fares are outside [the D.P.U.’s] jurisdiction,” whatever that might ultimately turn out to be. Id. at 5. Since the ICC claimed a formal request had not been presented to the MBTA, rather than appeal the ICC decision claiming a lack of jurisdiction, the more prudent course for the practitioner was to file a new petition on the basis of the Transit Authority’s inaction after the 120 day statutory period had expired.


58. Senate Report, supra note 21, at 9.
parison to identical routes. The Commission held that: "The rebuttable presumption in the statute does not require comparison of intrastate rates with interstate rates between the same two points but only for comparable interstate transportation." 59

Another issue surrounding the application of the rebuttable presumption is the rate which a carrier is charging. In comparing interstate with intrastate rates, the ICC is interested in only the ordinary, regular route rate. In its initial policy, the ICC stated it will not "take into account excursion fares and other discounts applicable to a petitioner's interstate rate structure." 60 The Commission's rationale for that reasoning was expressed in the following terms:

Promotional-type discount...ceiling fares or rates for certain qualifying traffic are generally initiated for promotional or advertising purposes and are frequently effective only for limited time periods. Therefore, we have concluded that such reduced rate options should generally not be considered in making comparisons under Section 11501(e)(2)(A)(i). 61

Although the ICC was ultimately directed by the court on appeal to consider the rates actually being charged, the court criticized the ICC's policy of completely ignoring excursion fares. The court concluded that, "The application of the [ICC's] policy in actions such as these results in a comparison of rates that does not necessarily reflect the actual rates charged." 62 Presumably, once the ICC considers these excursion fares, it will be accorded some latitude in finding the inevitable burden on interstate commerce.

Although there are other qualifications present in the preemption statute, petitioning carriers generally need to go no further than to demonstrate that an appropriate petition was filed with the state 63 and to show a

59. Bonanza Bus Lines—Rhode Island Pub. Util. Comm'n., No. MC-C-10886 at 2 (I.C.C. served December 12, 1983). In Texas v. United States, 761 F.2d at 211, the court affirmed the ICC's practice of seeking a comparison of rates for service over comparable distances, recognizing that per mile revenues for short trips are inevitably higher than those for longer trips, because of "the influence of costs of ticketing, baggage handling, other station expenses, and other expenses which do not vary significantly (or at least not proportionally) with the length of the trip." Texas v. United States, 761 F.2d at 216 (quoting Greyhound Lines, No. 10921, at 3) (I.C.C. served April 18, 1984) aff'd sub nom. Public Serv. Comm'n. of West Virginia v. ICC, 749 F.2d 32 (4th Cir. 1984).

60. Trailways—Texas, MC-C-10891 at 6.

61. Id. at 217. The Trailways—Texas decision resulted in a strong dissent by Chairman Taylor arguing that the facts in this case showed that Trailways made its arguments on published rates, but it was in fact "charging" lower intrastate rates, and that the rates actually being charged should apply. (Taylor, dissenting in part) (served January 22, 1984).


63. In Trailways—Texas, the argument that Trailways did not file a separate state petition and therefore could not appeal the Texas decision was promptly dismissed by the ICC. The ICC dismissed this argument in part because Trailways had actively participated in the case in ac-
disparity between intrastate and interstate rates. After those steps have been completed, success at the ICC is virtually assured.

Many states have devised a number of imaginative defenses against the carrier petitions for review that are directed to the ICC. The result is the same regardless of the defense; if intrastate rates are lower than comparable interstate rates, there is an undue burden on interstate commerce. The state has not overcome the “rebuttable presumption,” and the full intrastate increase is allowed by the ICC.

In both earlier and in more recent decisions, the Commission has consistently decided that it need not go beyond a comparison of interstate and intrastate rates. In its most recent decisions, with more than a year and a half of precedent behind it, the Commission has adhered to its interpretation of the BRRA, granting numerous requests with the same expressed rationale.64

cordance with state procedures. Perhaps the philosophy expressed in the following quotation gives the best view of the Commission’s view of this issue:

We can discern no valid reason for requiring the parties to repeat the process simply because Trailways did not technically file its own separate application. Such an approach would also be costly and time-consuming and not in the interest of the parties, this Commission or the public. Accordingly, we conclude that Trailways has requested permission from the [Texas Railroad Commission] to establish a rate and, because its request was partially denied, its petition is properly before the Commission.

Id. at 5.

In another case involving the recalcitrant Texas Railroad Commission, [TRC], the ICC held that even though the petitioning carriers had not presented rate comparison evidence to the state, but only introduced it in the ICC proceeding, the relief sought by the carriers would be granted. The ICC reasoned that since the statutory presumption concerns the effect of a difference in rates, not the reasons for the difference, carriers could present the ICC evidence of rate comparisons not required at the state level. *Kerville Bus—Texas*, No. MC-C-10979 at 4. It appears that so long as a carrier presents probative evidence to the state concerning the disparity between interstate and intrastate rates, it has met the burden of going to the state, even if the carrier does not present all the evidence the state might require. Another requirement is being certain to file a request with any state agency with any possible jurisdiction over intrastate rates and to name all such agencies in the ICC petition for review. *Plymouth & Brockton—Massachusetts*. In the area of rail preemption a carrier may petition the ICC to review a state administrative proceeding. The doctrine of “exhaustion of administrative remedies” has been raised as a defense, although without success. *Utah Power & Light*, 747 F.2d at 727-29. Since the BRRA includes a specific time limit as part of its jurisdictional standard, the doctrine of exhaustion of administrative remedies would seem to have no application in petitions under the Bus Act.

64. *Subsection 11501(e)(2)(A)(i)* established a rebuttable presumption that a prescribed rate, rule, or practice applicable to interstate transportation of passengers unreasonably burdens interstate commerce if it results in the carrier charging an intrastate rate which is lower than the rate applicable to comparable interstate service. The record clearly establishes that intrastate regular-route passenger fares, even at the proposed level, are significantly lower than comparable intrastate fares and that [Petitioner’s] other proposed intrastate rate would merely equal comparable interstate rates and charges. Protestants have not shown any difference in operating conditions, services or costs between intrastate and interstate operations which would justify the disparity in applicable fares and rebut the statutory presumption. This continued rate discrepancy results in subsidization of [Petitioner’s] intrastate operations by interstate operations, representing an excessive and undue burden on interstate commerce.
States have presented various arguments in attempting to defeat proposed intrastate rate increases. The ICC has consistently awarded relief despite those arguments. In an early case, the North Carolina Utilities Commission sought to assign responsibility to a carrier for the disparity between intrastate and interstate rates, especially through reference to past internal business practices such as the size of dividend payments to its corporate parent and management bonus incentives. With respect to such internal business practices, the ICC, in this case and in others similar to it, has adopted the concept, that business decisions are best left to the carrier and to its stockholders while carriers are operating in a transportation environment in which the rule of thumb is to "let the market regulate itself."

In responding to a question regarding the responsibility for disparity between interstate and intrastate rates, the Commission replied with a statement which provides a guiding light for future Commission decisions in this area: "Our responsibility under Section 11501 is not to investigate the history of burdens on interstate commerce, but to remove them." Another novel argument advanced by the North Carolina Commission was that the ICC could not authorize the requested rate increase, because even after the ICC had approved the requested rate increase, intrastate rates would still be lower than comparable interstate rates. The ICC rejected this contention and stated:

Section 17 of the Bus Act does not mandate immediate equalization of intrastate and interstate rates for services performed by passenger carriers. Rather, it provides a procedure for removal of unreasonable burdens on interstate commerce resulting from depressed intrastate rates. [Petitioner] has stated that it will pursue gradual equalization of rates. This is not an unreasonable approach. The proposed increase will reduce the burden on interstate commerce without unduly disrupting [Petitioner's] intrastate operations.

The state of Alabama argued before the Commission that various op-

68. Carolina Coach—North Carolina, supra note 65, at 9. In fact, many if not most early cases arising under this section resulted in intrastate increases which remained well below interstate rates. This may well be a vindication of the view that intrastate rates had been unreasonably depressed for so long that they could not be raised in one fell swoop to the level of interstate rates; the increase would be too great for the riding public to accept.
erating ratios indicated that approval of the requested intrastate increase was not warranted. The ICC did not accept this argument and held "[that] [T]he calculation of intrastate versus interstate operating horatios on mixed operations involves arbitrary accounting assumptions . . . . we do not find these calculations sufficiently reliable enough to rebut the statutory presumption raised by the rate discrepancies."69

The Georgia Public Service Commission employed the argument that the total equalization of interstate and intrastate rates would result in a very low intrastate operating ratio, while concluding that intrastate rates at the interstate level would be unreasonably high. Once again, the ICC failed to accept the argument, and concerned itself only with the discrepancy between interstate and intrastate rates.70

The Missouri Public Service Commission utilized the argument that the petitioning carrier's interstate rates, which were admittedly higher than its intrastate rates, were artificially high by virtue of their being set through the taking into account of improper costs. The ICC observed that a petition under Section 11501 was not the proper forum to raise the issue of the legality of interstate rates.71 The Missouri Commission appealed the decision to the Commission, in effect asking the Commission "what is a state to do" to rebut effectively the rebuttable presumption in favor of raising intrastate rates. In responding, the ICC suggested:

To rebut this presumption, respondent is required to demonstrate that intrastate rates which are below those for comparable interstate transportation are nonetheless reasonable. Generally, evidence of distinguishing factors in

69. Greyhound Lines—Alabama Pub. Serv. Comm'n., No. MC-C-10904 at 3 (I.C.C. served May 21, 1984). Citing Greyhound Lines—West Virginia Pub. Serv. Comm'n., 133 M.C.C. 382 (1984). In Greyhound Lines—New York State Dept. of Transp., No. MC-C-10865 (I.C.C. served December 12, 1983), aff'd sub nom. Commissioner v. I.C.C., 750 F.2d 163, the reviewing court concluded that since the concept of calculating "intrastate versus combined operating ratios involves a number of highly arbitrary accounting assumptions used to allocate revenues and expenses between intrastate and interstate operation," the ICC could reasonably conclude that New York's operating ratio evidence "was unreliable and insufficient" to rebut the statutory presumption. Id. at 179. Even more recently, the ICC was highly critical of the operating ratio argument as a means of a state satisfying its burden to rebut the presumption. Greyhound—Pennsylvania, MC-C-10913 at 4.


71. Trailways American Buslines and Midwest Buslines—Missouri Pub. Serv. Comm'n., No. MC-C-10856 at 4 (I.C.C. served July 22, 1983) [hereinafter cited as Trailways—Missouri]. Missouri appealed that decision to the ICC, arguing inter alia, that since revenues earned from intrastate increases exceed the carriers' cost of service, the presumption in 49 U.S.C. § 11501(e)(2)(A)(ii) (1982) involving a comparison of revenues and variable costs should come into play. The ICC properly held that the first presumption (the disparity between interstate and intrastate rates) was all that was in issue, and that in the absence of a showing that petitioner's evidence is materially flawed regarding the rate discrepancy, or showing that there are special characteristics of intrastate operation that produce lower costs, the presumption is not rebutted. Trailways—Missouri, No. MC-C-10856 at 4.
operating conditions and costs of services associated with providing intrastate as compared with interstate service is the most probative and relevant in establishing the reasonableness of the lower rates. 72

Though there are further examples which illustrate the futility of states seeking to block the increase in intrastate fares, they are all representative of the same proposition: the Interstate Commerce Commission will not be swayed from its path of infusing its own brand of "deregulation" upon the states. The previous examples relate to rate preemption, the most frequent preemption provision being considered by the ICC, although the philosophy expressed is equally illustrative of the other less frequent appeals to the Commission in which relief is sought from burdensome state regulation in other areas.

Section 16 of the BRRA provides for ICC preemption of requests by carriers to abandon intrastate regular routes. 73 Illustrative of cases under that section is a decision by the Oklahoma Corporation Commission to deny a request to abandon intrastate service, subsequently appealed to the ICC. 74 One of the involved routes had admittedly been dormant for 25 years, yet the Oklahoma Commission argued that approval of the abandonment "would threaten the integrity of the regulatory process." 75 With respect to the other routes, Oklahoma argued that the discontinuance of service would leave some patrons without bus transportation and suggested that the ICC order the carrier to conduct operations in vehicles with limited seating capacity. The ICC found it not in the public interest for a carrier to continue unprofitable operations and permitted the petitioning carrier to discontinue intrastate service.76

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72. Trailways—Missouri, supra note 72, at 2-3. Many states have advanced this argument, but the ICC has consistently found it unpersuasive on the facts. Perhaps there is no factual situation in which the costs of interstate operations are significantly different from those of intrastate operations. In any event, no such facts have yet been presented to the ICC.
73. BRRA, supra note 2, § 16, enacted as 49 U.S.C. § 10935 (1982).
75. Id. at 5.
76. The ICC, in a typical expression of the policies involved, held:
The proposed discontinuance will leave intermediate points on these routes without bus service, and there are no alternative modes of public transportation available to these points. The question is not, however, merely whether there will be a loss of service—that much is obvious by the mere filing of the exit request. Rather, the statute requires that we weigh, against the disadvantages caused by the loss of bus service to residents of and business in the affected communities, the goals of allowing the most productive use of equipment and energy resources, enabling efficient and well-managed carriers to earn adequate profits and attract capital, and improving and maintaining a competitive privately owned motor carrier system. To that end, it is not in the public interest to require [the carrier] to continue unprofitable operations which jeopardize its ability to provide service on its other routes, by requiring cross-subsidies for more successful operations. Consequently, the question requires a balance between the local interests in support of continuing these services and the policy of the Bus Act that favors exit.
The Minnesota Public Utilities Commission appealed an ICC decision which permitted a carrier to discontinue intrastate service. The Court observed that, "the congressional purpose of the Bus Regulatory Reform Act of 1982 was to free interstate carriers from state created impediments that prevented them from abandoning unproductive routes." 77

Congress included the most qualifications in that portion of the pre-emption scheme which deals with discontinuance of service. Congress' purpose was to be certain that the ICC did not ignore the needs of local residents who would lose bus service through any authorized discontinuance. 78 One reviewing court, while affirming the ICC's approval of discontinuance over five intrastate routes, disapproved its action authorizing discontinuance over a sixth. 79 The reviewing court required that before authorizing a discontinuance the Commission make independent findings with respect to each of the three standards specified in the statute. The court criticized the Commission's actions as "just such a charade" as Congress sought to avoid in reviewing requests for discontinuances. 80 Considering the context of the Commission's actions in this area and the deference given the Commission by reviewing courts, it seems that even in this case the ICC could have avoided court criticism by expressing its findings more precisely. This case which criticizes the ICC's action under the BRRFA is not a criticism of the ICC's rush toward deregulation. It is only a reminder that the Commission must dot most of its "i's" and cross most of its "t's" in reaching its deregulatory result. 81

In practice, the ICC is utilizing an interpretation of the BRRFA which

78. See text accompanying note 14, infra. A more recent decision, which includes a thorough examination of the ICC's role under Section 16 of the Bus Act, is illustrative of just how far the ICC will stretch credulity in finding that reasonable alternative service will exist following an abandonment of service by a petitioning carrier, as required by 49 U.S.C. § 10935(g)(2)(C) (1982). Greyhound Lines—New York State Dept. of Transp., No. MC-C-1515 (I.C.C. served August 23, 1985). The decision is also interesting in its consideration of the state's offer of financial assistance, which is one factor to be considered in abandonment cases, under 49 U.S.C. § 10935(g)(2)(B) (1982). The ICC found that in considering the reasonableness of the state's offer of a subsidy for the carrier to continue service, the carrier could reasonably and lawfully include a 10 per cent profit level in its calculations. Id. at 21-22.
79. Pennsylvania v. United States 749 F.2d at 841.
80. Id. at 855.
81. In what might be termed a tacit recognition of regulatory facts of life, the court concluded with the admonition that on remand "the ICC must consider the two, distinct findings required under section 16 of the Bus Act... before granting Greyhound's exit application." Id. at 855-56. (emphasis added.)
leads to the granting of relief to any carrier which comes before it, provided there is at least a tenuous link with interstate commerce. The Federal preemption provisions establish a situation in which state regulation, despite its merits, may be readily avoided by an interstate carrier. This leads to the consideration of Federal preemption from a more subjective point of view.

IV. THE PUBLIC INTEREST IN FEDERAL PREEMPTION

In enacting the BRRA, Congress was responding to severe problems that were facing the intercity bus industry. Other modes of transportation had previously been freed from often over-burdensome regulation. An observer can maintain almost any view of the wisdom of motor carrier regulation (except perhaps a pure "no regulation of any sort under any circumstances" approach) and acknowledge that some reform of state regulation of bus carriers was vital. As an active practitioner in the bus field, this writer would suggest that the horror stories detailed in the legislative history of the BRRA could easily have been expanded upon. The "chilling effect" on small carriers from the extraordinary delays and red tape associated with any modification of service was such that many carriers simply could not survive and at the same time continue to provide responsive service.

Congress, perhaps with a knowledge of those to whom the preemption provisions were directed, the state regulatory agencies, was rather insistent that its scheme of lessened regulation be adopted. The restate-ment of the National Transporting Policy in the BRRA includes specific directions to the ICC to "ensure that intrastate regulation is exercised in accordance with" the BRRA and further, that the "reform initiatives" enacted by the BRRA "are not nullified by State regulatory action." The statement in Section 17 of the BRRA directs the states to adopt the Federal procedures within two years of the effective date of the Bus Act.

This rather harsh language was included because it was generally recognized in the industry that the states, for the most part, were not in

82. In Commissioner of Transp. v. United States, 750 F.2d at 163. New York argued that its policy of permitting Greyhound easily to eliminate unprofitable rates and the fact that Greyhound had substantial monopoly power over many routes meant that the disparity between interstate and intrastate rates was not such a burden on interstate commerce warranting ICC action. The ICC rejected the seemingly meritorious arguments as irrelevant, because they do not address the issue of differences in operating costs or conditions. The Second Circuit agreed with the ICC, observing that, "although these arguments may support the wisdom of regulation in general and the benificence of New York's regulation in particular, they do not significantly relate to the existing disparity between interstate and intrastate passenger fares to rebut the statutory presump- tion." Id. at 171.

83. BRRA, supra note 2, § 5, 49 U.S.C. § 10101(a)(3) (1982)).

84. BRRA, supra note 2, § 17(d) (not codified, note following 49 U.S.C. § 11501).
any hurry to modify their regulatory philosophy.\textsuperscript{85}

The state reaction to the Federal initiative has in many instances been "ostrich-like," taking the position that if the new law is ignored, perhaps it will go away. This has been the reaction of many state regulators since the preemption issues were first raised in pending legislation.\textsuperscript{86}

It is admittedly poor practice to consider the argument of a litigant in an appellate brief as an objective argument. However, the comments of Greyhound in an appeal of an increase in intrastate rates awarded by the ICC by the New York Department of Transportation is a reasonable characterization of the philosophy of the states and their regulatory trade association, National Association of Regulatory Utility Commissioners (NARUC). In response to the NARUC \textit{amicus} brief, Greyhound argued that: "Congress intended that the Bus Act limit the States' role in regulating intercity bus companies."\textsuperscript{87}

Private discussion with representatives of state Commissions suggests that while there is even more general displeasure at having been preempted by Congress out of a regulatory role, there is even more concern on the part of the state regulators over abuses resulting from carriers that seek to create a tenuous relationship between their operations and

\textsuperscript{85} More than three years after the effectiveness of the Bus Act, few states have heeded the Congressional call to modify their practices.

\textsuperscript{86} The author, delivering a speech before the National Conference of State Transportation Specialists at Louisville, Kentucky, in June, 1982, observed that much of the conversation and presentations were no more than entreaties for the participants not to ignore the deregulatory handwriting on the wall and to lessen state regulation before Congress took responsibility for intrastate regulation of the bus industry away from the states. Few, if any, changes were forthcoming. The author is aware of continuing state arguments seeking to assert state supremacy over the regulation of intrastate transportation in proceedings underway at the time of this writing, including, for example, assertions by the Washington Utilities and Transportation Commission in a matter before the U.S. District Court for the Western District of Washington, in Port of Seattle v. Evergreen Trails, Inc., No. C84-1312M. (W.D. Wash. 1984).

\textsuperscript{87} Greyhound stated in its brief:

NARUC presents a generalized and unfocused objection to the Bus Act. It expressed displeasure with the fact that the ICC is now carrying out the mandate of Congress and the provisions of the Act. This generalized expression of displeasure, however, is not tantamount to a legally sufficient basis for opposition. . . Simply stated, NARUC desires to retrieve for the States the primary jurisdiction over intrastate rates which the States had prior to the Bus Act. Having failed to win in Congress the preservation of the status quo, NARUC now seeks to emasculate Section 17 and return to the States, contrary to the Congressional intent, that lost jurisdiction.

NARUC misunderstands or refuses to understand that Section 17, and other provisions of the Bus Act were specifically intended to limit the State's role in regulating intercity bus companies. Brief for Intervenor, Commissioner of Transp. v. United States, 750 F.2d at 163, \textit{supra} note 13 at 25.

interstate commerce to avoid intrastate regulation when that regulation should in fact be exercised.

Such occurrences have frequently arisen in the entry area when a carrier, which the state believes is unfit, obtains vast intrastate operating authority through the “automatic” entry provisions of the ICC. In Atlantic City Shuttle and Bus Service, Inc., the carrier, domiciled in northern New Jersey, faced the difficulty of obtaining intrastate operating authority to allow it to perform services to and from the gambling casinos at Atlantic City. The carrier filed for regular route authority between Staten Island, New York (immediately adjacent to the State of New Jersey) and Atlantic City, New Jersey. Each of the carrier’s routes began at Staten Island and immediately crossed into New Jersey, where the routes traversed almost all feasible highways in the area en route to Atlantic City. Obviously, the carrier sought not only interstate but also intrastate authority. Such a proposal is one of the many examples of the ingenuity of carriers to employ the entry provisions of the BRRA to avoid state regulation.

One cannot help but feel that the ICC has gone overboard in many instances by failing to recognize that the preemption provisions are not “automatic”; rather they place a high burden upon the state agencies seeking to retain jurisdiction over intrastate transportation. Such a high burden should not be equated with the insurmountable burden that the Commission has imposed. The legislative scheme embraced by the BRRA is one in which “Congress expressly declined to issue a blank de-regulation check to the Commission; instead it required consideration of . . . distinct statutory standards, . . .” in rendering decisions. Until the states and/or private carriers call to the attention of the Commission a truly unjust case, and form the basis of a reasonable legal argument

88. The author is unaware of any application for additional passenger authority under the BRRA which was denied on its merits.
91. The application required two full pages in the ICC Register to describe its numerous routes.
92. At the same time, this area of apparent abuse is one of the few areas in which the ICC has been required by the courts to proceed with caution. Applications seeking regular route intrastate authority to serve the gaming casinos in Atlantic City, N.J. are mostly transparent requests to perform intrastate “special operations” service. The ICC is barred by 49 U.S.C. § 10922(c)(2)(H) (1982) from awarding intrastate special operations authority. In Hudson Transit Lines v. ICC, 765 F.2d 329 (2nd Cir. 1985), the Court reminded the ICC of its limited power in this one area, while generally affirming its other regulatory interpretations.
94. The Texas Railroad Commission seems especially reluctant to accept Federal preemption jurisdiction. See cases involving Texas cited supra in notes 35, 55, and 56. Oklahoma’s
regarding the ICC exceeding its vast discretion, the floodgates at the ICC will remain open in this area as they have in so many other areas in the current deregulatory era.

Characterizing the ICC’s implementation of the BRRA as overly generous must not be equated with a finding that the Commission’s implementation is either consistent with or contrary to the public interest. The merits of meaningful transportation regulation, in which there are meaningful limits placed upon carriers for the entry into the market, or exit from that market, and for rates, rules, and regulations, can and are being debated again and again. Classical economic analysis suggests that there will be “winners” and “losers” from any change in the rules of the game. This has been true in motor carrier regulation. Some traditional carriers have been unable to keep pace with changing mores in the bus industry, while others have been able to apply their entrepreneurial talent to provide new and imaginative services where restrictive regulation precluded them before. An industry steeped in lethargy has raced belatedly toward the modern, highly competitive transportation market which exists today. At the same time, the bus industry, like other transportation industries, has been in a state of turmoil, and there is a great deal of uncertainty from day to day as to what service will be available for that consumer.

The same classical economic analysis suggests that we cannot weigh the benefits of the “winners” against the cost to the “losers” and

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95. The current debate is centered in the freight area, probably because those transporting freight and those using their services have had several years during which to try out the “new” regulation. The argument does include the same essential issues present in consideration of the BRRA, namely arguing if “deregulation does ... strike a balance between carriers and shippers as outlined in various deregulation laws.” I.C.C.—A House Divided and Under Fire, New York Times, December 9, 1984, at F12-13. NARUC remains a forum for this debate, NARUC Panels View Truck Industry: Plenty of Questions, Few Answers, TRAFFIC WORLD, Dec. 2, 1985, at 33-4. One of the first formal, empirical studies in the bus area is a study prepared by the Illinois Commerce Commission entitled ILLINOIS BUS SERVICE SINCE THE BUS ACT: A DIMINISHING INTERCITY NETWORK: (1984). That study’s introduction observes, “While it is perhaps too soon to judge the effectiveness of BRRA in revitalizing the industry, the effect of the Act on rural and small city Illinois has been severe, [with] whole areas of nonmetropolitan Illinois ... taken from the state bus network, without compensating service gains in more populated regions.” (unnumbered page—“Introduction”). Illinois, it should be observed, is one of those states most vociferous in its opposition to the concept of Federal preemption.

96. Airline/bus intermodal innovations are described in Deregulation Fostering National Transport Network, THE TRAVEL AGENT, Nov. 15, 1984, at 6; new pricing initiatives are described in Travelways Discounts RT Returns by 10%, THE TRAVEL AGENT, December 17, 1984, at 4.

97. For example, Trailways announced doubled levels of service on routes between Boston and New York, only a few months after a significant reduction in service over the routes. Trailways Reduced Fares as Union Takes Wage Cut, TRAFFIC WORLD, Dec.17, 1984, at 31.
calculate a satisfactory result. The only result of which we can be certain, is that the industry is in a state of change by virtue of the ICC’s implementation of the BRRA. The next generation of observers will ultimately determine if the implementation was beneficial or not.

V. WHERE DOES FEDERAL PREEMPTION UNDER THE BRRA LEAD?

In general, the Federal preemption provisions of the BRRA are successful insofar as the ICC and almost every carrier are concerned. In seeking to bring an end to overly restrictive state regulation, the ICC may have gone too far in some instances. However, the states have failed to seize upon examples of exceedingly unjust conduct or results under the BRRA and to bring them to the attention of the Commission or the courts. Interstate Commerce Commission preemption of state regulation of intrastate passenger transportation is here to stay.

With Federal preemption in the railroad industry far more extensive than in the bus industry, the only remaining fertile ground for preemption is in the trucking industry. One can have the same fears as those of any other observer of the transportation industry when it comes to peering into crystal balls. The apparent success of Federal preemption in the bus and rail fields cannot help but thrive in the fertile ground of complaints by property carriers. Property carriers have learned to live with Federal deregulation and presently find the only remaining restrictions are those of a continuing and burdensome regulation of intrastate service by the states.

Whatever the merits, it appears that the surface transportation industry will be operating under the philosophy of “let the marketplace regulate itself” for the foreseeable future. Federal preemption of state regulatory

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98. From the author’s experience, Greyhound has made extensive use of the relief provisions of the BRRA. Many smaller carriers have made great use of them as well. However, now that the smaller carriers see that the results of this new law include not only relief for them from onerous state regulation but also vast new intrastate competition (and new interstate competition under the liberal interpretation of all of the Bus Act’s entry provisions) where none existed before, the BRRA is not necessarily viewed in such glowing terms. Whether the BRRA preemption provisions will be viewed in the future by the majority of independent bus companies as a panacea for their ills is problematical. It is likely that all will agree that the BRRA will be viewed in retrospect as a strong catalyst for change.

99. See discussion of rail regulation in Section I, supra.

100. “One issue that will have to be resolved before you can have any further deregulation is the issue of federal preemption of the states. You cannot have an essentially deregulated environment on the federal level and a very highly regulated situation at the state level.” Chairman Reese Taylor of the ICC, quoted in The ICC in 1984: Where Has It Been, Where Is it Going?, TRANSPORT TOPICS, Dec. 17, 1984, at 12, in response to a question asking for his predictions of areas ripe for trucking legislation in 1985.

power over intrastate transportation is an important element in the current system of "regulation by non-regulation" and is possibly a harbinger of further Federal preemption of state transportation regulation.
Section 214 of the Staggers Rail Act: Is It Working as Congress Intended?

DAVID H. BAKER*

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I. INTRODUCTION

The purpose of this article is to examine the implementation of Section 214 of the Staggers Rail Act of 1980\(^1\) and the impact of this Section on the traditional state regulation of intrastate rail rates. The thesis of this article is that the Interstate Commerce Commission ("ICC" or "Commission") has interpreted Section 214 in a manner contrary to the intent of the drafters of the legislation. The few court decisions to date\(^2\) interpreting Section 214 have failed to conclusively resolve the issue of how far the ICC may go in directing state regulation of intrastate rail rates. Accordingly, it is recommended here that either Supreme Court review or further Congressional action is needed to resolve this issue.

The article will briefly review state regulation over rail rates prior to enactment of the Interstate Commerce Act, the various amendments to the Act as they pertain to state intrastate rail rate regulation and the background of Section 214 generally. The article will address in greater detail the more significant ICC and court decisions involving Section 214 with an emphasis on how far the ICC may go in directing the states rail rate regulation. The article will conclude with a discussion of the apparent conflict between the Sixth Circuit\(^3\) and the D.C. Circuit,\(^4\) on this issue and the possibility of Supreme Court review or the need for legislative change.

II. ENACTMENT OF SECTION 214 OF THE STAGGERS RAIL ACT OF 1980-
    49 U.S.C. SECTION 11501

   A. PAST PRACTICES

1. PRIOR TO INTERSTATE COMMERCE ACT

   Under the Commerce Clause of the United States Constitution\(^5\) Congress has the power to "regulate commerce among the several states." While in the early 1800's many states enacted statutes which purported to

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\(^2\) This article was completed in the summer of 1985.
\(^3\) Kentucky Util. Co. v. ICC, 721 F.2d 537 (6th Cir. 1983).
\(^4\) Utah Power & Light Co. v. ICC, 747 F.2d 721 (D. C. Cir. 1984), reh'g denied, 764 F.2d 865 (D.C. Cir. 1985).
\(^5\) U.S. CONST. art. I, § 8, cl. 3.
regulate intrastate and interstate transportation, by the latter part of the 19th century there were a number of federal legislative enactments dealing with interstate rail transportation including the Garfield Act of 1866 and the precursor to the Livestock Transportation Act of 1906. After the Supreme Court's decision in Wabash Rail Company v. Illinois, which held that a state may not regulate charges for carriage within its own boundaries of goods brought from outside the state or destined to points outside the state, it became apparent that the federal power over interstate rail transportation was quite broad, if not exclusive. With the passage of the Interstate Commerce Act in 1887, exclusive federal jurisdiction over interstate rail transportation was established. However, section 1 of the original Act expressly reserved jurisdiction over intrastate rail rates to the states.

2. **Shreveport and Transportation Act of 1920**

Through a series of court decisions and amendments to the Interstate Commerce Act, the Commission began to gradually acquire jurisdiction over certain aspects of intrastate rail commerce. In the Shreveport rate case of 1914, the Supreme Court held that the antidiscrimination provisions of the Interstate Commerce Act made it unlawful for railroads to maintain intrastate rates which discriminated against interstate commerce. The Court thus concluded that the Commission was authorized to order the removal of these discriminatory intrastate rates, although such rates had previously been considered to be exclusively within the state's jurisdiction. The Supreme Court's holding in Shreveport was enacted into law by Section 416 of the Transportation Act of 1920.

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6. See, Ill. Const., art. VII; see also the so called "Granger cases" headed by Munn v. Illinois, 94 U.S. 113 (1877).
9. 118 U.S. 557 (1886).
10. Id.
12. Id.. Section 1 provided in pertinent part as follows: The provisions of this Act shall not apply: To the transportation of passengers of property, as to the receiving, delivering, storage, or handling of property, wholly within one state and not shipped to or from a foreign country or to any state or territory as aforesaid.
14. 41 Stat. 484 (1920) (codified at 49 U.S.C. § 13(4) (1980)). Section 13 of the Interstate Commerce Act, which then governed intrastate rail rates, was amended to provide that:

(4) Whenever in any such investigation the Commission, after full hearing, finds that any such rate, fare, charge, classification, regulation, or practice causes any undue or unreasonable advantage, preference, or prejudice as between persons or localities in intrastate commerce on the one hand and interstate or foreign commerce on the other hand, or any undue, unreasonable, or unjust discrimination against interstate or foreign
Although the Commission was granted authority to establish intrastate rates where the rates were discriminatory or unreasonably interfered with interstate commerce, the Commission was not granted unlimited authority over intrastate rates. Rather, the states continued to have some autonomy over intrastate rail traffic.

3. **TRANSPORTATION ACT OF 1958**

The Transportation Act of 1958 expanded the Commission's authority over intrastate rail rates by further extending section 13 of the Interstate Commerce Act.\(^\text{15}\) Under the 1958 amendments, the Commission was given authority to institute an investigation into an intrastate rail rate even if it was being considered by the state commission at the same time.\(^\text{16}\) A carrier petition under Section 13\(^\text{17}\) was to be handled expeditiously as opposed to waiting for the state commission to act. The 1958 amendments\(^\text{18}\) were designed to expedite the authorization of general revenue ex parte increases in the several states, which often lagged behind authorization by the Commission at the interstate level by several years.

4. **RAILROAD REVITALIZATION AND REFORM ACT AMENDMENTS**

Further amendments to Section 13 resulted from the enactment of the 4R Act in 1976.\(^\text{19}\) Under the new provisions of the Act, the Commission was permitted to authorize an intrastate rail rate if a rate proceeding was pending before the state commission and the state commission did not act within 120 days of the commencement of that rate proceeding.\(^\text{20}\) The state thus retained primary jurisdiction over the rates if it acted within 120 days.\(^\text{21}\) With the call for new legislation in the late 1970's, the states' commerce, which is hereby forbidden and declared to be unlawful, it shall prescribe the rate, fare, or charge, or the maximum or minimum, or maximum and minimum, thereafter to be charged, and the classification, regulation, or practice thereafter to be observed, in such manner as, in its judgment, will remove such advantage, preference, prejudice, or discrimination. (emphasis added)


That upon the filing of any petition authorized by the provisions of paragraph (3) hereof to be filed by the carrier concerned, the Commission shall forthwith institute an investigation as aforesaid into the lawfulness of such rate, fare, charge, classification, regulation, or practice (whether or not theretofore considered by any State agency or authority and without regard to the pendency before any State agency or authority of any proceeding relating thereto) and shall give special expedition to the hearing and decision therein. (emphasis added)

16. Id.
17. Id.
18. Id.
20. Id.
21. The new language of section 13 provided:
role was to be greatly curtailed.

B. NEED FOR CHANGE

One of the premises of enactment of new federal rail legislation\(^{22}\) in the late 1970's was that the carriers were facing a severe capital shortfall and in deteriorating financial condition.\(^{23}\) Excessive regulation of both interstate and intrastate rail rates was widely perceived as the principal cause of the railroads' problem.\(^{24}\) The House Committee on Interstate and Foreign Commerce noted in its report in May of 1980\(^ {25}\) that intrastate rail traffic was under a different regulatory scheme than interstate traffic and that as a result the average revenue to variable cost ratio for intrastate traffic was 120 percent as compared to 136 percent for interstate traffic.\(^ {26}\) The House Committee went on to note that:

if the intrastate ratio had been equal to the interstate ratio in 1977 the railroads would have earned $400,000,000 in additional revenues.\(^ {27}\)

Thus Congress perceived a need to bring the State's rail regulatory authority in line with the Interstate Commerce Commission's regulations.\(^ {28}\)

C. CONGRESSIONAL RESOLUTION

On October 14, 1980, President Carter signed into law the Staggers Rail Act of 1980,\(^ {29}\) with an effective date of October 1, 1980. Section 214 of the Staggers Act\(^ {30}\) radically changed the relationship between State Commissions and the Interstate Commerce Commission as to regulation

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The Commission has exclusive authority to prescribe an intrastate rate for transportation provided by a rail carrier subject to the jurisdiction of the Commission under subchapter I of chapter 105 of this title when—

(A) a rail carrier files with an appropriate State authority a change in an intrastate rate, or a change in a classification, rule or practice that has the effect of changing an intrastate rate, that adjusts the rate to the rate charged on similar traffic moving in interstate or foreign commerce; and

(B) the State authority does not act finally on the change by the 120th day after it was filed.

24. Id.
26. Id., at 61.
27. Id., at 61.
The conferees' intent is 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. Accordingly, the Act preempts state authority over rail rates, classifications, rules and practices. States may only regulate in these areas if they are certified under the procedures of this section.
29. Staggers Rail Act, supra note 1.
of intrastate rail rates. The avowed purpose of these changes was, to bring state practices in line with federal practices so as to avoid (1) regulatory delay by the state commissions31 and (2) the use of standards different than those used by the Interstate Commerce Commission.32

Section 214 of the Staggers Act substantially modified 49 U.S.C. Section 11501 of the Interstate Commerce Act.33 Under revised Section 11501(b), a state commission may only exercise jurisdiction over intrastate rail rates in accordance with the provisions of the Interstate Commerce Act.34 Pursuant to revised Section 11501(b), state commissions were required to submit to the Commission by January 31, 1981, standards and procedures in accordance with the Interstate Commerce Act.35 Within 90 days thereafter, the Commission was to certify the State Commissions if the Commission determined that "such standards and procedures are in accordance with the standards and procedures applicable to regulation of rail carriers by the Commission . . . ." pursuant to the Act.36 Unfortunately, neither the Commission nor the States were able to comply with this 90 day time limitation. Congress somewhat presaged the Commission's ability to implement this program by noting in Section 214 of the Staggers Rail Act that the existing standards and procedures "shall be deemed to be certified by the Commission . . . ." until the Commission could issue a decision certifying or denying certification for the individual states.37

A carrier may appeal the decision of a state commission to the ICC on the ground that the standards and procedures applied by the state commission were not in accordance with the Interstate Commerce Act. Shippers are not provided with a similar remedy. Arguably, appeals must be taken within 20 days of service of the state commission decision, since an appeal of right must be filed within 20 days under federal standards and procedures.38 However, a good argument can also be made that an appeal constitutes a petition to reopen which may be filed at any time,39 or a new petition before the Commission, which presumably may also be filed at any time.

Under revised Section 11501, the Commission must take final action on any such petition "within 30 days after the date it is received."40 If the

32. Id.
38. 49 C.F.R. § 1115.2 (1985).
Commission determines that the state commission standards and procedures are not in accordance with the Interstate Commerce Act, the Commission is to "determine and authorize the carrier to establish the appropriate rate . . .".\footnote{41}

It is generally perceived that through the revised certification process, the Commission has much greater authority over state intrastate rail rates than ever before. However, it appears that Congress envisioned the Commission to be an appellate tribunal in state rate cases, as opposed to a trier of fact. If that is the case, the Commission's authority is limited to determining whether the state agency utilized the proper standards in reaching its conclusions. As long as the evidence supports the state's findings, the Commission could not set state agency findings aside. The extent to which the Commission may overrule the state's findings is at the center of the controversy on Section 214. The decisions discussed below will deal with this issue in greater detail.

III. EX PARTE NO. 388, STATE INTRASTATE RAIL RATE AUTHORITY

A. COMMISSION CERTIFICATION PROCESS

In response to the Congressional mandate in Section 11501(b), the Commission instituted Ex Parte No. 388, State Intrastate Rail Rate Regulation—PL 96-448.\footnote{42} In response to this notice, 40 states filed for certification.\footnote{43} By decision served April 21, 1981, the Commission certified conditionally each state which had expressed its intention to exercise jurisdiction consistent with the law and to do so in a timely fashion.\footnote{44} This conditional or provisional certification was to expire June 29, 1981. On June 30, 1981, the Commission extended the conditional or provisional certification an additional 90 days—until October 19, 1981.\footnote{45} Petitions by Conrail and the Florida rail carriers to revoke the provisional certifications in Indiana and in Florida respectively were rejected by Commission order served September 3, 1981.\footnote{46}

B. STATE IMPLEMENTATION

The majority of the 40 provisionally certified state commissions filed various implementation rules with the Commission in the fall of 1981. The Commission concluded that it still did not have enough information upon

\footnotesize{\begin{itemize}
\item \footnote{41} Id.
\item \footnote{42} 45 Fed. Reg. 74571 (1980).
\item \footnote{44} Id. at 3.
\item \footnote{45} State Intrastate Rail Rate Auth., (I.C.C. served June 30, 1981).
\item \footnote{46} State Intrastate Rail Rate Auth. (I.C.C. served Sept. 3, 1984).
\end{itemize}}
which to base its final certification decisions.47 To aid the states in the certification process, the Commission provided an outline or model of what, at a minimum, the state filing should contain.48 In issuing this decision, the Commission for a third time extended the provisional certification of the 36 remaining states seeking certification (Maine, Mississippi, North Carolina, and Rhode Island of the original 40 withdrew their requests to be certified).49

On May 11, 1982, the Commission announced that it was assuming jurisdiction over intrastate rail transportation in six states which had specifically requested that the Commission assume such jurisdiction50—California, Connecticut, Delaware, Mississippi, Nevada, and North Carolina.

The Commission did not assert jurisdiction over intrastate rail rates in Alaska, Arizona, Hawaii, Maine, Massachusetts, Rhode Island, South Dakota, Vermont, or the District of Columbia51 because certification was not sought by these states nor was a request made for the Commission to assume jurisdiction. Thus, theoretically there is neither federal nor state regulation of intrastate rail movements in these jurisdictions. Arguably common law principles are applicable to movements within the states.

As a result of the Commission’s continuing extensions of the conditional certification, the Illinois Central Gulf Railroad challenged an Indiana Public Service Commission decision reducing their switching charges on the basis that the conditional certification of the State Authority was invalid under the Staggers Act.52 The 7th Circuit affirmed the Commission’s action of certifying states on a continuing basis.53 Nonetheless, the Court admonished the Commission for allowing the states to continue regulating intrastate rates without conformity to federal standards and prolonging conditional certificates.54 The Commission seems to have taken this decision to heart and began to issue certification decisions for a number of

48. Id. at Appendix.
49. Id. at 1. The new deadline for revised standards and procedures by the states was set at April 9, 1982. Id., at p. 9. However a fourth extension was granted on April 9, 1982 to file revised standards and procedures. State Intrastate Rail Rate Auth.—Pub. L. No. 96-448, (I.C.C. served April 9, 1982).
51. Id. at 2.
54. Id. at 963. As the situation exists now, many states are regulating intrastate rail carriers without having established that they are doing so in conformity with federal standards. While we are not prepared at this time and on this record to say that the conditional certification scheme is now invalid, we believe it appropriate to expedite the certification process and bring an end to conditional certification.
state authorities.\textsuperscript{55}

\section{C. Court Challenges to Certification}

\subsection{1. Illinois}

In its first certification decision (August 5, 1982), the Commission merely moved from a "conditional" or "provisional" certification for the Illinois Commerce Commission to a "tentative conclusion" that the Illinois Commerce Commission had met the requirements for certification.\textsuperscript{56} The Commission, however, sought further comment on the extent to which a state must adopt each and every federal exemption under Section 10505.\textsuperscript{57} In this tentative certification of the Illinois Commerce Commission’s standards and procedures, the Commission noted that the Illinois plan appeared to apply section 10505 criteria.\textsuperscript{58}

On January 27, 1983, the Commission certified the state of Illinois to exercise jurisdiction over intrastate rail rates based on the conclusion that the states need not follow Commission regulations and precedents in all subject matters.\textsuperscript{59}

Despite this general language, the Commission changed its position on the extent to which the states may deviate from the federal exemptions under Section 10505.\textsuperscript{60} The language of the decision indicates that unless conditions in a state could be shown to be unique,\textsuperscript{61} a state may not deviate from a federal exemption of rail traffic.\textsuperscript{62} Accordingly, the Commission concluded that Illinois must modify its plan to comply with Com-

\textsuperscript{55} State Intrastate Rail Rate Auth.—Pub. L. No. 96-448 (I.C.C. served Oct. 6, 1982), the Commission assigned a sub number to each of the 37 states then seeking certification and individual certification decisions began to be issued shortly thereafter. To date, approximately 21 states have received final certification. Office of Proceedings in the late summer of 1985.

\textsuperscript{56} State Intrastate Rail Rate Auth., 365 I.C.C. 855, 856 (1982).

\textsuperscript{57} Id. at 856-857.

\textsuperscript{58} Id. at 857. In its tentative certification of the Illinois Commerce Commission’s standards and procedures, the Commission stated:

Section 11501(b) does not appear to require state adoption or endorsement of every ICC exemption. The requirement for certification is that the states apply the same Section 10505 criteria. The Illinois plan clearly indicates that it will do so . . . . Recognizing that we may have an opportunity to review a state's failure to follow an interstate exemption, we conclude that the Illinois position that it will not automatically follow an interstate exemption is not a bar to certification.

\textsuperscript{59} State Intrastate Rail Rate Auth., 367 I.C.C. 149 at 151 (1983). In that decision the Commission noted:

. . . this does not mean that states have to follow each Commission regulation and every Commission precedent in all subject matters. This would in essence deprive a state of any jurisdiction and/or discretion over intrastate rates, rules and practices. The Staggers Act does not require preemption to that extent.

\textsuperscript{60} Id. at 152.

\textsuperscript{61} Id. at 154.

\textsuperscript{62} Id. at 152.
mission guidelines.\textsuperscript{63}

In a strongly worded dissent, Commissioner Simmons, joined by Chairman Taylor, noted that the so-called standard for exemption is Section 10505, not Commission rulings under Section 10505.\textsuperscript{64} Much of the dissent focussed on the different conditions which exist between intrastate and interstate traffic.

The Illinois Commerce Commission appealed the Commission's decision to the United States Court of Appeals for the District of Columbia Circuit\textsuperscript{65} and sought a stay from the Commission, pending judicial review. By Commission decision served March 4, 1983, the Commission denied the stay request and extended the due date for modifications to the Illinois rules until July 1, 1983.\textsuperscript{66}

The Commission's decision was affirmed by the D.C. Circuit in \textit{Illinois Commerce Commission v. ICC}.\textsuperscript{67} In that decision, the Court concluded that a federal exemption is a "standard or procedure that bound the State regulators."\textsuperscript{68} Significantly, Judge Swygert refused to adopt the broad interpretation of the term "standards and procedures" proffered by the intervenor railroads.\textsuperscript{69} He noted, "the only issue before us is whether 'standards or procedures' should be interpreted broadly enough to include federal exemptions."\textsuperscript{70} The court concluded: "In view of the overriding importance of the exemption provisions, it was reasonable for the ICC to conclude that the statute required states to give immediate and automatic effect to federal exemptions."\textsuperscript{71}

Judge Antonin Scalia, a noted administrative law expert, dissenting from the three member panel hearing the case, rejected the majority's view that total preemption of state regulation was mandated by Congress.\textsuperscript{72} Scalia then proceeded to discuss the legislative history of Section 214 of the Staggers Rail Act and surmised that the determination of the exemptions under the Act is not a standard, but rather the final deter-

\textsuperscript{63} Id. at 154. The pertinent language stated: Because we conclude that a state must follow our exemptions as to rates, classifications, rules, practices, Illinois must make appropriate modifications to its plan as submitted.

\textsuperscript{64} Id. at 155. Judge Simmons noted: I also see no logical necessity for automatic extension of an exemption found appropriate for interstate movements to the same category of intrastate traffic. The transportation conditions within an individual state can be significantly different than those of the Nation as a whole with respect to a particular traffic segment.

\textsuperscript{65} No. 83-1120 (D.C. Cir. 1983).

\textsuperscript{66} State Intrastate Rail Rate Auth., No. 96-448, (I.C.C. served March 4, 1983).

\textsuperscript{67} Illinois Commerce Comm'n v. ICC, 749 F.2d 875 (D.C. Cir. 1984).

\textsuperscript{68} Id. at 883.

\textsuperscript{69} Id.

\textsuperscript{70} Id.

\textsuperscript{71} Id. at 884.

\textsuperscript{72} Id. at 887.
mination to be made.\textsuperscript{73}

In light of the 2-1 split, the Illinois Commerce Commission petitioned the U.S. Supreme Court for review, but the petition was denied on October 7, 1985.\textsuperscript{74} Thus, the D.C. Circuit decision remains the final word on this issue for the time being.

2. \textit{FLORIDA}

The Florida Public Service Commission (PSC) also opposed the Commission’s efforts to require that it adopt each and every federal exemption developed under Section 10505.\textsuperscript{75} The posture of the Florida litigation was somewhat different than that of the Illinois litigation. In the Commission’s March 18, 1983 Florida certification decision, it noted that it tentatively found that Florida had met the basic requirements for certification, but required that Florida adopt the federal exemptions in lockstep fashion.\textsuperscript{76}

The Florida PSC filed a petition for review of the Commission’s tentative certification decision with the United States Court of Appeals for the 11th Circuit on April 29, 1983.\textsuperscript{77} The appeal was taken prior to the issuance of a second order, reviewing Florida’s subsequent submissions, as in the Illinois case. The Florida railroads moved to dismiss the Florida PSC Petition for Review before the Eleventh Circuit on the basis that it was not a final order. Although the motion was originally carried with the case,

\textsuperscript{73} Id. at 889. Judge Scalia, in what is probably the most piercing of all of the judicial analyses of Section 214 and the meaning of standards and procedures, notes:

> The question before us whether a Commission class-of-traffic exemption—that is, a Commission determination under 49 U.S.C. § 10505 that a particular category of interstate traffic (such as boxcar or export coal traffic) shall be exempt from one or more provisions of the Act (e.g., rate regulation)—constitutes an internal ‘standard or procedure’ of the Commission. It seems to be obvious that it does not. A Commission exemption—exemption from rate regulation, for example—is in no sense a standard by which the validity of a rate is determined, but is rather the determination itself, in effect approving all rates for the subject commodity . . . the mere existence of some ‘generality in a determination is not alone enough to make it a standard, since the same is obviously true of the carrier ‘rules’ and ‘classifications’ that the Commission approves.

> . . . What is meant by a standard is a principle of of general application regarding degree of competition, revenue adequacy, service needs or other elements of the national transportation policy which will, when applied to particular facts, determine the legitimacy of railroad behavior. Prototypical examples are the ‘formulas or procedures’ for determining variable costs and the ‘standards and procedures for establishing adequate revenue levels’ that the Commission is required to adopt. [citations omitted] To confuse such a standard with an exemption is to call a criterion a conclusion or a test an outcome.


\textsuperscript{76} Id.

\textsuperscript{77} No. 83-3268, (11th Cir. 1983).
on January 25, 1984, just prior to scheduled oral argument, the Eleventh Circuit granted the motion to dismiss without prejudice to the Florida PSC to file another Petition for Review upon issuance of a final Commission order.\footnote{78}

On July 1, 1985, the Florida PSC, in part in response to the D.C. Circuit’s decision on interstate exemptions, gave up the struggle to regulate its intrastate rail rates and requested that the Commission assume jurisdiction over intrastate freight rates.\footnote{79} Thus, the issue of federal exemptions is over in Florida.

In a proceeding involving similar issues in Colorado\footnote{80} the Commission specifically ruled that ‘‘the [federal] boxcar exemption is in effect in the State of Colorado . . .’’ and authorized the three petitioning railroads to cancel all boxcar tariffs.\footnote{81} Chairman Taylor dissented, noting that although he is opposed to the automatic extension of interstate exemptions to intrastate movements, and opposed to the federal boxcar exemption decision, the states are required to abide by federal rules.\footnote{82} In light of the D.C. Circuit’s decision in \textit{Illinois Commerce Commission v. ICC}\footnote{83} the Colorado decision was probably correctly decided as the law currently exists.

3. \textit{Texas}

The state of Texas may be the least enthusiastic of all the states about the Commission’s increased authority as a result of Section 214 of the Staggers Act. On December 12, 1980, the state of Texas filed suit against the Commission in the United States District Court for the Western District of Texas seeking a declaratory judgment that Section 11501 of Title 49 was unconstitutional.\footnote{84} Judge Nowlin of the District Court granted the government’s request for summary judgment, denied Texas’ request for summary judgment and dismissed the case with prejudice.\footnote{85}

\footnote{78. Florida PSC v. ICC, 724 F.2d 1460, at 1462 (11th Cir. 1984). In granting the motion, the Court noted: 
\ldots judicial action at this time could severely disrupt the administrative process. The March 18 Order provides a schedule for interested parties to comment on Florida’s standards and procedures. When the agency makes its final determination of Florida certification, it may rely on concerns expressed in these comments. Until the final decision is rendered, the Court cannot know either whether failure to adopt federal exemptions will result in denial of certification or what other grounds for denial the agency may use . . . .
\footnote{81. \textit{Id.} at 2.
\footnote{82. \textit{Id.} at 4.
\footnote{85. \textit{Id.} \ldots}}}}}}
The state of Texas appealed that decision along with support by the National Association of Regulatory Utility Commissions ("NARUC") and the state of Kansas, both of whom intervened in support of Texas. The Fifth Circuit, by Judge Wisdom in *State of Texas v. ICC*, affirmed the District Court and noted that the "Act is in nature a preemptive statute. If the state wishes to continue regulating, it must do so in accordance with federal policy."86 The Court noted that the preemption of state law is implicit in the goals and operations of the Staggers Act.87 Therefore Texas' challenge to the statute was rejected. However, the Court expressly avoided the issue of the extent to which certified state agencies must follow policies and decisions of the Commission.88

In related proceedings, the Commission decertified the Railroad


87. Id. at 347.

88. Id. at 347-348. In addition, the state of Texas raised four constitutional objections to Section 214 of the Staggers Act. Because two of the objections are common to a number of the certification cases, including Illinois and Florida, they merit more detailed discussion here.

First, Texas asserted that the preemptive scheme set forth in Section 214 of the Staggers Act exceeded Congress' authority under the commerce clause. The court, in rejecting this argument, noted that it must give great deference to a Congressional finding that a regulated activity substantially affects interstate commerce so long as there is any rational basis for such a finding. Once this basis is found, the Court's only remaining function is to inquire as to whether there is a reasonable connection between the regulatory means selected and the asserted ends. In this instance, the Court concluded that it is well established that the regulation of intrastate railroad rates has a direct and substantial effect on interstate commerce. Further, the Court concluded that there is a reasonable connection between preempting independent state rail regulation and overall deregulation of rail ratemaking.

The second argument relied upon by the state of Texas, and raised in the Illinois and Florida litigation, concerns the effect of the 10th amendment upon the Commission's actions under Section 214. Texas argues that Section 214 intrudes upon the sovereignty of the states under the 10th amendment. The 10th Amendment provides as follows:

The powers not delegated to the United States by the Constitution nor prohibited by it to the states are reserved to the states respectively, or to the people.

The court concluded that Section 214 is not an unconstitutional intrusion upon the sovereignty of the states. The Court noted that even under the most liberal construction of this argument, as expressed by the Supreme Court in *National League of Cities v. Usery*, 426 U.S. 833 (1976) it could not reach such a conclusion.

Judge Wisdom rejected the argument that Section 214 gives the ICC direct control over state standards and procedures, in effect regulating the states in their traditional role of governing their internal economies. The Court noted that Section 214 preempts state law, but gives the states the option either to continue regulation in compliance with federal law or to cease independent regulation altogether. The Court held:

Because the states have this option, because there is no affirmative coercion of the states by the federal government, the Act does not implicate the two principal concerns underlying 10th Amendment jurisprudence: political accountability and separation of powers.

The Court's opinion emphasized that "Congress may not act in such a manner as to impair the States' integrity or their ability to function effectively in a federal system. *Fry v. U.S.*, 421 U.S. 542 (1975). Thus, the Court appears to suggest that while Section 214 of the Staggers Act does not in itself violate the 10th Amendment, compulsive action, presumably by the Commis-
Commission of Texas, effective May 20, 1984.\textsuperscript{69} By Commission decision served April 20, 1984,\textsuperscript{90} Texas' application to be certified to regulate intrastate rail rates, classifications, rules and practices was denied. At the same time, the Commission revoked the provisional certification that was granted to Texas during the pendency of this application for certification.\textsuperscript{91} The Commission noted that because Texas refused to comply with federal law as expressed by Commission decisions, both rulemaking and adjudicatory, in particular, the rail contract rules,\textsuperscript{92} the Commission concluded that Texas standards and procedures "are wholly deficient in that it is unwilling to regulate intrastate rail rates in accordance with federal law".\textsuperscript{93} Furthermore, the Commission concluded it would be contrary to the spirit of Section 11501 to continue provisional certification where Texas had so grossly ignored and violated federal standards.\textsuperscript{94} Under the Commission's decision, the Railroad Commission of Texas was directed to wrap up all existing proceedings to the maximum extent feasible during the 30 day period following issuance of the Commission's decision and to transfer any cases that could not be completed to the Commission.\textsuperscript{95} Further, the Railroad Commission of Texas was directed not to commence any new proceedings.\textsuperscript{96}

On June 21, 1985, the D.C. Circuit issued its decision affirming the
ICC decision to deny certification to the Railroad Commission of Texas. Judge Starr, writing for a unanimous panel, rejected all of Texas' arguments and notes that the Court's decision "does not forever leave Texas behind, as it were, with the train having pulled out of the station; to the contrary, Texas may resubmit new standards and procedures to the ICC, and if the new submission is adequate, then the RCT will join the growing ranks of certified state authorities." The Court concluded "the upshot of all of this is that Texas now must demonstrate compliance with federal law before it may regulate."  

IV. COURT INTERPRETATION OF STATE REGULATION OF INTRASTATE RATES AND PRACTICES SINCE STAGGERS

There are also four recent state agency decisions which have worked their way through the appellate courts and now provide some guidance in determining the extent of the Commission's authority over state intrastate rate determinations. These decisions are from the Third, Sixth, Seventh and D.C. Circuits and deal with the interpretation of standards and procedures under Section 11501.

A. ILLINOIS CENTRAL GULF RAIL COMPANY v. ICC

The first appellate decision to issue on the interpretation of "standards and procedures" under Section 11501 was a Seventh Circuit decision, Illinois Central Gulf Rail Company v. ICC. In this case, Union Carbide shipped 143 cars of coal via the Illinois Central Gulf Railroad within the state of Kentucky. Because of extremely cold weather, Union Carbide had difficulty unloading the coal and kept the cars in excess of the free time specified in its average demurrage agreement with the railroad. The railroad assessed demurrage charges and Union Carbide paid the charges. On December 18, 1980, Union Carbide filed a complaint with the Kentucky Railroad Commission seeking a refund of the penalty portion of the demurrage charges on the basis that such charges were unreasonable in light of the extreme weather conditions and its diligence in unloading the coal. The Kentucky Commission agreed and

98. Id. at 226.
99. Id. In addition, Starr reviewed the Railroad Commission of Texas' failure to comply with Commission standards as to suspension of rates, jurisdiction, contract rate disclosure, and refusal of tariffs. Starr concluded that these problem areas will alone be sufficient to demonstrate that the ICC's denial of certification to Texas was neither arbitrary nor capricious.
101. Id. at 112.
102. Id. at 113.
ordered the railroads to return nearly $160,000 in demurrage charges.\textsuperscript{103} The Illinois Central Gulf Railroad filed a Petition for Review with the Commission arguing that the Kentucky Commission’s decision not to enforce the average demurrage agreement was inconsistent with ICC standards and procedures.\textsuperscript{104} The Commission affirmed the Kentucky Railroad Commission noting that the "Kentucky Commission’s decision is within the limits of the discretion remaining to the states."\textsuperscript{105} Curiously, the Commission took the position that because the Interstate Commerce Act does not specifically require the enforcement of average demurrage agreements, the Section 11501 requirement that a state exercise jurisdiction "exclusively in accordance with the provisions of this subtitle" is inapplicable, and that whether demurrage agreements are upheld rests within the discretion of the State Commission.\textsuperscript{106}

The Seventh Circuit overruled the Commission, holding that "consistent rulings of the ICC must necessarily be incorporated and adhered to by State Commissions exercising jurisdiction pursuant to the Staggers Act".\textsuperscript{107} The Court never indicates whether it views average demurrage agreements as a "standard procedure or practice", nor defines these terms, but rather indicates that: "... [w]hether the ICC’s insistence in honoring average agreements is considered a 'standard', 'procedure', or 'practice', it should have been applied by the Kentucky Commission."\textsuperscript{108} Thus, the first decision to interpret the meaning of "standards and procedures" and "exclusively in accordance with the provisions of the Interstate Commerce Act" somewhat sidesteps the issue of the meaning of these terms. However, the actual effect of the decision was to imply a rather broad interpretation to these terms, because the case dealt with neither a statutory provision nor a regulation, but rather a Commission interpretation through case law. Presumably if state agencies had to comply with Commission case law, they would have little or no discretion.

\textbf{B. KENTUCKY UTILITIES CO. v. ICC}

In the next significant Court decision, \textit{Kentucky Utilities Co. v. ICC},\textsuperscript{109} the Sixth Circuit vacated an ICC ruling and ordered that the State Commission’s tariff be reinstated. In this case Kentucky Utilities filed a complaint with the Kentucky Railroad Commission challenging the

\begin{thebibliography}{9}
\bibitem{103} Id.
\bibitem{104} Id.
\bibitem{106} Illinois Central Gulf, supra note 100, at 114.
\bibitem{107} Id. at 115.
\bibitem{108} Id. at 116.
\bibitem{109} Kentucky Util. Co. v. ICC, 721 F.2d 537 (6th Cir. 1983).
\end{thebibliography}
reasonableness of the Louisville and Nashville’s (L & N) rate on an intra-state movement of coal. The Kentucky Railroad Commission heard the case, considered federal standards, including the then applicable ton/ton mile formulation and prescribed a rate 20 cents per ton less than that requested by the L&N.\textsuperscript{110} Shortly after the issuance of the Railroad Commission’s decision, the ICC issued its decision rejecting the ton/ton mile methodology as a cost formula.\textsuperscript{111} The railroad then sought review of the Kentucky Commission’s decision before the ICC.\textsuperscript{112}

The Commission, in its review of the State Commission’s decision, noted that sufficient consideration was not given to how these rate prescriptions would assist the L&N to achieve revenue adequacy.\textsuperscript{113} The Commission further found that because the rate set by the KRC was “only 8 percentage points above” the level at which the ICC could assert jurisdiction over a rate case, the Kentucky Railroad Commission order was set aside. Finally, the Commission found that the railroad’s original proposal was not excessive and approved the carrier’s rates.\textsuperscript{114}

The Sixth Circuit concluded that because the Commission failed to formulate its own benchmark ratemaking standard, no meaningful state certification could occur and therefore under Section 11501(b)(3), the standards and procedures of the Kentucky Railroad Commission “shall be deemed to be certified by the Commission.”\textsuperscript{115}

The Court rejected the Commission’s argument that because the rate was only 8 percentage points above the then jurisdictional threshold of 165 percent, the rate could not be found to be unreasonable.\textsuperscript{116} As the Court noted, the Commission implied that such a relationship between the revenue to variable cost ratio of the proposed Kentucky rate and the statutory threshold was evidence that the rate was unreasonably low and could not promote the Staggers Act goal of revenue adequacy.\textsuperscript{117} The Court highlighted that the revenue to variable cost ratio was to serve as a jurisdictional threshold in the determination of market dominance and not

\textsuperscript{110} Id. at 541-542.
\textsuperscript{112} Kentucky Util. Co., supra note 109.
\textsuperscript{113} Id.
\textsuperscript{114} Id.
\textsuperscript{115} Id. at 544. As the court noted:

"Properly understood, the Court here merely finds that the ICC’s dereliction of its initial responsibility under the Staggers Act to formulate a polestar ratemaking standard for use in certified state standards has established the standards employed by the KRC as the applicable rate formula herein, limiting the scope of the Commission’s inquiry to the issue of whether the Kentucky standards were applied “in accordance with the provisions of this subtitle.”

\textsuperscript{116} Id.
\textsuperscript{117} Id.
as a test for reasonableness.\textsuperscript{118}

The Court went on to reject the Commission's summary approval of the proposed rates.\textsuperscript{119} In this instance, the Court decided deference should not be given to the Commission's decision because of the lack of evidence and the application of law to fact.\textsuperscript{120} Further, just because 30 days is a short time within which to make a rate determination, does not mean that the Commission can simply approve the rate proposed by the carrier.\textsuperscript{121} The Court concluded that the Commission's decision must be vacated, and rather than remanding it to the Commission for further action, the Court ordered the Kentucky Railroad Commission decision reinstated.\textsuperscript{122}

Obviously, this decision will be relied upon by shippers seeking to challenge intrastate rail rates. Without an administratively final and judicially approved standard of rate reasonableness, it can be argued that the Commission has no polestar standard for ratemaking and thus the State Commission should be given greater discretion in this area.\textsuperscript{123} Further, the Sixth Circuit's decision will make it more difficult for the Commission simply to reject a State Commission's determination and approve the proposed rate increase filed by the carriers. Now, the Commission will have to make a more detailed determination as to the reasonableness of the rate.

\textbf{C. WHEELING-PITTSBURGH STEEL v. ICC}

In \textit{Wheeling-Pittsburgh Steel v. ICC},\textsuperscript{124} the Public Service Commission of West Virginia prescribed a maximum reasonable rate on intrastate coal movements not to exceed a revenue to variable cost ratio of 175 percent.\textsuperscript{125} The Public Service Company (PSC) found the existing rates to be unreasonable and directed that refunds be paid. The Chesapeake and Ohio Railroad petitioned the ICC for review of the PSC order. The Commission set aside the PSC order on the grounds that:

1. The order did not give sufficient consideration to revenue adequacy;
2. The order lacked a rationale for establishing a revenue to variable cost ratio of 175 percent;
3. The order failed to allow the Commission to review the PSC’s anal-

\textsuperscript{118} \textit{Id.}
\textsuperscript{119} \textit{Id.} at 544. As the court noted "judicial deference is extended only to reasoned agency decisions."
\textsuperscript{120} \textit{Id.} at 544-545.
\textsuperscript{121} \textit{Id.} at 545.
\textsuperscript{122} \textit{Id.}
\textsuperscript{123} \textit{Id.} at 546.
\textsuperscript{124} \textit{Wheeling-Pittsburgh Steel v. ICC}, 723 F.2d 346 (3rd Cir. 1983).
\textsuperscript{125} \textit{Id.} at 356.
ysis of basic costing matters. The Commission, as in the Kentucky Utilities case, simply adopted the rates instituted by the carriers as the appropriate rate. In dictum, the Court noted that the Staggers Act "did not fundamentally reallocate federal and state ratemaking authority . . . but rather, it appears that Congress, by rejecting federal preemption of intrastate rates, intended to preserve this traditional sphere of state competence." The Wheeling-Pittsburgh Steel case, along with the Kentucky Utilities case, provides some basis for arguing that Section 214 has not totally preempted state intrastate ratemaking.

The Court here interprets the term "standards and procedures" to encompass "standards and procedures promulgated and interpreted in decisions and orders of the ICC as well as those standards or procedures expressly incorporated in the Interstate Commerce Act." This broad interpretation of the terms standards and procedures is consistent with the Seventh Circuit's view of terms which went so far as to include average demurrage agreements as standards and procedures. The Third Circuit concluded that "[o]n questions of law as to whether state authorities have complied with these standards and procedures, the Commission's review is plenary." (emphasis added)

The Commission's proposed stand alone cost guidelines were promulgated subsequent to the PSC's determination. The Court determined that because the PSC did not have the benefit of the Ex Parte 347 standards, it must conclude that its February 10 order did not meet federal standards for calculating costs or computing maximum reasonable rates. Accordingly, the Court enforced that portion of the Commission's order holding that the rates did not meet federal standards. However, the Court rejected the Commission's cursory approval of the rates instituted by the C&O. Similar to the Kentucky Utilities case, the

126. Id. at 350-351.
128. Wheeling-Pittsburgh Steel, supra note 124, at 351.
129. Id. at 354-355.
130. Id. at 354-355.
131. Id. at 355.
132. Id. at 355.
133. Id. at 356.
134. Id.
135. Id. at 357. The case was remanded to the ICC. No. 82-3122, (3rd Cir. 1984). Order issued February 6, 1984. On remand, the Commission reopened the proceeding and requested comments on a number of issues including whether the proposed coal rate guidelines should be applicable to the decision, the relationship between Section 11501 rate prescriptions and the general rate reasonableness standards of the Act, the applicability of the Long Cannon factors to rate reasonableness determinations under Section 11501, and whether the case should be remanded to the PSC. Docket No. 38973, order served Feb. 7, 1984. NARUC and the Public
Commission acted without articulating any standard for the appropriate rates.

C. UTAH POWER & LIGHT COMPANY v. ICC

While the three Court of Appeals decisions discussed above can be interpreted in a consistent manner, the D.C. Circuit's recent decision in Utah Power & Light Company v. ICC\textsuperscript{136} conflicts with the Sixth Circuit's decision in Kentucky Utilities and perhaps portions of the Third and Fifth Circuit decisions. The Utah Power case involved a movement of coal from a mine in Utah to a power plant in Salt Lake City.\textsuperscript{137} Utah Power & Light maintained that the existing rate of $5.97 per ton was unreasonably high.\textsuperscript{138} The Utah Public Service Commission agreed with the shipper and ruled that the railroads had market dominance, that the Denver and Rio Grande Railroad was revenue adequate and that the subject rates were unreasonably high.\textsuperscript{139} The Utah Commission ordered the railroads to reduce the rates and to pay refunds to the shipper.\textsuperscript{140} The railroads filed a Petition for Review of the Utah PSC decision with the Interstate Commerce Commission.\textsuperscript{141} The ICC reversed the Utah PSC and held that the rates and issues were reasonable.\textsuperscript{142} The shipper then filed a Petition for Review of the ICC's decision with the United States Court of Appeals for the District of Columbia Circuit.\textsuperscript{143}

One of the bases of the Petition for Review was that the ICC exceeded its appellate jurisdiction by unlawfully conducting a de novo review of the record compiled before the Utah Public Service Commission.\textsuperscript{144} The Court noted that the shipper had asserted that the standard of ICC review of state agency action was similar to that of a court reviewing federal agency action based on the Sixth and Seventh Circuit's decisions discussed above.\textsuperscript{145} The Court rejected this argument.\textsuperscript{146}

\textsuperscript{136} Utah Power & Light Co. v. ICC, 747 F.2d 721 (D.C. Cir. 1984).
\textsuperscript{137} Id. at 723.
\textsuperscript{138} Id. at 724.
\textsuperscript{139} Id.
\textsuperscript{140} Id.
\textsuperscript{141} Id.
\textsuperscript{142} Id. at 725.
\textsuperscript{143} Id.
\textsuperscript{144} Id.
\textsuperscript{145} Id. at 732.
\textsuperscript{146} Id. at 732-733. Judge MacKinnon wrote:

The exact scope of the ICC's authority over the decisions of State Commissions is not
Judge MacKinnon concluded that the decision was in agreement with the Third Circuit in *Wheeling-Pittsburgh Steel Corp. v. ICC*. However, the Third Circuit noted only that the Commission’s powers were plenary as to questions of law. It did not go as far as Judge MacKinnon and give the ICC power to review all factual matters. It appears that Judge MacKinnon is seeking to bolster his decision by trying to make it seem consistent with the Third Circuit.

If Judge MacKinnon’s views were adopted by the Supreme Court, they would clearly emasculate the state’s authority over intrastate rail rates. By giving the Commission broad and unlimited power both as to questions of law and questions of fact, and permitting the Commission to start over and prepare a new record, the state commission’s record building and decision making process would be an exercise in futility.

The decision by Judge MacKinnon appears to place the D.C. Circuit somewhat at odds with that of the Sixth Circuit in *Kentucky Utilities Company v. ICC*. The Sixth Circuit expressly noted that it was not the intent of Section 11501 to have a “de novo rate hearing.” However the D.C. Circuit stated: “we cannot agree with such construction of the Staggers Act, which denies the oversight responsibility of the ICC so clearly envisioned by Congress.”

V. CONCLUSION

It seems inconsistent for Congress to have so clearly enunciated a program whereby states would seek certification from the ICC so that they could act in the first instance on intrastate rail rate matters and then, per-

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147. *Id.* at 734.
149. *Utah Power & Light*, supra note 136 at 734. Judge McInnon noted:

> We agree with the Wheeling-Pittsburgh Court and also consider that the ICC, while conducting its Section 11501 review, may choose to limit its review to the record compiled before the state agency, or start over if it considers the case so requires. (emphasis added)

150. *Id.* at 734, fn. 18.
151. *Id.*
152. *Id.* Petitioner Utah Power and Light Company sought rehearing and rehearing *en banc*. The three-judge panel agreed to rehear the case and accepted responses to the Petition for Rehearing from the ICC. *Utah Power & Light Co. v. ICC*, 764 F.2d 865 (D.C. Cir. 1985). The panel, however, ultimately dismissed the Petition for Rehearing and affirmed its original decision. To date, no petition for *writ of certiorari* has been filed. Thus, it is likely that the case on the merits will proceed on remand before the Commission.
mit the ICC to conduct a second full hearing on the issue, including compiling a new record. In the opinion of this writer, there does not appear to be any support in the legislative history, or a review of the Section 214 amendments to 49 U.S.C. § 11501, to support this interpretation of how far the Commission may go in directing state regulation of intrastate rail rates. Indeed, it would appear that the D.C. Circuit's view would in effect result in a federal statute regulating the states as states in a area of traditional state economic regulation. Accordingly, the conflict between the D.C. Circuit and the Sixth Circuit should be resolved by the Supreme Court, or if the Supreme Court refuses to hear this matter, by further legislative action.

There are a number of legislative proposals to further amend or fine tune the Staggers Rail Act of 1980. The most recent proposals expressly deal with the issue of the extent of the Commission's appellate review of state intrastate rail decisions. S. 477, introduced by Senator Andrews on February 20, 1985 and H.R. 1190, introduced by Congressman Tauzin on February 21, 1985 provide that the Commission's review of state agency decisions be limited to normal appellate review, similar to 5 U.S.C. § 706, as opposed to de novo review. Further, a shipper as well as a carrier would be permitted an appeal. It may well be that if the Supreme Court does not act on this issue by early 1986, 49 U.C.S. § 11501 will be clarified by further Congressional action. In the interim, a split exists in the Circuits thus causing a great deal of uncertainty as to how state intrastate rail rate challenges will be conducted.

156. id. at Section 9(b).
157. id. at Section 9(a).
The Constitutionality of State Approval Requirements for the Acquisition or Transfer of Control of a Common Carrier or Public Utility

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This article addresses the question of whether, in light of the recent Supreme Court decision in Edgar v. MITE Corp.,¹ state approval requirements² for the acquisition of a public utility or common carrier are subject

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2. The laws of fourteen states—i.e., Arizona, Arkansas, California, Illinois, Kansas, Louisiana, Missouri, Nevada, New Mexico, Oklahoma, Oregon, Tennessee, Texas, and Utah—were surveyed with respect to the question of whether state approval was required for the acquisition
to challenge under the Supremacy$^3$ and Commerce$^4$ Clauses of the United States Constitution. Part I presents a brief background concerning questions surrounding the constitutionality of state takeover statutes, which were at issue in *Edgar*, and demonstrates how these questions relate to the state approvals here in issue. Part II presents a discussion of the holdings of *Edgar*, as well as a summary analysis of related federal circuit and district court case law. Part III discusses strategies for potential constitutional challenges to the state approval requirements, particularly in light of the recent decision in *National City Lines v. LLC Corp.*$^5$

Finally, Part IV concludes (1) that a strong challenge could be made to the state approval requirements under the Commerce Clause; and (2) that a less persuasive, but nevertheless legitimate, challenge to the state approval requirements could be made pursuant to the Supremacy Clause.

I. BACKGROUND

In 1968 the United States Congress passed the Williams Act, which amended the Securities Exchange Act of 1934 to provide for certain filing and disclosure requirements in connection with the making of cash tender offers.$^6$ Although the Williams Act did not preempt the entire field of securities regulation with respect to cash tender offers,$^7$ it nevertheless sought to establish a national system of regulation governing tender offers$^8$ which would strike a neutral balance between the incumbent man-
agement of the target company and the offeror. Approximately four months before passage of the Act, certain states began adopting their own takeover bid disclosure statutes; ultimately, by 1981, 37 states had adopted such state takeover laws.9


The state statutes shared certain common characteristics. Generally, the statutes regulated tender offers for state corporations, frequently defined as including companies incorporated, headquartered, or having their principle place of business within the state, as well as corporations 10% of whose stock was held by state residents.\(^\text{10}\) The statutes generally provided for disclosure of tender offers to the applicable state authority and to the target company’s management a specified number of days—frequently twenty—prior to the effective date of the tender offer.\(^\text{11}\) The state statutes generally subjected such filings to a decision by the requisite state authority as to the fairness to investors of the planned takeover. The state authority generally was empowered to conduct a formal investigation or to hold hearings on the issues at hand, and pursuant thereto could indefinitely suspend the effective date of a tender offer until such time as the investigation or hearing was concluded and a ruling promulgated.\(^\text{12}\)

The constitutionality of the state takeover statutes was first chal-

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With the passage of the Maine statute in 1978, more than two-thirds of the states had purported to regulate the making of corporate tender offers. Comment, The Constitutionality of the Maine Takeover Bid Disclosure Law, 30 ME. L. REV. 246, n.2 (1979).


11. In contrast to the five day requirement promulgated under authority of the Williams Act, supra at n.6. 17 C.F.R. § 240.14d-2(b) (1985).

The state statutes also classified, and strictly limited, acquisitions of more than ten percent of a target company’s stock during a given time period, and thereby assumed that such acquisitions were in contemplation of a corporate takeover attempt. The state statutes generally also sought to regulate so-called “creeping tender offers,” defined to include open market and privately negotiated acquisitions whereby an entity acquired a large percentage of a target’s voting securities over time without use of a formal tender offer. Such “creeping tender offers” are not subject to the formal tender offer disclosure requirements of § 14D of the Williams Act, although they are subject to the filing requirements of § 13D once an entity has acquired five percent of the securities of that target company. See Telvest, Inc v. Bradshaw, 697 F.2d 576 (4th Cir. 1983) (discussing Virginia Take-over Bid Disclosure Act, VA. CODE § 13.1-529(b)(ii) (Supp. 1985), as amended in 1979 to reach “creeping tender offers”); and Agency Rent-A-Car, Inc. v. Connolly, 542 F. Supp. 231 (D. Mass.), rev’d, 686 F.2d 1029 (1st Cir. 1982) (discussing Massachusetts Takeover Statute, MASS. GEN. LAWS ANN. ch. 110C (Supp. 1985), as amended by 1981 Mass. Acts 508).

12. See supra n.10.
lenged in federal court in the late 1970s, in the leading case of *Great Western United Corp. v. Kidwell.* In *Kidwell,* the Idaho state takeover statute was challenged under the Supremacy Clause as being preempted by the Williams Act disclosure requirements; it's validity also was challenged under the Commerce Clause. The Fifth Circuit agreed with plaintiff Great Western on both grounds. In reaching its conclusion concerning the Commerce Clause challenge, the court employed the balancing test set forth in *Pike v. Bruce Church, Inc.* Between the time of *Kidwell* and the 1982 decision in *Edgar,* at least thirteen other state takeover statutes were declared unconstitutional.

15. Preemption is judged under the three-part test of *Rice v. Santa Fe Elevator Corp.*, 331 U.S. 213, 230 (1947): (1) how pervasive is the scheme of federal regulation; (2) how dominant is the federal interest; and (3) what portions, if any, of the state’s law conflict with or are otherwise inconsistent with federal law. The third inquiry is the toughest and most critical portion of the test. See McCauliff, *Federalism and the Constitutionality of State Takeover Statutes,* 67 VA. L. Rev. 295, 300 (1981).
16. *Kidwell* clearly demonstrated one of the most difficult aspects of the existence of numerous state laws and the burdens such statutes create for interstate commerce: a single tender offer could be subject to regulation by the federal statute and by two or more state statutes. In *Kidwell,* four states—Idaho, Maryland, New York and Washington—all had an interest in the outcome of the tender offer. See Comment, *The Constitutionality of the Maine Takeover Bid Disclosure Law,* 30 ME. L. Rev. 246, 253 n.56 (1979).
17. 397 U.S. 137, 142 (1970):
Where the statute regulates evenhandedly to effectuate a legitimate local public interest, and its effects on interstate commerce are only incidental, it will be upheld unless the burden imposed on such commerce is clearly excessive in relation to the putative local benefits. If a legitimate local purpose is found, then the question becomes one of degree. And the extent of the burden that will be tolerated will of course depend on the nature of the local interest involved, and on whether it would be promoted as well with a lesser impact on interstate activities.
In particular, it is important to note that the court in *Natomas* invalidated the Nevada takeover
Each of the state statutes discussed above and in n.18 supra were general state takeover bid statutes. Various states, however, also adopted statutes governing the acquisition of, or control over, corporations or entities in a given industry, such as insurance and, as in the present case, common carriers including railroads. Certain of these industry-specific statutes have been the subject of challenges patterned after the more general takeover statutes; in particular, state insurance holding company statutes have been the subject of constitutional challenges in Missouri, Kansas, Indiana, and Florida19 with varying results.20 It is these cases, when set against the background of the decisional law concerning general state takeover statutes, which provide the closest analogy to the current question, for the local and state benefits discussed in the insurance cases provide a rubric of parallel values which may offset corresponding burdens on interstate commerce under any Commerce Clause challenge. The district court decision in National City Lines provides a particularly good blueprint of the type of constitutional challenge which might be brought successfully against the state approval requirements governing the acquisition of common carriers and public utilities, such as railroads and oil pipelines.

II. THE DECISION IN EDGAR V. MITE CORP.21

Edgar addressed the constitutionality of the Illinois takeover statute22 which provided that a tender offer for the shares of a target company must be registered with the Illinois Secretary of State and communicated to the target company twenty business days before the offer became effective. During that twenty day period, the Secretary of State was empowered to hold a hearing to adjudicate the substantive fairness of the statute, as Nevada is one of the two jurisdictions with state approval requirements for the acquisition of railroads.


20. The conflicting outcomes in the insurance holding company cases apparently have resulted in large part from problems caused by the complicating factor of the MacCarran-Ferguson Act, 15 U.S.C. § 1012 et seq., which permits states to regulate the "business of insurance." It also should be noted that Roussel, National City Lines, Sun Life, and Gunter all were decided prior to Edgar.


offer if he or she believed a hearing was necessary to protect the interests of the shareholders of the target corporation. The law was applicable if the target corporation was organized under the laws of Illinois, had its principal place of business in Illinois, or had at least 10 percent of its stated capital and paid-in surplus represented within Illinois.

Plaintiff MITE Corporation, which had made its tender offer for the Chicago Rivet and Machine Company in compliance with the disclosure provisions of the Williams Act, sought to avoid the state act and challenged it in federal court on three separate grounds: (1) as preempted by the Williams Act under the Supremacy Clause; (2) as a direct burden on interstate commerce; and (3) alternately, as an indirect burden on interstate commerce. Although Justice White, in his opinion, addressed all three arguments in seriatim, only his analysis of the Illinois act as being an unconstitutional indirect burden on interstate commerce\textsuperscript{23} garnered the five votes necessary to become the opinion of the Court.\textsuperscript{24} A plurality of four supported Justice White's opinion that the Illinois Act also represented an unconstitutional direct burden on interstate commerce, while there were only three votes for his conclusion that the statute was preempted by the Williams Act under the Supremacy Clause.

\textbf{A. PREEMPTION UNDER THE SUPREMACY CLAUSE}

Justice White's Supremacy Clause preemption analysis was predicated on two factors. First, in passing the Williams Act, the Congress adopted a uniform national regulatory scheme of strict neutrality as between the incumbent management of the target company and the offeror.\textsuperscript{25} Congress adopted such a position in light of its finding that


\textsuperscript{24} Chief Justice Burger and Justices Powell, O'Connor, and Stevens joined in Part V-B.


Prior to \textit{Edgar}, there was some dispute as to whether the Williams Act specifically manifested a policy or purpose of strict neutrality.

Certain commentators suggested that the federal circuit courts, in elevating neutrality in tender offers to be a central purpose of the Williams Act, had ignored the Supreme Court's finding in \textit{Piper v. Chris-Craft Indus., Inc.}, 430 U.S. 1, 29 (1977) that such neutrality was but one characteristic of legislation designed specifically and primarily to protect investors. McCauliff, \textit{Federalism and the Constitutionality of State Takeover Statutes}, 67 Va. L. Rev. 295, 302-303 (1981); accord AMCA Int'l Corp. v. Krouse, 482 F. Supp. 929 (S.D. Ohio 1979). Other commentators, in contrast, criticized McCauliff's reliance on the language in \textit{Piper} regarding neutrality. See Sargent, \textit{On the Validity of State Takeover Regulation: State Responses to MITE and Kidwell}, 42 Ohio State L.J. 689, 714 (1981); accord, Crane Co. v. Lam, supra note 18. In \textit{Crane Co.} the court stated:

\textit{The question before the Court in Piper—whether the Williams Act confers a private right of action upon defeated offerors—was altogether different. The Piper court's objective was to determine who the Williams Act was designed to protect, and the Court concluded that the Williams Act was intended only to protect shareholders, not offerors.}
takeovers and tender offers often provided economic benefits, such as serving as a necessary check on entrenched but inefficient managers.\textsuperscript{26} Any state provisions which tipped the balance in favor of one party, therefore, were contrary to the intent and purpose of the Williams Act and subject to preemption. In particular, the Illinois statute provided for registration of a tender offer with the Illinois Secretary of State and with the target company twenty days before the effective date of the tender offer, as compared with the maximum five day waiting period provided for by the Williams Act, and thereby tipped the balance towards the incumbent management.\textsuperscript{27} So, too, did hearing provisions which allowed the Secretary of State to suspend a tender offer indefinitely pending state approval.\textsuperscript{28}

Second, Justice White found that the Williams Act had incorporated the Congressional finding that investors, when provided with all necessary information by means of the Williams Act's disclosure requirements, were to be the final arbiters of the fairness of a tender offer.\textsuperscript{29} The provision of the Illinois Act requiring a determination by the Secretary of State as to the fairness of a tender offer ran contrary to the plan of the Williams Act and was preempted.\textsuperscript{30}

Justice White's analysis was addressed by only five members of the Court. Chief Justice Burger and Justice Blackmun supported White's position, while Justices Stevens and Powell refused to join the opinion, stating that they were unconvinced that Congress' decision to follow a policy of neutrality manifested an intention to preclude states from providing special protection for certain interests including, but not limited to, incumbent management.\textsuperscript{31}

\begin{flushleft}
\textsuperscript{26} The Piper Court thus had no occasion to consider whether the neutral approach to tender offers adopted by Congress in the Williams Act was intended to establish a federal policy of neutrality with which the states cannot interfere.

509 F. Supp. 782, 788.

Accordingly, some commentators previously had concluded that the Williams Act had a two-fold purpose: to inform the investor, \textit{Piper}, 430 U.S. 1 at 30; and to favor neither the offeror nor the target, Rondeau v. Mosinee Paper Corp., 422 U.S. 49, 56 (1975). Comment, \textit{Challenges to State Takeover Laws: Preemption and the Commerce Clause}, 64 MARQUETTE L. REV. 657, 663 and note 27 (1981).

\textsuperscript{27} 457 U.S. 624, 626-27, 634-36.

\textsuperscript{28} Id. at 636-39.

\textsuperscript{29} Id. at 639-40.

\textsuperscript{30} Id.

\textsuperscript{31} 457 U.S. 624, 646-47 (opinion of Justice Powell); 457 U.S. 624, 655 (opinion of Justice Stevens).
\end{flushleft}
B. The Direct Burden on Interstate Commerce

Justice White was joined by Chief Justice Burger and Justices Stevens and O'Connor in his conclusion that the Illinois act was an unconstitutional direct burden on interstate commerce. Justice White's analysis was predicated on the fact that the Illinois Act, by its terms, directly regulated transactions which took place across state lines, even if wholly outside the state of Illinois, i.e., it impacted directly on tenders for, and transactions involving, securities made across state lines conducted by means of the mails, telephone, and other similar methods. Such transactions, which are themselves interstate commerce, would be prohibited unless the Illinois Act was complied with and the state approval given for a tender offer. This would be so even if none of the target's shareholders was a resident of Illinois. Accordingly, Justice White found the Illinois Act to be an unconstitutional direct burden on interstate commerce, relying on Southern Pacific Company v. Arizona, Shafer v. Farmers Grain Company, and Shaffer v. Heitner.

C. The Indirect Burden on Interstate Commerce

As previously noted, a majority of the Court supported Justice White's final conclusion that the Illinois act was a prohibited indirect burden on interstate commerce, under the balancing test of Pike v. Bruce Church, Inc.

The Court stated that the most obvious burden the Illinois Act imposed on interstate commerce arose from the statute's nationwide reach which purported to give Illinois the power to determine if a tender offer could proceed anywhere in the country. Against this "substantial" burden, the state raised two offsetting legitimate local interests: (1) that the Illinois Act served to protect resident security holders; and (2) that the

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32. Justices Blackmun and Powell did not address this point.
34. 457 U.S. 624, 641-42.
35. Id. at 642.
36. Id.
37. Id.
38. 325 U.S. 761, 775 (1945). The "practical effect of such [state] regulation is to control . . . [conduct] . . . beyond the boundaries of the state . . ." and therefore was prohibited.
39. 268 U.S. 189, 199 (1925). "[A] state statute which by its necessary operation directly interferes with or burdens . . . [interstate] commerce is a prohibited regulation and invalid, regardless of the purpose with which it was enacted."
40. 433 U.S. 186, 197 (1977). "[A]ny attempt 'directly' to assert extraterritorial jurisdiction over persons or property would offend sister States and exceed the inherent limits of the State's power."
41. See supra note 17.
42. 457 U.S. 624, 643.
43. Id.
Act served to regulate the internal affairs of companies incorporated under Illinois law. 44

With respect to the first point, the Court noted that Illinois had no legitimate interest in protecting non-resident shareholders and that insofar as the act burdened out-of-state transactions, there were no offsetting legitimate local interests to be weighed. 45 Furthermore, the Act exempted a target company’s acquisition of its own shares from regulation, thereby potentially undermining the Act’s asserted legislative purpose of protecting investors. 46

With respect to the second point, the Court cited Kidwell for the proposition that tender offers contemplate transfers of stock by stockholders to a third party and do not themselves implicate the internal affairs of the target company. 47 Furthermore, the proferred justification was incredible as the Act would apply in some instances even to wholly non-Illinois corporations, i.e., in situations where 10 percent of the outstanding shares of the target were held by Illinois residents but where the corporation was neither incorporated in, nor had its principal place of business in Illinois. 48

Accordingly, the Court found that the Illinois Act imposed a substantial burden on interstate commerce which outweighed the putative local benefits and therefore was invalid under the Commerce Clause. 49

D. RESULTS IN THE FEDERAL COURTS

Since Edgar was decided in 1982, the federal circuit and district courts have applied the decision to general state takeover statutes on at least four different occasions. 50 In three of those instances, involving the state takeover statutes of Missouri, 51 Maryland, 52 and Virginia, 53 the implicated statute was found to be unconstitutional under both the Supremacy and Commerce Clauses. In an anomalous decision, how-

44. 457 U.S. 624, 644.
45. Id.
46. Id.
47. 457 U.S. 624, 645.
48. Id. at 645-46.
49. Id. at 646.
ever, the Massachusetts takeover statute was upheld against like constitutional challenges.\textsuperscript{54}

\textit{National City Lines} concerned a challenge under the Supremacy and Commerce Clauses to both the Missouri Takeover Bid Disclosure Act\textsuperscript{55} and the Missouri Insurance Holding Companies Act.\textsuperscript{56} The Missouri Takeover Statute was virtually identical to the Illinois act at issue in \textit{Edgar}.\textsuperscript{57} The court, as a result, found that the issues raised under the Commerce Clause were controlled by \textit{Edgar}.\textsuperscript{58} At the same time, since only a plurality of the Supreme Court had reached the Supremacy Clause issues in \textit{Edgar}, the circuit court engaged in a lengthy, detailed analysis applying the preemption test summarized in \textit{Jones v. Rath Packing Company}.\textsuperscript{59}

The court's analysis carefully paralleled that of Justice White in \textit{Edgar} and relied heavily on the decisions of the various circuit courts in \textit{Kidwell, Kennecott Corp.}, and \textit{MiTE Corp. v. Dixon}.\textsuperscript{60} The court concluded

\textsuperscript{54} Agency Rent-A-Car, Inc. v. Connolly, 686 F.2d 1029 (1st Cir. 1982) (vacating the preliminary injunction granted by the district court as reported at 542 F. Supp. 231 (D. Mass. 1982), discussed supra note 15, and remanding to the district court).

\textsuperscript{55} Mo. Rev. Stat. § 409.500 (Supp. 1986) et seq.

\textsuperscript{56} Mo. Rev. Stat. § 382.010 (Supp. 1986) et seq. The insurance act was allegedly applicable because the target company, LLC Corp., had as one of its subsidiaries a Missouri insurance company, the Personal Life Insurance Company. Although the district court concluded that the McCarron-Ferguson Act did not preclude federal preemption of the insurance act, the circuit court found that LLC did not meet the definition of a "domestic insurer" under the state act; accordingly, the insurance act was held to be inapplicable.

\textsuperscript{57} 687 F.2d 1122, 1128.

\textsuperscript{58} Id.

\textsuperscript{59} 430 U.S. 519, 525-26 (1977):

The first inquiry is whether Congress, pursuant to its power to regulate commerce, U.S. CONST. art. I, § 8, has prohibited state regulation of the particular aspects of commerce involved in this case. ... [W]hen Congress had "unmistakably ... ordained," Florida Lime & Avocado Growers, Inc. v. Pauli, 373 U.S. 132, 142 (1963), that its enactments alone are to regulate a part of commerce, state laws regulating that aspect of commerce must fall. This result is compelled whether Congress' command is explicitly stated in the statute's language or implicitly contained in its structure and purpose. City of Burbank v. Lockheed Air Terminal, Inc., 411 U.S. 624, 633 (1973); [citation omitted].

Congressional enactments that do not exclude all state legislation in the same field nevertheless override state laws with which they conflict. U.S. CONST., art. VI. The criterion for determining whether state and federal laws are so inconsistent that the state law must give way is firmly established in our decisions. Our task is "to determine whether, under the circumstances of this particular case, [the state's] law stands as an obstacle to the accomplishment and execution of the full purposes and objectives of Congress." Hines v. Davidowitz, 312 U.S. 52, 67 (1941), Accord, De Canas v. Bica, 424 U.S. 351, 363 (1976); Perez v. Campbell, 402 U.S. 637, 649 (1971); [citation omitted]. This inquiry requires us to consider the relationship between state and federal laws as they are interpreted and applied, not merely as they are written.

As explicated in \textit{Kennecott Corp.}, 637 F.2d at 188, \textit{Jones} stands for the proposition that: "Preemption analysis focuses on whether the state law serves as an obstacle to the operation of federal law 'in the circumstances of the particular case,' rather than in all cases or in a hypothetical case." (Citing \textit{Jones}, 430 U.S. 519 at 525-26).

\textsuperscript{60} All cited supra at note 18.
(1) that, as with the Illinois act, the twenty-day waiting period of the Missouri act conflicted with the short time table of the Williams Act by creating undue delay in the commencement of the tender offers, which upset the neutral balance between incumbent management and the offeror mandated by Congress;\textsuperscript{61} (2) that the far more extensive disclosure requirements of the Missouri act provided a mass of irrelevant data which only served to confuse investors, in conflict with the policy of the Williams Act that informed investors should be able to make an unfettered choice about the merits of a tender offer;\textsuperscript{62} and (3) that the substantive requirements of the Missouri act, including specific withdrawal rights and pro rata rights, were in direct conflict with the parallel provisions of the Williams Act.\textsuperscript{63}

\textit{Bendix Corp. v. Martin Marietta Corp.} involved the Maryland Takeover Statute, which closely paralleled the Missouri and Illinois acts.\textsuperscript{64} The court began by engaging in a careful analysis of the six different opinions written by members of the \textit{Edgar} Court\textsuperscript{65} and reciting a lengthy list of cases in which state takeover statutes had been challenged.\textsuperscript{66} The court then went on to hold (1) that the Maryland Act imposed an unconstitutional \textit{indirect} burden on interstate commerce because by its terms Maryland assumed the power to block a nationwide tender offer and to decide if a tender could proceed anywhere;\textsuperscript{67} (2) that the Maryland Act was an unconstitutional \textit{direct} burden on interstate commerce because it regulated transactions in securities which took place across state lines;\textsuperscript{68} and (3) that its lengthy waiting period, with the possibility of indefinite delay while a hearing or investigation was in progress, and its exemption of offers approved by the target company, conflicted with the goals and purposes of the Williams Act and was therefore preempted.\textsuperscript{69}

\textit{Telvest, Inc. v. Bradshaw} presented a somewhat different analytical pattern than \textit{National City Lines} and \textit{Bendix}. \textit{Telvest} concerned Virginia's

\textsuperscript{61} 687 F.2d 1122, 1130.
\textsuperscript{62} \textit{id.} at 1131.
\textsuperscript{63} \textit{id.} at 1132-33.
\textsuperscript{64} The Maryland act provided that, for the act to be applicable, the target company had to be a Maryland corporation, doing business in Maryland, with at least 35 shareholders residing in Maryland. A tender offer was exempted from the act if it was approved by the target's board of directors. There was a twenty-day waiting period following registration, during which time the Maryland state commissioner could commence a hearing and institute an investigation to determine if the tender offer complied with Maryland law; the tender offer could not go forward while the hearing was pending. \textit{Md. Corp. \\& Ass'ns Code Ann. §§ 11-901 to 908 (1985 \\& Supp. 1985)}.
\textsuperscript{65} 547 F. Supp. 522, 525-29.
\textsuperscript{66} \textit{id.} at 529.
\textsuperscript{67} 547 F. Supp. 522, 532 (relying on \textit{Edgar} and \textit{Pike v. Bruce Church, Inc.}).
\textsuperscript{68} 547 F. Supp. 522, 533.
\textsuperscript{69} \textit{id.} (citing \textit{Kennecott Corp., Kidwell, and National City Lines}).
Take-over Bid Disclosure Act\textsuperscript{70} which had been amended\textsuperscript{71} to require a declaration of intent in connection with so-called “creeping tender offers”\textsuperscript{72} where the target was a Virginia corporation. The court, confronted with a two-prong challenge under the Commerce Clause, found that the principles announced in \textit{Edgar} with respect to impermissible indirect burdens on interstate commerce were controlling.\textsuperscript{73}

The court found the sole local interest supporting the statute to be the protection of Virginia shareholders. By contrast, Virginia could have no legitimate interest in protecting non-resident shareholders. Furthermore, the disclosure requirements of the Williams Act better served investors, as disclosure became mandatory once an investor or offeror had acquired 5 percent of a company’s stock, as opposed to the 10 percent trigger set by the Virginia act. So too, the state’s purpose was called into question by virtue of the exemption for purchases by a Virginia corporation of its own shares.

At the same time, the identifiable economic burdens resulting from the act were numerous, including the fact that the act would discourage investment in Virginia corporations; that it would impact on the ability of the free market to effectively price securities and allocate resources; and that it would reduce the incentives to incumbent management to perform well and thereby maintain a high market price for the target’s securities.\textsuperscript{74}

\begin{thebibliography}{74}
\bibitem{70} \textsc{Va. Code §§ 13.1-528 to 541 (1985)}.
\bibitem{71} \textsc{id., as amended in 1979}. The Virginia act applied when an offeror acquired more than 10 percent of the stock of a Virginia corporation through open-market purchases or otherwise, if the offeror had purchased more than 2 percent of the corporation’s stock in the last twelve months. At that point, the offeror had to refrain from further open-market purchases until it filed a statement with the Virginia State Corporation Commission setting forth its intent, the purpose of its (assumed) desire to change control of the company, the manner in which such change was to be carried out, and other pertinent information. The offeror was presumed to intend to change control of the target company and could only obtain an exemption after proving its benign purpose to the State Commission. 697 F.2d 576, 578.
\bibitem{72} The rationale for regulating “creeping tender offers” was that would-be offerors found that, pursuant to § 14 of the 1934 Act, they could strengthen their position before making a tender offer by continuing to buy shares after reaching 5% of the shares of the target and then filing on the tenth day. See Strode v. Esmark, Inc., 1980 Fed. Sec. L. Rep. (CCH) ¶ 97,538 at 97,805-06 (Ky. Cir. Ct. May 13, 1980); McCauliff, supra note 15 at 307.
\bibitem{73} New proposed SEC rules on takeovers, coming in reaction to the massive wave of huge mergers in the oil industry in the first three months of 1984, have in part focused on precisely this situation:
\begin{quote}
One target of the proposals is the “sneak attack,” which would be curbed by closing the ten-day period that allows investors to buy secretly as much stock as possible in a target company before filing disclosure of a 5 percent holding with the commission. The SEC rejected a recommendation to require registration 48 hours in advance, however, due to fluctuations in the stock price once the announcement is made. The precise filing time has yet to be determined.
\end{quote}
\end{thebibliography}
Furthermore, the indeterminate delay which might result from a hearing concerning the offeror's intent posed a heavy burden on interstate commerce.\textsuperscript{75}

The court concluded, under \textit{Edgar} and \textit{Pike v. Bruce Church, Inc.}, that although the burdens imposed by the Virginia act were less than those imposed on interstate commerce by the Illinois act at issue in \textit{Edgar}, the purported protections for resident investors in Virginia nevertheless were too speculative to sustain the statute's validity under the Commerce Clause.\textsuperscript{76}

By contrast to \textit{Telvest, Bendix,} and \textit{National City Lines}, the court in \textit{Agency Rent-A-Car, Inc. v. Connolly}\textsuperscript{77} upheld the Massachusetts take-over statute\textsuperscript{78} there in issue. The Massachusetts act sought to regulate "creeping tender offers" in much the same manner as had the Virginia act. With respect to the Commerce Clause challenges, the court simply remanded to the district court for determination of the issues in light of \textit{Edgar}, as the district court previously had not addressed those issues.\textsuperscript{79}

At the same time, the court reversed the district court's finding of preemption under the Supremacy Clause. The court first analyzed the split among the five \textit{Edgar} justices who had discussed the preemption issue, and then went on to distinguish the Illinois act and other similar laws as being in far greater conflict with the Williams Act than was the Massachusetts statute. The court found one critical distinction: in \textit{Agency Rent-A-Car}, the plaintiff had completely failed to challenge the disclosure, filing and hearing requirements of the Massachusetts law, but rather only had challenged the sanctions provision of the act. Given this procedural posture, the court held that all delay (and sanctions) which might result from application of the act could be avoided simply by full compliance with the statutory requirements.\textsuperscript{80} Such was not the case with other similar statutes which contained hearing and timetable provisions and which had certain delays built in to the regulatory framework.

In sum, with rare exception, the vast body of law both prior to and following \textit{Edgar} almost uniformly has held general state takeover statutes invalid on each of the three bases discussed in Justice White's opinion. The rare exceptions, such as \textit{Agency Rent-A-Car}, appear to be anomalous.

\textsuperscript{75} \textit{id.} at 580.
\textsuperscript{76} \textit{id.} at 582.
\textsuperscript{77} 686 F.2d 1029 (1st Cir. 1982), rev'd 542 F. Supp. 231 (D. Mass.).
\textsuperscript{79} 686 F.2d 1029, 1040.
\textsuperscript{80} 686 F.2d 1029, 1038-39.
III. Strategies for Attacking State Approval Requirements for the Acquisition of Public Utilities and Common Carriers

Any constitutional challenge to state approval requirements for the acquisition of public utilities and common carriers ("approval requirements" or "state approvals") must therefore be considered against the imposing background of case law concerning general state takeover statutes. As we have seen in the specific cases of the Nevada and California approval requirements, such requirements are worded in a far more general, non-specific manner than are the various general takeover statutes previously discussed. With respect to Nevada, the applicable law only states that a transfer of stock of a public utility which would result in a change of corporate control of the public utility or in the transfer of 15 percent or more of the common stock of the utility will be invalid without prior state approval.81 No specific provision is made within the public utility laws with respect to timetables, disclosures, or the conduct of hearings or investigations.82

Similarly, California’s public utility code simply provides that no corporation shall acquire or control a public utility organized and doing business within California, either directly or indirectly, without first securing state authorization to do so.83 No other specific provisions with respect to approval requirements are made. The initial question then becomes whether such industry-specific approval requirements necessarily engender the same constitutional problems as the general state takeover statutes, and whether such flaws are over-balanced by sufficient legitimate local interests.

Surely, although the state approval requirements may be said to reflect legitimate local interests in protecting resident investors and in regulating the internal affairs of resident corporations (as was the case with the general state takeover laws), their primary purpose is to ensure the continued proper functioning of public service-type corporations and the concomitant availability of critical public services. At the same time, however, the industry-specific approval statutes impose substantial burdens on interstate commerce, and also present the potential for serious conflict with the purposes and plan of the Williams Act.

By necessitating state approval for a sale of stock which would result either in the transfer of 15 percent of the common stock of, or in a change of control in, a public utility, Nevada law impacts directly on securities

81. Nev. Rev. Stat. § 704.410(8) (1985) (public utility is defined to include a railroad or a holding company which controls a railroad).
82. As previously discussed, Nevada had a separate general takeover statute which was held unconstitutional in Natomas v. Bryan, 512 F. Supp. 191 (D. Nev. 1981).
83. Cal. Pub. Util. Code § 854 (West Supp. 1985) (a railroad is considered to be a common carrier which in turn comes within the definition of a public utility under California law).
transactions across state lines. The same is true of California’s change-of-control approval requirements. Such transactions, executed by instrumentalities of interstate commerce including the mails and the telephone, normally will implicate situations where both parties are non-residents. States, however, have no legitimate interest in regulating transactions between non-residents.

Secondly, by their own terms, the state approval statutes do not merely regulate the implicated corporate body, but rather regulate the entire tender offer transaction which might, as one of its components, impact on an in-state utility or carrier. Accordingly, both the Nevada and California acts have assumed the state’s power to block a tender offer anywhere in the nation, not just in the home state.

So, too, the requirements of state approval in both California and Nevada before a change in control or transfer of stock takes place may result in the indefinite delay of a tender offer, occasioned by hearings or investigations at the state level. The potential for such delays, according to Congress, will necessarily tip the balance in a tender offer situation in the direction of the incumbent management, in contravention of the purposes of the Williams Act.

Similarly, the state statutes do not specify the criteria to be used by the states in rendering their decisions to approve or disapprove a transfer of control. An application for such approval may entail the offeror disclosing far more information than is called for by the Williams Act, thereby threatening to deluge investors with a mass of irrelevant data. Furthermore, the state decisions may encompass factors about the fairness of the proposed transaction, which would also contravene the plan of the Williams Act.

Finally, to the extent time delays, hearings, and investigations impinge on the potential for success of a tender offer the ability of the national free market to price securities and allocate resources effectively would be damaged.

In sum, each of the critical factors used to support the conclusion in Edgar and in the various federal circuit and district court opinions that general state takeover statutes are unconstitutional, exist in the context of the state approval requirements. This conclusion is best illustrated in the parallel context of the state insurance holding companies act cases. As previously mentioned, in at least four states—Missouri, Florida, Indiana, and Kansas—Supremacy and Commerce Clause challenges have been made to the insurance acts along the same analytical lines as the challenges to the general takeover statutes.

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84. Or, in the case of Nevada, on the intent to purchase at least 15 percent of a target’s common stock.
Perhaps the best example of this is presented by the district court's opinion in *National City Lines* where the court concluded that:

To uphold the challenged sections of the Insurance Act would permit the state to gain jurisdiction over a tender offer and to halt all purchases of stock merely on account of the fortuitous circumstance that the target company controls a domestic insurer. Since the Division of Insurance's interest in protecting policyholders does not extend to the regulation of securities, the challenged sections of the Insurance Act pose significant burdens on interstate commerce.

The court found that the Missouri insurance director could still engage in the regulation of the "business of insurance" pursuant to the McCarran-Ferguson Act and could ensure the protection of policyholders by a whole series of protective measures. Valid protective measures might include, but would not be limited to, specifying the content and form of insurance policies; setting rates; revoking licenses; and protecting against questionable management practices. To allow more than this, however, was to grant the insurance director the power to engage in "the regulation of securities" rather than the regulation of the "business of insurance," and would conflict with the "pervasive requirements" of the Williams Act. The court found that the Williams Act had preempted the authority of the insurance director "to regulate the relationship between a stockholder and the company in which he owns stock..." The court's finding was fully consonant with the statement in *Edgar* that "[t]ender offers contemplate transfers of stock by stockholders to a third party and do not themselves implicate the internal affairs of the target company."

In a similar case, *Gunter v. AGO International B.V.*, the Florida Insurance Holding Company Act was held invalid by a federal district court pursuant to a Supremacy Clause attack. The court reasoned that the Act contravened the purposes of the Williams Act because it required the disclosure of additional information not mandated by the Williams Act, and because it imposed serious problems of delay.

In contrast to *National City Lines* and *Gunter*, the district court in *Professional Investors Life Insurance Company v. Roussel* rejected Supremacy and Commerce Clause challenges to the Kansas Insurance

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86. Id. at 912.
87. Id. at 911.
88. Id. at 910.
89. Id.
90. 457 U.S. 624, 645 (citing Kidwell).
91. FLA. STAT. § 628.361.
Holding Company Act in a pre-
Edgar decision. The Kansas Statute re-
quired persons or related entities wishing to purchase more than 10 per-
cent of a Kansas insurance company’s stock to file an application with the
Commissioner of Insurance. The complicating factor, in the opinion of
the Roussel court, was the extent of the exemption provided by the Mc-
Carran-Ferguson Act, which allows states to regulate the “business of
insurance.” The court found that to the extent the Kansas act operated
to protect security holders, it did not receive McCarran-Ferguson protec-
tion. The court, however, stated:

Nevertheless, the KIHCA is safe from constitutional attack relative to the
Supremacy and Commerce Clauses as long as the KIHCA does not signifi-
cantly impede the purpose of federal securities regulation and does not
place an excessive burden upon interstate commerce.

The court then went on to find that the Kansas act merited McCarran-
Ferguson Act protection because it also served to protect the security of
policyholders. As such, state authority in the area of insurance regulation
should enjoy a presumption of validity. In specifically disagreeing
with the district court’s reasoning in National City Lines, the Kansas distric-
t court stated:

We recognize that [MITE Corp. v. Dixon, Kidwell, and Empire, Inc. v. Ash-
croft] provide some support for defendants’ position. These cases, how-
ever, are distinguishable on the grounds that they consider the
constitutionality of general takeover statutes. Such statutes must have a
greater impact upon commerce and be a greater impediment to federal se-
curities regulation than a law concentrating on insurance company transac-
tions. In addition, the statutes are not protected by McCarran-Ferguson.

The court in Sun Life Group, Inc. v. Standard Life Insurance Co. of
Indiana disagreed with the Roussel court’s application of the McCar-
rann-Ferguson Act, yet upheld the constitutionality of the Indiana Insurance
Company Holding Act there in issue. In addressing McCarran-Fer-
guson, the court stated:

95. 528 F. Supp. 391, 394.
97. Obviously, such a complicating factor does not exist in the context of state approvals for
acquisitions of common carriers and public utilities.
98. 528 F. Supp. 391, 402.
99. Id.
100. Id.
101. Id.
102. Id. A detailed analysis of the impact of the Edgar decision on the state insurance holding
company acts is presented in Webster, State Regulation of Tender Offers for Insurance Compa-
104. IND. CODE ANN. § 27-1-23 (Burns Supp. 1980) (current version at § 27-1-23 (Burns
Supp. 1985)).
Section 14d of the Securities Exchange Act, which is the federal statute under which the tender offer rules are promulgated, refers expressly by its terms to insurance companies. As a result the McCarran-Ferguson Act, 15 U.S.C. § 1012, is inapplicable by its terms. Moreover, under Securities and Exchange Comm'n v. National Securities Corp., 393 U.S. 453, 89 S. Ct. 564 (1969), the dissemination to shareholders is in the center of the area of insurance company affairs that is subject to federal regulation under the McCarran-Ferguson Act, 15 U.S.C. § 1012, and is not "the business of insurance" subject to exclusive state regulation.  

The court, however, went on to find that the Indiana Act did not conflict with SEC Rule 14d-2(b) insofar as the state insurance administrator construed the Act—a state takeover statute applicable only to insurance corporations—as permitting a tender offer to commence prior to the expiration of the Act’s 30-day waiting period; Indiana could require that the offer be expressly conditioned upon later approval by the administrator.  

IV. CONCLUSION  

In conclusion, with the exception of the Kansas insurance act decision in Roussel, there is essentially uniform authority on which to base Supremacy and Commerce Clause challenges to state approval requirements for the acquisition or transfer of control of a public utility or common carrier. With respect to Roussel, it should be remembered that that decision appeared before the Supreme Court’s opinion in Edgar and that the district court judge did not have the benefit of the Court’s pronounce-

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105. Sun Life, supra note 100, at 97, 117-18.  
106. Rule 14d-2, 17 C.F.R. § 240.14d-2 (1985), defines the circumstances under which a tender offer is deemed to have commenced. In particular, Rule 14d-2(b) triggers a tender offer if specific information is made public.  
107. See Sargent, supra note 9 at 692 n.18 and 710 note 145.  

Compliance with both state precommencement notification and waiting periods, and with the SEC requirement under Rule 14d-2(b) that an offer proceed immediately, generally will be impossible. See Ryndak, State Takeover Statutes Under Attack—Casualties in the Battle for Corporate Control—MITE Corp. v. Dixon, 30 DePAUL L. REV. 989, 991 note 14 (1981). The court’s analysis in Sun Life, discussed in the text supra, was one of the few isolated attempts to reconcile the apparently conflicting demands of antipathetic state and federal requirements, and thereby preserve the state statute.  

The court’s line of reasoning was the subject of later attack from commentators. So, for example, in Comment, Challenges to State Takeover Laws: Preemption and the Commerce Clause, 64 MARQUETTE L. REV. 657, 685 (1981), the writer in no uncertain terms concluded that “the administrative rules promulgated by the SEC [i.e., Rule 14d-2] made clear that state takeover laws are preempted by the Williams Act.” However, prior to the Court’s decision in Edgar, other commentators suggested that while existing state takeover acts would be found invalid under preemption and Commerce Clause attacks, modifications limiting the applicability of the various acts might be made so that they would comport with the Williams Act and with Rule 14d-2. See Comment, The Utah Takeover Offer Disclosure Act: Constitutional and Practical Considerations, 1979 UTAH L. REV. 583.
ment on the non-relationship of a transfer of stock vis-a-vis regulation of the internal affairs of a corporation.\(^{108}\) In light of the Court’s comment in Edgar, the argument is strong that Edgar and the analysis set forth in National City Lines would prevail over that in Rousser. Furthermore, it also should not be forgotten that all of the insurance act cases are complicated by the presence of the McCarran-Ferguson Act, a factor not present in the public utility/common carrier context.

It has been suggested that both Commerce and Supremacy Clause challenges could be made to industry-specific state takeover statutes, such as those of Nevada and California. In light of the fact that only three of the five justices who addressed the Supremacy Clause challenge in Edgar supported that challenge, it is problematic as to whether such an attack would continue to have persuasive effect in the future.\(^{109}\) The fact

\(^{108}\) 457 U.S. 624.

\(^{109}\) The preemption question is further muddled by the presence of § 28(a) of the 1934 Act, 15 U.S.C. § 78bb(a) (1982) which provides:

Nothing in this chapter shall affect the jurisdiction of the securities commission (or any agency or officer performing like functions) of any state over any security or any person insofar as it does not conflict with the provisions of this chapter or the rules and regulations thereunder.

State regulation of securities, specifically by means of so-called “blue sky” laws, antedated federal securities regulation and § 28(a) specifically was designed to preserve such blue sky laws. Comment, The Utah Take-Over Offer Disclosure Act: Constitutional and Practical Considerations, 1979 Utah L. Rev. 583, 593. Thirty-four years later the Williams Act was passed as an amendment to the 1934 Act without change being made in § 28(a) with respect to its application to the entire 1934 Act; in particular, no change was made and the legislative history does not address the need for clarification concerning the impact of § 28(a) on the continuing validity of state takeover laws. Accordingly, some confusion has arisen as to the applicability of § 28(a) to the Williams Act and its various state counterparts. The Supreme Court stated in dictum in Leroy v. Great Western United Corp., 443 U.S. 173, 182 (1979) that “[t]he section was plainly intended to protect, rather than to limit, state authority.” This language and the basic provisions of § 28(a) were cited by a number of commentators, in the years before MITE and before Edgar, as support for the propositions (1) that § 28(a) provided for dual federal and state regulatory authority over takeover offers; and (2) that Kidwell was incorrectly decided and that the preemption and Commerce Clause challenges to the state laws were invalid. See e.g., Comment, The Constitutionality of the Maine Takeover Bid Disclosure Law, 30 Maine L. Rev. 246, 257, 272-73 (1979).

Similarly, other commentators argued for the validity of such laws, at least where they were limited in application to domestic corporations with a substantial presence in the jurisdiction, or to “pseudo-foreign” corporations, with such presence, under the rationale that such laws are part “of the traditional sphere of state corporate law and not a form of state securities regulation designed to protect non-resident investors.” Sargent, supra n.9 at 729; see also Ryndak, supra note 104 at 997 note 46, 1004, 1019 note 199. Sargent, in particular, argued that a legitimate local purpose of the state statutes was to protect investors through the regulation of fundamental changes in corporate ownership and organization. This line of reasoning, obviously, has not been borne out by subsequent judicial decisions.

Furthermore, the Court of Appeals in MITE v. Dixon reasoned that § 28(a) was aimed primarily at preserving, and generally limited to, state blue sky laws. 633 F.2d at 491 n.5. See Ryndak, supra note 104 at 1001 note 77 (1981).

Recently, however, the SEC has again come to scrutinize the state/federal dichotomy in
that the First Circuit rejected a Supremacy Clause attack in Agency Rent-A-Car, although distinguishable on its facts, lends at least a small amount of credence to the suggestion that a preemption argument would prove to be a weaker line of attack than a Commerce Clause challenge.

Both on the facts and on the law, a strong Commerce Clause challenge could be mounted against the industry-specific state approval requirements. As suggested, the Nevada and California statutes present precisely the same substantial burdens on interstate commerce as did the general state takeover statutes, *i.e.*, by virtue of the state’s assumed power to regulate interstate securities transactions between non-residents and to block nationwide tender offers. The state interest in ensuring the availability of adequate public services can be served through a variety of means other than the state’s engaging in the “regulation of securities,” as was argued persuasively by the district court in *National City Lines*. Finally, unlike a preemption argument, a Commerce Clause analysis would be controlled by the principles set forth by a majority of the Supreme Court in *Edgar*.

In sum, even if state authority has not otherwise been preempted by federal statute, such state approval authority is subject to strong challenge under the Commerce Clause pursuant to *Edgar* and to a lesser extent under the Supremacy Clause as having been preempted by the Williams Act.

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considering new proposed federal takeover rules against the backdrop of the surge of massive mergers announced in the oil industry. The *Washington Post* reported in part:

The SEC agreed with the vast majority of the experts’ ideas. The few areas of disagreement involved the question of federal preemption of state laws. While the activities of bidders are largely regulated by federal law because tender offers take place in national securities markets, the actions of target companies are generally governed by state law.

The SEC refrained from adopting preemption on charters and bylaws provisions to restrict takeovers, but may preempt state laws as to issues of self tenders and crown jewels.


110. It is possible that such an argument might exist with respect to railroads and other common carriers under such federal statutes as the Staggers Railway Act of 1980, particularly as codified at 49 U.S.C. §§ 10501, 11343, and 11501 (1982). This article, however, does not address this issue.
The Legal Right Of A Port To Cargo
In the Age Of Containerization:
Going, Going . . . Not Quite Gone

J. STANLEY PAYNE, JR.*

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I. INTRODUCTION

In the past 5 years the United States has seen the transformation (if not the outright upheaval of) the American transportation system. Legislation has conferred upon the airline, trucking, railroad and intercity bus industries significant degrees of freedom from federal regulatory control and involvement. The foundation for the transformation of the maritime industry, however, was laid nearly 30 years ago through the use of technical innovation rather than through legislation. The birth of the "container revolution" in 1955 subjected ocean transportation to a...
change likened to the replacement of sailing ships by steam powered ships during the 19th century. With ports comprising an integral part of the maritime industry, the advent of containerization changed the existing maritime situation dramatically. Because the containerization of cargo provided shippers with an increased flexibility in routing their cargo, it subsequently represented a danger to the flow of cargo from the hinterland. Such flexibility would prove to be decisively fatal in what had been a 50 year battle waged by ports to protect that flow of cargo. The following article will explore the development of the federal protection of the flows of commerce which are exclusive or "naturally tributary" to individual ports or particular ranges of ports. Also addressed


9. The Virginia Port Authority, in fact, "chastised" Congress for not giving ample recognition to the importance of ports in its consideration of so-called "maritime reform legislation": Ports are integral components of the foreign commerce of this country, not merely insignificant funnels through which cargo is channelled. H.R. 1878 and the recently passed S.47 are best viewed as compromises between shippers and carriers, with added powers and protections for each, with ports not considered so important as separate components to command much specific consideration. It must be remembered, however, states and cities have invested millions, billions of dollars in shoreside terminals to facilitate trade. Ports spin-off billions of dollars in benefits to localities, states, and this nation as a whole. In other words, ports are big business and a growing vibrant industry and their views on shipping legislation warrant as much consideration as do those of steamship lines—both ports and carriers exist merely to serve the shipper.


10. "'Containerization is often referred to as 'intermodal transport' because of the ease with which containers can be transferred from one mode of transport to another. Thus, the shipper's proximity to a port is less important than before, e.g. a shipper in Chicago can ship containers destined for England through any number of East Coast U.S. or Canadian ports." G. SLETMO, & K. WILLIAM, LINER CONFERENCES IN THE CONTAINER AGE xxviii (1981).

11. "'Hinterland' has been defined as "that area within the nation where a port's exports are produced and where its imports are marketed." Interstate Com. Comm'n, Rail Services Planning Office, Rail Rate Equalization to and from Ports v. (July 7, 1978).

12. The first allegation of port discrimination pursuant to the Shipping Act, 1916 was Alaskan Rate Investigation 1 U.S.S.B. 1 (United States Shipping Board) (1919). The Port Differential Investigation, 1 U.S.S.B. 61 (1925) marked the initial examination of established cargo flows from interior points to particular port ranges.

13. Many cases have dealt with exclusivity of cargo to ranges (North Atlantic, South Atlantic, etc.) of ports. See, for example The Port Differential Investigation, 1 U.S.S.B. 61 (1925).

14. The doctrine of naturally tributary cargo has its foundation in Section 8 of the Merchant Marine Act, 1920. Pub. L. No. 66-261, § 8, 41 Stat. 992 (1920) which reads:

That it shall be the duty of the board, in cooperation with the Secretary of War with the object of promoting, encouraging and developing ports and transportation facilities in connection with water commerce over which it has jurisdiction, to investigate territorial regions and zones tributary to such ports, taking into consideration the economies of transportation by rail, water, and highway and the natural direction of the flow of com-
will be the impact of the evolution of containerization on the concept of "naturally tributary cargo", with a particular emphasis on the emergence of "load center" or "super ports". The article will conclude with a look at how to ultimately resolve the conflict between port rights and carrier practices within the context of the Shipping Act of 1984.

II. A PORT AND ITS FOUNDATION; THE HINTERLAND

The link between a port and its hinterland has been succinctly described in the following manner: "Waterborne commerce must flow through seaports with facilities for handling ships and the[ir] cargoes. The anchorage in quiet water is, however, second to the all important hinterland. Lacking that hinterland, harbors possessing great natural advantages can possess only strategic value." A stable dependable hinterland and the flow of cargo from it serves as the basis for the continued existence of the port itself. Although not quite as obvious, the hinterland also serves as a foundation for the umbrella of industry activity radiating from it. It is this latter link of cargo flow sustaining the commercial infras-
structure built upon the port that most clearly explains the zeal with which legal protection has been sought for ports (through the protection of their cargo flows). Magnified by the so-called "multiplier effect" the economic spinoff of port activity is substantial and far ranging. To illustrate, in 1979 the Port of Hampton Roads, Virginia generated 134,693 jobs (6% of the total state work force) in the Commonwealth, 80,000 of which were outside the port. Port related jobs earned 2.3 billion in income (10% of the salaries and wages in the state) and generated 267.4 million in personal and corporate taxes (over 8% of all taxes paid in Virginia in 1979). From a slightly different perspective, each ton of containerized cargo created $93.38 in revenue and every 169 tons of containerized cargo moving through the port created one job.

The dramatic impact of port activity is not unique; the generation of

18. The ratio between the total volume of sales (or income or employment) generated and sales directly related to the port is the multiplier for the port industry. The size of the multiplier depends on the structure, size and diversity of the port district's (or region's) economy. U.S. Dept of Com., Mar. Admin. Port Economic Impact Kit 9 (September, 1979) [hereinafter cited as Port Economic Impact Kit]. The geographical spread of the multiplier effect of a load center, or even simply a major port, may be nationwide. Port Development in the U.S., supra note 8, at 38-39.


20. Jobs in transportation and port services include stevedores, longshoremen, warehousemen, ship repair tug boat operators, marine survey, ship watch, ship chandlers, pilots, naval architects, launch service, ship cleaners, industrial marine supply, weighers and samplers, seamen's service, crane service, hydraulic repair, railroad and trucking, steamship owners and agents, freight forwarders/customhouse brokers, and state and federal government employees (Dept. of Agriculture, Coast Guard, Customs, etc.). id. at 16-21.

The Port of Baltimore boasts, for example, of 33 firms specializing in freight forwarding, three specializing in customhouse brokerage and an additional 36 firms performing both services. Maryland Port Administration, Port of Baltimore Handbook 1983-84 12 (1983).

21. Economic Impact of Virginia's Ports, supra, note 19, at Ch. V, VI.

22. id. at 35.

23. id. at 43.

24. Three examples serve to illustrate this point; first in 1981 the Port of Houston generated 31,699 jobs for Texas residents, 56 percent of which were generated by general cargo. Further, the port generated nearly 3 billion in revenue to the state and national economy with over 50 percent remaining in Texas, including $510 million to the banking and insurance sectors. Finally, the port generated $1.6 billion in personal income for the residents of Texas. Booz, Allen & Hamilton, Inc. (For the Port of Houston Authority) The Economic Impact of the Port of Houston, September, 1982.

Second in 1980, the port of Baltimore generated $1.2 billion in revenue and jobs for 79,000 Maryland residents (4% of the state's work force) Port of Baltimore Handbook (1983), supra note 20.

As a final example, on the average 2,000 forty foot containers per month pass through the port of Oakland as a result of a joint venture between General Motors and Toyota. The joint venture would directly generate 114 jobs and would indirectly generate 76 more jobs as well as
"community benefit." has served to justify the public financial aid and subsidies that have historically been extended to the majority of public port authorities. The fact that some governmental subsidy has been considered a general necessity to continued port viability further illustrates the fact that, even in the past, when cargo flows were protected both legally and through established patterns of transportation, port facilities have not traditionally produced income sufficient to cover their costs of operation. Tradition notwithstanding, an emerging trend is for state and local governments to virtually withdraw from the subsidization of ports and to force port authorities to depend increasingly on their own revenue for further growth and development. Revenue bonds have replaced general obligation bonds as the principal method of long term borrowing by ports. Such bonds are predicated on cargo flow and the generation of revenues to serve as security. The capital intensive nature of containerization with its costly, specialized terminals and related equipment has already placed enormous financial demands on public port agencies. The thrust towards self-sufficiency in the development and growth of ports has presented the ports with a problem that has two dimensions. On the one hand, a port with limited resources and a limited expectation of cargo flow will find the competitive position of its future revenue bond issues in the financial market less promising than other competing ports which have a more established business volume. On the other hand, those ports with bonds already outstanding and with a diminishing cargo base may also find their current bonds jeopardized.


For an overview on the economic impact of port activity in general, see *Port Economic Impact Kit*, supra note 18, and Mar. Admin., U.S. Dep't of Com., *What U.S. Ports Mean to the Economy*, (September 1978).

25. The term "Community" is used to refer to the "public," rather than connoting a geographical limitation. The national impact of the port industry is significant. In 1980, the U.S. port industry contributed $35 billion to the gross national product, generated $66 billion in direct and indirect dollar income from gross sales and services, and provided jobs for more than one million persons. In 1982 dollars, the total impact of the stevedoring/marine terminal industry [direct and indirect] amounted to $8.4 billion in revenues, 138,000 jobs, 2.5 billion in wages and salaries, 1.4 billion in business income, and 1.0 billion in Federal tax revenues. Mar. Admin., U.S. Dep't of Transp., *The U.S. Stevedoring and Marine Terminal Industry 3* (March, 1983).

26. See also, Mar. Admin., U.S. Dep't of Com., *Public Port Financing in the United States* (June, 1974) [hereinafter cited as "Public Port Financing"]).

27. *Port Development in the U.S.*, supra note 8, at 38.


This trend toward self-sufficiency may place the burden of generating port operating revenues on the ports' themselves, and the lack of steady dependable traffic may threaten the level of their daily functioning. Thus, with the stability of the hinterland of a port already the lifeblood for the massive industrial activity generated by it, its flow of cargo may additionally bear the burden of providing port operating and developmental revenues as well. The various pressures associated with pushing the ports toward self-sufficiency have placed an even greater premium on a stable, assured hinterland.

A. THE PROLIFERATION OF PORTS

Despite the apparent risk involved with an investment in the development of port facilities, the role of the port, both as a major industrial development in and of itself and as a "magnet" for economic development has led to their dramatic proliferation. As of 1980, the United States had 1,456 marine terminals located in 189 seaports, comprising 2939 deep-draft ship berthing facilities. Also included within these totals were 1,448 general cargo berths. In 1980 there were 137 container berths despite expenses which averaged as much as $17,102,500 per container berth in the North Atlantic range. Notwithstanding such associated costs, the industry as a whole annually spent upwards of $66 million between 1973-78 on port development. It is estimated that by 1990, at least 111 new container berths will have to be completed to meet the projected demands. In an industry that was "built" upon public investment, port authorities will be faced with a monumental task. There is every indication, however, that they will be willing to meet such demand. The ports of Baltimore, Charleston, Jacksonville, Los Angeles, Miami, Oakland, San

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32. Aside from the economic benefits, there is an intangible and allusive attraction to port activity, perhaps linked to the past when "the arrival of [a] ship was a great occasion." Ports are recognized as centers of "population [for] trade, industry and economic growth," Report to Congress, supra note 26, at 2. See also Mar. Admin., U.S. Dep't. of Com., National Port Assessment—What U.S. Ports Mean to the Economy, 4 (1978).


34. Id.

35. Id. at 20. Estimated cost for construction of a container berth (in 1977 dollars) on the Gulf coast, was $11,450,000; on the Pacific Coast, $9,360,000 and on the Great Lakes $13,598,000.

36. Id. at 23.

37. Id. at 73.

38. In 1980, out of the 167 container facilities nationwide, only five were privately owned. Id. at 71-74.
Francisco, Savannah, Seattle, and Tacoma, among others, have completed or are planning expansion of their container facilities. Additional container cranes have been added in Philadelphia, a port that has historically been beset by its location between the major container ports of New York and Baltimore. Boston, similarly situated between New York and Canadian gateways, has recently placed a new container facility into operation. Despite the high cost of specialized port facilities and the increasing difficulties encountered in obtaining financing for their develop-


Massachusetts faces the "location" problems similar to Philadelphia, by being in the shadow of New York. See Boston Fears Loss of USL Direct Calls, J. Com., Dec. 12, 1983 at 1A, col. 4 (United States Lines to discontinue direct call at Boston and serve the port by trucking cargo to New York); see Report to Congress, supra note 28 at 32-33; Port Development in the U.S., supra note 8 at 111-112, 131-132.


The Massachusetts Port Authority has been especially active and vociferous in defending its hinterland from encroachment. See Petition for Leave to Intervene of Massachusetts Port Authority at 3 Charter and Cargo Revenue Pooling Agreements in the US/Japan Trades 22 SRR 1010 (1984) (Japanese Flag Five Line Consortium space charter and revenue pooling agreements attacked as means to reduce port calls; "...Boston would be the No. 1 candidate for total elimination"); Reply of Massachusetts Port Authority to Petition Seeking Reconsideration of Maersk Container Service Co. Request for Temporary Operating Authority, I.C.C. Docket No. MC 164032 (Sub 1 (ITA) granted 1983) (attacking Maersk Container Service Company trucking rights application as providing for the transporting of its "local cargo for a tour of East Coast ports overland.")

The Massachusetts and Delaware River Port Authorities have jointly tried to prevent diversion of cargo to New York. See Schmeltzer & Peary, Prospects and Problems of the Container Revolution, 2 TRANSPI. L.J. 263, 299 (1970). Together with Hampton Roads, Massachusetts and Delaware port authority have expressed a definite bloc of concern with the North Atlantic Conference's application for intermodal authority, for fearing that such authority would be used to concentrate cargo at one or two load centers. North Atlantic Ports Split on Intermodal Proposal, J. Com., August 26, 1983, at 1A, col. 5.

42. Supra note 35 and accompanying text.
The construction of ports continues. Faced with the decision of whether they should supply additional facilities and services in an attempt to attract future traffic or whether they should wait for demand to develop, ports have historically built so as to avoid obsolescence. The structure of the American port industry, an industry built upon this nation's notion of free enterprise and competition, has subsequently resulted in an ever-increasing number of port terminals.

III. INNOVATION—CONTAINERSHIPS AND LOAD CENTERS

While containerization has presented ports and port authorities with an opportunity to share in an ever-increasing cargo volume, the opportunity has brought along with it a concomitant danger inherent in the new technology. Enormous investment in shoreside facilities is required to utilize the technology of containerization and these expenditures are in turn matched by the huge costs of the containerships that are constructed to utilize such facilities. The economics of containership operation are straightforward: large containerships are costly, ranging up to $55 million for each vessel. These ships represent investments that must be amortized at a rate approaching several thousand dollars a day. Because of such financial obligations, the non-revenue earning time must be kept to a minimum. The frequent service required of containerships results in fewer port calls and subsequently faster turn-around times. Calls must

44. Supra note 33.
47. Containerization ships are only in port an average of 25% of the time compared with a 60% rate for a conventional vessel. Note, Containerization and Intermodal Service in Ocean Shipping, 21 STAN. L. REV. 1077, 1088-89 (1969); See Sietmo & Williams, supra note 45 at 133.
48. The Japanese Consortium replaced 25-30 conventional vessels with 7 containerships on its East Coast-Japan service. Schmeltzer & Shepphard, supra note 46, at 216. The Comptroller General found that the rapid adoption of container technology accounted for the decline in the U.S. general fleet from that of the second largest in the world in 1965 to the eighth largest in 1979. Comptroller General, General Accounting Office, Report to the Chairman, Committee on Merchant Marine and Fisheries U.S. House of Representatives of the United States, Changes in Federal Maritime Regulation Can Increase Efficiency and Reduce Costs in the Ocean Liner Ship-
be restricted to ports offering substantial cargo volume capacity and the opportunity for a rapid turn-around. There is therefore an incentive to concentrate cargos in as few ports as possible—this is the basis for the container "load center" port.

The concept of load centers and the economics necessitating them are not new. Their establishment was predicated upon the development of an inland transportation structure that can legitimately funnel cargo away from the weakening inland boundaries of other ports. The continuing maturation of intermodalism has provided steamship lines with the tools needed to supplement the long established practices used to draw cargo into load centers. The flexibility provided by containerized

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ping Industry, 12-14 (July 2, 1982). The trend is toward replacing older ships with new, larger containerships on something close to a two-for-one basis. Fewer Containerships Expected to Handle Growing Tonnage, J. Com., December 13, 1982, at 1C, col. 5.

New "round-the-world service" by steamship lines has placed even greater time constraints on vessel utilization. See Round the World Service Begins As Big Fleets Hit the High Seas, J. Com, December 10, 1984, at 1C, col. 3.

49. Load centers must be heavily financed, to provide equipment needed for fast vessel turnaround. For example, three of the carriers calling at Baltimore now request three cranes per vessel when the equipment is available. Load-Center Ports Seem Inevitable, J. Com., February 1, 1984, at 12A, col. 2. Such substantial funding may require private participation, creating such problems for smaller ports as such funds are inevitably concentrated on load centers. From a technical standpoint, the sheer size of the new 4,200 TEU ships of U.S. Lines may preclude calls except at the world's largest container facilities. American Shipper, supra note 46 at 33 (June, 1983).

50. The Economic Impact of Virginia's Ports, supra note 19. Load centers have been referred to as base or principal ports, Container Feeder Systems, supra note 46, 217 note 8; "centers," note, Containerization and Intermodal Service in Ocean Shipping, 21 STAN. L.R. 1077, 1093; "intermodal cargo gateways," Load Center Ports Seem Inevitable, supra note 49; and "superport", Talbot, The Dawn of the Superport—Will it Happen Here, Tidewater Virginian 44 (October 1983).


51. Discussion focusing on intermodalism must include three terms exclusive to shipping:

Landbridge—method of shipping from Far East ports . . . to Europe, by using water transport across the North American Continent (by rail) to an East Coast port on the Atlantic Ocean, and water transport again on to a European port—essentially "bridging by land" between Asia and Europe across America.

Mini-Bridge (often spoken as mini-landbridge)—a movement from a Far East port to a U.S. East Coast port that involves water transport to a U.S. Pacific Coast port and then overland transport to a U.S. East Coast port. Another mini-bridge system in effect and working is from a U.S. Gulf port to a Far East port, utilizing overland transport from the Gulf port to a U.S. West Coast port and then water transport to a Far East port. Micro-Bridge—the shipment moves directly from the inland point to a port. Whelan, "Bridges . . . Once and For All", Jacksonville SeaFarer 4, 5 (December, 1979).

"Microbridge" service was initiated as late as 1978 but is predicted to account, for one day up to 70% of all container movement in the United States international ocean trade. See Shreffler, "How can Microbridge Survive," American Shipper 38 (May 1982).

In each of the three, the container moves under a single or through bill of lading—a single
transport, along with the rapid growth of intercity trucking and the development of TOFC/COFC\textsuperscript{53} railroad services has resulted in a major shift of inland traffic patterns towards the ports and has dissolved the integrity of

factor through rate (covering ocean and land transport and terminal charges) is charged, Wetherell, "\textit{Bridges... Once and For All}," Jacksonville Seafarer 4, 5 (December, 1979).

It has been called "the ultimate in ratemaking" giving a shipper both facility in dealing with costs, and the advantage of a single carrier assuming liability for the cargo's entire movement by land and sea." Schoedel, \textit{Intermodal Ratemaking to Cause Major Change in North Atlantic Box Trades}, J. Com. Dec. 12, 1983, at 13c, col. 5. Seven conferences were recently granted authority by the Maritime Administration to set collective intermodal ("bridge") rates in the North Atlantic trade may be the final tool necessary for the development of load centers, for the single factor rates to interior points will be published by the conference, with member carriers quoting the same rate but deciding individually which port to use. See Richardson, \textit{Effects of Intermodalism—On Cargo Gateway Selection and The Port Industry}. World Wide Shipping/World Ports 83 (1984).

For a discussion of the foundations for load center, "bridge" service, and the relationship between the two, see \textit{Load Centers and Landbridges Move to Center Stage,} Container News, June, 1985, 12.

52. Such "long-established" practices have generally been utilized to "equalize" the shipper's cost of using a more distant "load center" with that to the port nearest the cargo's origin. In Sea-Land Services, v. South Atlantic & Caribbean Line, 6 SRR 1105, 1112 (F.M.C. 1966) (SRR: Shipping Rules and Regulations), the Commission discussed the various practices used to effectuate port equalization, excerpted here:

Port equalization is accomplished in various ways. In its simplest form (sometimes called "equalization" in contradistinction to "proportional rates" or "transshipment"), the carrier pays to the shipper or, sometimes, to the inland carrier directly, the amount by which the cost to the shipper of overland transportation to the port of loading exceeds the cost of overland transportation from the same point of origin to the nearest port. (Note: this is often referred to as "absorption," as the carrier "absorbs" the difference. See City of Portland v. Pacific Westbound Conference, 4 F.M.B. 664 (1955).

A more complicated method involves "proportional rates," accomplished through the deduction of specified differentials from ocean tariffs where shipments originate at certain points defined in the tariff, see \textit{City of Mobile, infra note 82}.

A similar method, although relatively limited in scope, was proposed in \textit{Proportional Commodity Rates on Cigarettes and Tobacco, supra}. There the basic commodity rates on certain tobacco products, from New York to Puerto Rico, were to be subject to deduction of specified differentials according to the location of the Virginia or North Carolina manufacturing plant at which the shipment originated. In each case, the differential specified in the tariff would have been equivalent to the exact amount by which the motor-carrier rate from point of origin to New York exceeded the motor-carrier from the same point to Baltimore. By means of these so-called proportional rates, the carrier would achieve precise equalization against the port of Baltimore on the commodities.

Port equalization may also be effected through "transshipment." As used here transshipment refers to the movement of cargo, usually by land carrier, in the water carrier's name and at its expense, from a dock or terminal at the port where it is originally delivered by the shipper to the water carrier, to the dock or terminal at another port where it is loaded aboard a vessel of the water carrier. Although sometimes employed when the water carrier, for operating or other reasons, does not make a scheduled call at the port where the cargo is delivered, transshipment is also recognized, along with equalization, as a method of meeting the competition of carriers who call directly at a port where the equalizing or transshipping carrier does not call.

53. \textit{Port Development in the U.S., supra} note 8, at 21. The nomenclature of inland transportation of containers is COFC (Containers-On-Flat-Car), or the movement of cargo containers on flat cars by rail, and TOFC (Trailer-On-Flat-Car); the movement of highway type trailers on rail operated flat cars. TOFC is also called "piggyback." I.C.C. Rail Service Planning Office, \textit{Rail Rate Equalization To And From Ports, Preliminary Report V} (July 7, 1978).
their hinterlands, causing such services to overlap significantly. A policy dilemma has resulted.

IV. PORT VS. CARRIER—THE POLICY DILEMMA OF DEREGULATION

While the maritime and airline industries have faced the transition of deregulation through different means, certain similarities concerning deregulation can still be drawn. The emerging concept of smaller ports or inland carriers feeding a container load center port closely resembles that of the hub-and-spoke system prevalently employed in the airline industry. Just as small communities feared that deregulation of the airlines would bring about a loss of service or inadequate substituted service at best, small ports also fear that the loss of a dependable hinterland will severely cripple their service and activities. The analogy however, is not complete. The evolution of intermodalism has given carriers the ability to feed their hubs overland while bypassing some smaller ports completely. Unlike the Civil Aeronautic Board's guarantee of retaining some level of service to smaller communities, such guarantees have never been

54. North America cannot be easily split up into smaller segments for the purpose of analysis. Overland transport connections mean that ports in different geographical ranges can share overlapping hinterlands. Subsequently the port rotations adopted by many carriers have caused different port ranges to become interlocked. High Service Standards Prevail in North Atlantic Trades, Lloyd's Export Shipping 6 (Jan./Feb. 1983). Put in another way, "[t]he hinterlands of individual ports are no longer mutually exclusive but overlap, [and . . .] extensive areas of the United States are served by more than one port, [and are] commonly served by several ports or even ranges of ports on different coasts." Port Development in the U.S., supra note 8, at 33.

55. For an examination of the phenomenon of the "hubbing" of airline operations, see Civil Aeronautics Board, Report to Congress, Implementation of the Provisions of the Airline Deregulation Act of 1978, 9, 10 (January 31, 1984) [hereinafter cited as "CAB Report"].

56. The analogy between the two industries, and their regulatory burden, is interesting. The Federal Aviation Act, 49 U.S.C. 1302 et. seq., the basis for the regulation of airlines until 1978, stated that things vested with the public interest included: "(b) the regulation of air transportation in such manner as to recognize the inherent advantages of . . . carriers and (c) The promotion of adequate, economical and efficient service by air carriers at reasonable charges, without unjust discrimination, undue preferences or advantages, or unfair or destructive competitive practice." These goals parallel to some extent those of maritime regulation. See note 60 infra and note 14 supra. It is not surprising that the fear of smaller communities regarding the loss of regulatory protection curtailling carrier service is shared now by ports. It was also predicted that economically marginal routes to smaller cities, and low traffic density sectors would simply be abandoned by the airlines. See Dupre, A Thinking Person's Guide to Entry/Exit Deregulation in the Airline Industry, 9 TRANSP. L.J. 273, 282-3 (1977).

57. The Airline Deregulation Act of 1978, 49 U.S.C. 1301 et seq. has as its policy the encouragement of competition, the development of feeder or satellite airports, and seeks to maintain adequate service as well. To counteract the displacement of service, the Act provides guaranteed "essential air service" to smaller American communities. See Dubuc, Significant Legislative Developments in the Field of Aviation Law, 45 J. AIR L. & COM. 29-32 (1979). See also Havens & Heymsfield, Small Community Air Service Under the Airline Deregulation Act of 1978, 46 J. AIR L. & COM. 641 (1981).

Substitute services and smaller nonjet aircraft were introduced, with many airlines adopting
within the statutory powers of the maritime regulatory bodies of this country.\textsuperscript{58} Through its own decisions, the Federal Maritime Commission has been forced to acknowledge carrier needs for flexibility and freedom while at the same time recognizing that such freedom and flexibility could subsequently saddle the port industry with facilities that could easily become redundant because of economizing by steamship companies.

V. THE DOCTRINE OF NATURALLY TRIBUTARY CARGO

The Federal Maritime Commission (FMC) and its predecessors,\textsuperscript{59} entrusted with the protection of shippers, steamships and ports, have been forced to apply statutes passed in 1916\textsuperscript{60} and 1920\textsuperscript{61} to a shipping in

a hub and spoke concept, by connecting a major air center with the surrounding smaller communities. Substituted service, as a means of protection, has not been entirely adequate, however. "Although this approach increases the overall efficiency of the services provided, it cannot counteract the detrimental effects on air service caused by a decrease in the number of seats on departing flights and the diminished quality of service experienced by the smaller community." See Meyer, Section 419 of the Airline Deregulation Act: What Has Been the Effect on Air Service to Small Communities, 47 J. AIR L. COM. 151, 167 (1981). Among the negative effects of such substitute service has been a decrease in the attractiveness in locating in new communities. Id. at 175. See also CAB Report, supra note 55.

Airline regulatory reform was also opposed by airport operators, who feared, as did the ports, that carrier freedom would undermine their financial stability. One commentator, however, felt that deregulation would lead to "less monument building", or capital investment several times that justified by reasonably foreseeable levels of traffic. Kelleher, Deregulation and the Practicing Attorney, 44 J. AIR L. COM. 261, 290 (1978).


60. Allegations of violation of Sections 16 First and 17 of the Shipping Act, 1916 are the crux of port discrimination cases. Section 16 First 46 U.S.C.A. § 815 (Cum. Ann. Supp. 1983) makes unlawful to . . . make or give any common carrier by water or any other person subject to this chapter, either acting alone or in conjunction with any other person, directly or indirectly . . . any undue or unreasonable preference or advantage to any particular person, locality, or description or traffic in any respect whatsoever, or to subject any particular person, locality, or description of traffic to any undue or unreasonable prejudice or disadvantage in any respect whatsoever.

Section 17 provides that:

no common carrier by water in foreign commerce shall demand, charge, or collect any rate, fare, or charge which is unjustly discriminatory between shippers or ports, or unjustly prejudicial to exporters of the United States as compared with their foreign competitors.

Section 17's prohibition against undue discrimination among shippers could not logically be applied to ports. Discriminatory practices involve carriers exacting different payment from shippers using the same carrier, from the same point of origin and to the same point of destination.
industry that has undergone significant technological and structural changes since such statutes were enacted. Commission difficulties have never been greater than when the Commission is forced to reconcile the interests of the ports and the carriers, interests that have dramatically diverged along with the growth of containerization.

The "law" of discrimination against ports began as early as 1919 and has continued to evolve along with the maritime industry. From the

Discrimination among ports, however, must always involve two ports. Undue discrimination under Section 17 should be viewed as undue or unreasonable preference or prejudice under Section 16 First. Council of No. Atl. Shipping Assoc. v. American Mail Lines, 17 SRR 781, 839-47 (F.M.C. 1977). See also Heavy Lift Practices and Charges, 17 SRR 505 (1977) (discussion of undue preference, prejudice under Section 16 First and unjust discrimination under Section 17).

61. See note 14 supra, and accompanying text. The Merchant Marine Act, 1936 contains specific port protection language. Section 205 provides:

Without limiting the power and authority otherwise vested in the Federal Maritime Commission and the Secretary of Transportation, it shall be unlawful for any common carrier by water, either directly or indirectly, through the medium of an agreement, conference, association, understanding, or otherwise, to prevent or attempt to prevent any other such carrier from serving any port designed for the accommodation of ocean-going vessels. [One can not prevent a carrier] located on any improvement project authorized by the Congress ... lying within the continental limits of the United States, [from providing service] at the same rates which it charges at the nearest port already regularly served by it.


Section 205 is incorporated into Shipping Act considerations. In Sacramento-Yolo Port District v. Pacific Coast European Conference, 12 SRR 528 (F.M.C. 1971). The port of Sacramento instituted a barge service from Sacramento to San Francisco, offering the service to carriers and not shippers. The conference agreement governing the activities of the steamship lines that might use the prohibited absorption of barge service expenses. Sacramento alleged that the prohibition violated Sections 15, 16 First, and 17, and was contrary to Section 205 since it prevented lines from serving the port.

The Commission held that activity which contravened Section based on the legislative history of section 205, activity which contravened sec. 205 clearly was not approvable under Section 15. The commission and struck down the nonabsorption provision as contrary to the public interest under the latter section. Id. at 537. In a later case, Associated Latin Freight Conferences, 12 SRR 985 (F.M.C. 1972), the relationship between the Shipping Act and the Merchant Marine Act, 1936, was examined, with specifically Section 205 serving as the single legal issue. That the Commission surmised [the fact that different agencies may have been primarily responsible for enforcing the two sections does not mean that the substantive or policy content of those sections exist in a vacuum independent of each other. Id. at 989. Further, [the fact that Section 205 was not assigned to the Commission and Reorganization Plan No. 7 [does not indicate that it was an affirmation of] the intent of Congress to dilute, in any manner, the policy or proscriptions set forth in that section. Id. Despite the fact that the Commission has no specific authority to enforce Section 205, Section 205 could not "operate in its own statutory vacuum oblivious to the overall policy or objectives of Congress. Id. The Commission application of Section 8 of the Shipping Act was cited because it provides an expansive interpretation of the available rights. Id. Apparently overruled was India, Pakistan, Conference—Discount Tariff Rule 9 SRR 727 (F.M.C. 1967) (a proceeding brought under Shipping Act, not under Merchant Marine Act, which precluded consideration of Section 205 principles).
initial cases that formed the historical foundations of the present port/carrier conflict arose the distinct interests that would have to be balanced: the interests of the ports; the interests of those who gained an advantage or who were disadvantaged through carrier practices; the interests of steamship lines; the interests of shippers, and most importantly the interests of the American public. It suffices to say that cases in this area are decided on the basis of what interests are the most deserving of the protection of the Commission. Commission decisions can also be rendered based upon the perceived reasonableness of the "methods" utilized by steamship lines to serve the hinterland of a port without the necessity of a direct ship call. Such a notion of "fairness" was to become a formal standard of the Commission in the late 1970's. Another consideration that permeates this long line of port discrimination cases is the extent to which technological advances outdate Commission policy and the degree to which such policy is either modified in recognition of and to accommodate those changes, or is maintained in resistance to such change. The strength of Section 8 of the Merchant Marine Act (MMA) reflects Congressional policy regarding the protection of ports and illustrates the extent to which rigid adherence to such protection could stifle innovation.

VI. EARLY CASES

In 1919, during the infancy of the Shipping Act of 1916, the United States Shipping Board (USSB) instituted a general investigation into the rates, regulations, and practices of ocean carriers involved in the Washington State Alaska trade. This investigation would mark the beginnings of the first port discrimination case.

In Alaskan Rate Investigation, Anchorage farming and coal interests contended that higher ocean rates were being charged between Juneau and Anchorage than were being charged at Puget Sound ports, and that this practice subjected Anchorage to unjust discrimination. The USSB agreed that the price differential was unduly preferential to the Puget Sound ports and prejudicial to the Anchorage ports. The USSB found that much larger quantities of commodities would have moved through the Anchorage ports if the rates at this port were not 40 to 50% above the rates charged at the Puget Sound ports. Furthermore, the defendant steamship company could not show any justification for the differential and they themselves testified that the rates charged at the different ports

63. Alaskan Rate Investigation, 1 U.S.S.B. 1 (1919).
for the commodities in question should be equalized.\textsuperscript{64}

Aside from its purely historical significance,\textsuperscript{65} the decision in \textit{Alaskan Rate Investigation} suggested a two step test for the consideration of allegations of port discrimination. Under the first step, an aggrieved port (or port interest) would have the burden of proving that the rate or practice has a detrimental impact on its flow of cargo.\textsuperscript{66} Second, once this causal link has been established, carriers could then offer evidence justifying the practice and could then balance their interests with those of the complainant ports and shippers.\textsuperscript{67} Such a decision underscores the important link between the ports and their hinterland, while adding weight to the general premise that whatever burdens the flow of products from a port’s hinterland necessarily damages the port.\textsuperscript{68}

In the next two cases, the broad scope and impact of the practices in question are pivotal with regards to the evolution of the right of a port to cargo.

In the first case, \textit{The Port Differential Investigation},\textsuperscript{69} a system of rate differentials set by North Atlantic, South Atlantic, and Gulf steamship conferences in the heavy U.S.-European trade route (reflecting the differences in operating costs among the three ranges) was alleged to violate Sections 16 and 17 of the Shipping Act.\textsuperscript{70} Unlike \textit{Alaskan Rate Investigation}, in which rate differentials precluded shippers in the hinterland of one

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\item \textit{Id.} at 11.
\item In upholding the tariff rule that required vessel calls at a private dock to offer a minimum of 25 tons of freight, the Shipping Board would also be forced to weigh the advantages, disadvantages, and legality, of limiting port calls to load centers, the steamship owned docks. Disadvantages included the following: increased steamship line costs in handling several small shipments rather than one large one, the issuance of separate shipping receipts, thus creating separate way bills and expense bills. The commission, in an analysis that is still applicable to the present day concept of load centers, reasoned that if shippers are required to call at ports for amounts of cargo smaller than the minimum, "ships would be seriously delayed by calling at various loading places for small shipments, . . . [and this would necessitate the use of] more circuitous routes of travel and in decreased efficiency of operation", contrary to the "public interest."  \textit{Id.}
\item Commonly called the "but for" or "sine qua non" rule in actions based in tort, it provides that "[t]he defendant's conduct is not a cause of the event, if the event would have occurred without it."  W. PROSSER, HANDBOOK OF THE LAW OF TORTS 238-9 (4th ed. 1971).
\item Steamship lines could attempt to show that the two ports were "substantially dissimilar" or not "substantially similarly situated," thus justifying the differentials. \textit{Supra} note 63 at 10, 11.
\item Underscoring the link between hinterland and port, the shippers asserted that undue discrimination against the port was, in essence, discrimination against them. Compare with Board of Commissioners v. Seatrain 2 U.S.M.C. 500, 504 (1941) "A port and its transportation service are indissolubly linked together, are interdependent and a practice harmful to one injures the other."
\item The Port Differential Investigation (United States Maritime Commission) 61 (1925).
\item South Atlantic interests asserted that their rates were set differentially higher than for North Atlantic ports, and that this violated Sections 17 and 18 of the Shipping Act, 1916. Section 18 provides, in part:
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port from competing effectively with shippers in the hinterland of another port, *The Port Differential Investigation* focused on the competition among three port ranges for the same cargo which came from the industrial U.S. Midwest.

As in the *Alaskan Rate Investigation*, such allegations faced a two-tiered level of scrutiny: one excluding the rate differentials, more cargo would have moved through the aggrieved port (or port range); two carriers could not justify their rate or practices by factors such as the volume of traffic handled at the port, the competition or distance among the ports, the advantages of location of one port over that of another, the character of traffic at the port, the frequency of service at the port, or the cost of operations at the port.\(^71\) The fact that such aforementioned factors could be successfully utilized in the defense of a rate or practice was clearly elucidated in a preliminary statement issued by the Board in which "the character of discrimination inhibited by these provisions (Section 16 and 17 of the Shipping Act of 1916) is discrimination which is undue, unreasonable, or unjust."\(^72\)

In *The Port Differential Investigation*, the Board focused on the hinterlands of the respective port ranges so as to determine the impact of the rate differentials. The Board found that the South Atlantic and Gulf ports primarily drew "low class, unmanufactured articles. . . from territory. . . recognized as local to [such] port groups" while the North Atlantic range captured a substantial volume of "high-class package freight" from the Midwest market, a market deemed to be a competitive area for all three groups. Moreover, witnesses representing the South Atlantic and

\[\text{"(a) Every common carrier by water in interstate commerce shall establish, observe, and enforce just and reasonable rates, fares, charges, classifications, and tariffs, and just and reasonable regulations and practices relating thereto and to the issuance, form, and substance of tickets, receipts, and bills of lading, the manner and method of presenting, marking, packing, and delivering property for transportation, the carrying of personal, sample, and excess baggage, the facilities for transportation, and all other matters relating to or connected with the receiving, handling, transporting, storing, or delivering of property.}\]

\[\text{[Further]... Whenever the Commission finds that any rate, fare, charge, classification, tariff, regulation or practice, [which is] demanded, charged, collected, or observed by such carrier is unjust or unreasonable, it may determine, prescribe, and order enforced a just and reasonable maximum rate, fare, or charge, or a just and reasonable classification, tariff, regulation, or practice, was deemed inapplicable by the Board and was not considered. 1 U.S.M.C. at 63.}\]

\[\text{Conversely the Norfolk Port Commission, representing the southernmost port in the North Atlantic range, conversely, attacked rates set at parity among the three ranges and certain commodities as violative of Sections 16 and 17. \textit{id.} at 64.}\]

\[\text{Because the focus of the Board's investigation and discussion were the fixed rate differentials set among the three ranges, this will be the focus for the purpose of this paper.}\]

\[71. \text{The Commission stated, however, that it did not concur in the theory that a carrier is justified in burdening a port with a differential for the sole and only reason that the cost of operation from that port is greater than from some other port. \textit{id.} at 69.}\]

\[72. \text{\textit{id.} at 65. See text accompanying note 60, supra.}\]
Gulf port interests testified, in a statement that was to be fatal to their cause, that the normal flow of Midwest cargo was through the North Atlantic ports, and that "[in the] absence of congestion or [the] inability of such ports to handle this traffic, it is not likely, even with parity rates, that any appreciable volume of it [would] move through the Gulf or South Atlantic ports.\textsuperscript{73} In other words, factors other than the rate differentials determined the direction of the flow of cargo\textsuperscript{74} and therefore the threshold of causation had not been met.

The statutory right of a port to federal protection of its cargo base was not specifically addressed by the Board in its decision in The Port Differential Investigation. The interpretation of the Merchant Marine Act of 1920 (MMA) and particularly Section 8 of the Act promoting the development of ports through the protection of cargo was, however, vigorously

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\textsuperscript{73} 1 U.S.M.C., at 68. Port development in the United States was, to no small degree, dependent on the port's vital link to its hinterland, first by road and inland waterway, later by canals and most importantly, railroads. The rail networks expanded, westwardly and rapidly into the developing "Western hinterland," culminating in 1826 with two all-rail routes linking New York and Chicago. Midwest links to other North Atlantic ports followed. \textit{Port Development in the U.S.} at 15-18.

Southern and Gulf ports would "reach" the interior somewhat later. Prior to the latter part of 1919, there were virtually no through joint export rates from the interior territory of the country to the Gulf and South Atlantic ports. Interior territory roughly points eastward of a line drawn from Chicago, through Indianapolis to Cincinnati. Railroads serving the "southern" ports, unable to reach this industrial area with their own rails, could only do so with joint through rates with, eastern carriers that served the North Atlantic ports with their own rails from that territory. Such joint through rates were established only with the assumption of Federal control over the railroads in 1919 during wartime emergency. \textit{See generally} Export and Import Rates To and From South Atlantic and Gulf Ports 169 I.C.C. 13 (1930).

After the war, South Atlantic and Gulf railroads proposed an adjustment in their federally-established joint export through rates with eastern carriers, asserting that only with differentially lower rates could their disadvantages be offset to any extent and "enable foreign commerce to move freely" through Southern and Gulf ports. In justification of such an adjustment, and highlighting their disadvantages, South Atlantic and Gulf witnesses blamed "the established trend of cargo movement between the North Atlantic and foreign ports and the tendency of shippers to prefer routes they have long been accustomed to use,". Export and Import Rates, 169 I.C.C. at 34. They attributed their lack of success in directing a more than minimal flow of manufactured goods through their ports to their concomitant lack of success in attracting fast, frequent steamship service, which in turn could be attracted only by higher rates attainable for carriage of manufactured goods. \textit{id.} at 37. Caught in a vicious circle, the South Atlantic and Gulf ports, without the populous, industrial hinterlands of the North Atlantic ports, and with no "presence" in the interior of the country, were outlets only for a limited number of raw products of the south from territory adjacent to the ports. \textit{id.}

\textsuperscript{74} Other ports in the North Atlantic not only did not enjoy the advantages of the port of New York vis-a-vis southern ports but in fact labored under many of the same handicaps. 169 I.C.C. at 51. New York's advantages included being the location of the headquarters of a majority of the principal steamship lines and most of the export and import brokers controlling traffic. \textit{id.} at 50-51. New York also had many more sailings and service to more foreign ports by larger and faster steamships, and superior banking facilities. Differential Rates 11 I.C.C. 13, 27 (1905).
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advanced by the port interests.\textsuperscript{75} The Board at least acknowledged the concept of "tributary" cargo flows in its analysis, focusing on the "natural flows" of cargo to the respective port ranges. The Board also focused on Section 8 by stating that "in the great public interest it would seem obvious that rate structures should be made so as to permit the flow of traffic to pass through as many ports as [the] economics of transportation and distribution will allow."\textsuperscript{76}

\textsuperscript{75} The hearing transcripts indicate some confusion over the applicability of Section 8. Witness H.H. Haines, Vice President and General Manager, Houston Chamber of Commerce, was told after specifying the provision, that he "did not have Section 8 in mind" because it did "not authorize the Shipping Board to remove discriminations." His response was that while the authority was not specified in the provision itself, "there are provisions of the Shipping Act which do, and the expression of those sections of the Merchant Marine Act and Transportation Act indicate very clearly the intent of Congress." Hearing Record, Oct. 10, 1924 at 847-48, The Port Differential Investigation 1 U.S.M.C. 61 (1925).

Matthew Hale, representing the South Atlantic Steamship Association went further, providing a history of the advantage of North Atlantic ports over those in the South Atlantic, recognized by the United States Congress when Section 8 was framed:

In other words, just to review, in 1860 we were at least even with the North Atlantic, and according to statistics a little bit ahead. In 1860 to 1865, it was not economic law which developed the foreign trade of New York. It was northern armies and northern navies which cut the South off, and from 1865 to 1877, the critical period in the building up of the commerce of the United States, it was not economic range that built up the North Atlantic, it was negro domination of the South, and at the same time railroad building by the North helped by taxes—just get this gentlemen—out of the national treasury to which the South contributed. In other words, while we were being subjected by negroes in the South, we were helping to pay for the railroads built from the North Atlantic to the Middle West and the far West, which are now to be used, thirty or forty years later, as a reason for our continuing to stay in subjection because of, first, military domination, second, political domination, and third, an arbitrary system of rail rates, and this is what diverted this traffic to the North Atlantic.

It was for this injustice that Congress enacted Section 8, asserted Hale. Hearing Record, November 25, 1924 at 911 The Port Differential Investigation. Id.

Richard K. Hale, for the Department of Public Works, Commonwealth of Massachusetts asserted that the case must be decided in light of the broad principles of the Transportation Act (1920) and the Merchant Marine Act (1920), agreeing with the southern ports "in support of the proposition that as many channels of trade as possible ought to be opened for the flow of the Nation’s business." "The new law," he summarized, "contemplates that the railroads should have adequate rates to sustain them in order that they might render service. It provides consolidations of railroads to eliminate wasteful routes. It provides for the development of ports and you were to cooperate with the Secretary of War in that respect. It provided for a national fleet of merchant vessels under your direction. It provided for the coordination of rail and water transportation in the interest of the Nation."

Hearing Record, November 25, 1924, at 969-970, The Port Differential Investigation. Id.

\textsuperscript{76} This was advanced by counsel for the Port of New York Authority in conjunction with the New England ports, 1 U.S.S.B. at 71. Both were certainly aware of the conclusion earlier by the I.C.C. "[that] the maintenance of equal rates through all ports would divert traffic to New York to a much greater extent than it at present moves through the port." In the Matter of Differential Rates 11 ICC 13, 28 (1905).

The notion of equalized "through" rates was, of course, "manifestly beyond the scope of the Shipping Board’s jurisdiction." 1 U.S.S.B. at 71. On the continuing question of "regulatory" jurisdiction over joint rail/water rates and additionally an examination of the "law" of cargo diver-
The assertion that Section 8 reflected Congressional intent and, as such, imposed responsibilities on the Shipping Board through the Shipping Act deliberations, although somewhat surprising, was still a tenuous concept at best. Section 8 may best be viewed as a response to the rail congestion that besieged the port of New York during World War I and which crippled vital European supply lines.77 The principal aim of Section 8 was to break the stranglehold that the dominant northeast railroads and their North Atlantic outlets had on cargo moving from the interior of the country overseas.78 While Section 8 granted the Shipping Board79 the

77. There had been a growing inability on the part of the carriers to meet the country’s expanding commercial and industrial needs satisfactorily even prior to the outbreak of war. See generally J. Sharfman, The Interstate Commerce Commission 157 (1969). In 1907, at hearings examining the severe car shortages in the Midwest and Great Plains, the president of the Northern Pacific (Railroad) stated that in “attempting to handle freight offered they were trying to force a 3-inch steam through a 1-inch nozzle.” In the Matter of Car Shortages and Other Insufficient Transportation Facilities 12 I.C.C. 561, 565 (1907) (hearing of January 2, 1907). The President of the Great Northern Railroad testified that “[d]uring the time from 1905 to 1905 the business of the country—the tons moved 1 mile—increased 110 percent, and the facilities—the increase of facilities for doing the business and handling the miles—increased 20 percent in ten years, or 2 percent per annum. But of that 20 percent three-fourths of it was new mileage that was built in sections of the country that added to the congestion of the old.” Id. at 565. Other witnesses testified that the problem was more one of poor use of existing equipment, “loading cars standing from two to twenty days at the points of origin, of empty cars lost in congested terminals or lying unused, sometimes in solid trains, for equal lengths of time.” Id. at 566.

By 1916, the burden on the nation’s railroads had become unprecedented. Interstate Com. Comm’n Annual Report, 72-73 (1916), 72-73. The “conditions of car distribution had...no parallel in U.S. history.” Car Supply Investigation 42 I.C.C. 657 (1917). The Commission found “in consequence mills have shut down, prices have advanced, perishable articles of great value have been destroyed, and thousands of carloads of food products have been delayed in reaching their natural harbors.” Id. at 661.

With formal American declaration of war in 1917, this burden on the railroads increased tremendously. “In the first five months after a state of war was declared to exist between this country and Germany, the railroads handled more freight than in any whole year previous to 1904.” J. Sharfman, The Interstate Commerce Commission 143, note 11 (1961) (quoting C.O. Ruggles “Railway Service and Regulation,” Quarterly Journal of Economics, Vol. 33 (November, 1918, 129-130). With the predominant flow of cargo to Europe naturally through Atlantic ports, New York harbor became “an extraordinary sight.” Not since the days of Jefferson’s embargo preceding the War of 1812 had there been such a mass of ships riding at anchor or made fast to docks. By 1918, thousand of freight cars waiting to be loaded jammed New York terminals. N.Y. City WPA Writers Project, A Maritime History of New York, (1941). On January 1, 1918, 7086 carloads of freight were “standing on wheels” at New York. On January 15, 1918, port congestion caused by the shifting and reshifting of cars to match ships, resulted in 213 ships waiting in New York for bunker coal. J. SMITH, INFLUENCE OF THE GREAT WAR UPON SHIPPING 205-206 (1919).

78. Prior to the latter part of 1919, there were no joint through export rates from the interior territory to Gulf and South Atlantic ports. See Export and Import Rates 169 I.C.C. 13, 18 (1930). The first such export joint rates were mandated in a letter of September 24, 1919, from the
power to investigate the means of promoting, encouraging, and develop-

Director General of Railroads, United States Railroad Administration to North Atlantic "interests".  
Id. at 69-70, Appendix B. The "proposal", understandably, was not met with enthusiasm by 
Eastern railroads, which felt it would cause the diversion of considerable traffic, working to 
"short-haul a number of carriers upon whose lines the business originates," and causing freight 
to move twice its normal distance to seaport.  Id. at 71. The Railroad Administration responded 
that, "It is certainly in the best interest of the country as a whole to distribute the export traffic in a 
reasonable way among all ports which is what we have in mind in this adjustment."  Id. at 72.

The legislative history of Section 8 itself is quite sketchy, as the Commission 
noted in Board of Comm'n v. Seatrain International, 18 SRR 763, 772 (F.M.C. 1978). The "single 
statement concerning the amendment which eventually became Section 8 provides "Amendment 
No. 53: This amendment confers general powers upon the board to investigate terminal 
facilities at ports, and in case it finds that rates of rail carriers are detrimental to the upbuilding of 
such ports or that new rates or additional terminal facilities should be made by carriers it may 
submit its findings to the Interstate Commerce Commission. . . ." Joint Conference Committee 
1107, 66th Cong., 2nd Sess. 27-28, and 25-26 (1920)."

Most, if not all, of the debate focused on the disposition by the government of the enormous 
fleet of vessels accumulated during World War I through the establishment of a large number of 
shipping lines to operate on trade routes from the many coasts of the country. Excerpts of the 
 ensuing Congressional debate show that a secondary thrust of the legislation, to stimulate the 
flow of commerce through many more ports, was debated:

The people of this country are not going to divert their products as a matter of 
sentiment from the ordinary lines of commerce. Our people in the Mississippi Valley, 
who desire to ship their goods direct to Europe, are going to take the shortest and most 
rapid route to get the goods to Europe. They are not going to divert their commerce 
to ports at one side of the main routes of commerce. They are not going to send their 
traffic around by a by-path just for the sake of establishing traffic at a given small port, 
either on the Gulf Coast or the Atlantic Coast. In one way I can sympathize with small 
ports on the Atlantic and Pacific regarding which there is an idea that by furnishing 
ships for them we can build up their commerce and give them a trade that under natural 
conditions they cannot obtain. But there are two matters involved in the problem. It is 
not only a matter of furnishing ships but it is the course and trend of the import and 
export trade of the country. In other words, will a certain class of commerce go to a 
certain port just because you have ships ready, or will it go to a port because of the 
trade and traffic and market for the goods there? My own idea is that you cannot build 
up any such commerce by artificial means. Cong. Rec. 6809 (daily ed. May 10, 1920) 
(statement of Senator Nelson).

The problem of port congestion was highlighted:

A system has developed centralizing very largely the shipping from the North 
Atlantic ports of our country. This tendency toward the Centering of the shipping from the 
North Atlantic ports was emphasized during last year when it came to the question of the 
Shipping Board allocating its vessels.

If there is one evil in this country from which the American people should be re-
lied it is the bottling up of the freight from all over the country in the city of New York. 
There is scarcely a section of the country but that has suffered on account of the con-
gestion which almost continuously exists, bottling up everything in this particular center. 

It is very important, however, that the ownership of these ships shall be distributed 
all over the United States. During the recent World War there was a great congestion of 
goods for shipment in the maritime ports, and there has been congestion since that 
time. It is said that there was string of loaded cars from New York back to Cleveland 
and possibly farther west. I wish that the ports of this country could be opened clear 
around the waterfront of the United States.

Just recently five of the South Atlantic ports sent a very large delegation out West; 
they went to Detroit and possibly as far as Minneapolis. I think the distance from
ing ports, it vested in the Interstate Commerce Commission (ICC) the ultimate authority to take action against "rail rates and practices" contrary to that end.80 Perhaps this clear jurisdictional division of responsibility explains the Board's hesitancy to both adopt Section 8 in The Port Differential Investigation in 1925 and to broaden its authority. Still unsettled, however, was the question concerning how ocean transportation could be effectively regulated in a vacuum, without consideration of the impact of the often intertwined rail transportation on the flow of cargo to the seaboard.

Charleston or Savannah to Chicago is practically the same as it is from there to New York. So if we would open up the South Atlantic and Gulf ports, instead of railroads being congested and not being able to handle our freight, the freight being shipped to those ports, we should get our goods to market more quickly and cheaply, and the whole country would thereby be benefitted.


79. Section 8 was amended in 1981 to give the Secretary of Transportation this responsibility. See text accompanying note 14 supra.

80. Many railroad sought to increase the volume of international traffic at the ports they served by operating their own marine terminals. "With the exception of New York, port development in the United States has been of one railroad, by one railroad, to serve one railroad. The waterfront, the railroad pier, and even the line of ships berthing at the pier have all come to be considered by the railroad as part of its own private system." Port Development in the U.S., at 19, quoting R. MacELWEE, PORT DEVELOPMENT 273 (1926).

Other rail practices could be utilized to increase rail control over the flow of commerce. In Mobile Chamber of Commerce v. Mobile & O. R.R. 23 I.C.C. 417 (1912) the Southern Railway and Mobile & Ohio Railroad were accused of denying ships access to their docks, giving preference to those lines with which the railroads had special arrangements forcing shippers to other wharves where they would have to pay the switching, docking, and unloading charges absorbed if railroad wharves could be utilized, and refusing to issue through bills of lading to shippers unless the cargo would both move over railroad piers and to Europe on preferred steamship lines. Id. at 418. The Commission was especially critical of this latter practice, stating that "if this practice were to obtain at all ports it would be but a short time before there would be only so many steamer lines as there are railroad lines, and the ocean would become in a sense the property of the railroads, for they could make their ship-side rates and issue through bills of lading only to those shippers who accepted movement beyond the ports by the railroad steamship lines." Id. at 426. For a discussion of other railroad-steamship line arrangements, see Pacific Navigation Co. v. Southern Pac. Ry., 31 I.C.C. 472, 480 (1914) ("To permit the rail carriers serving a port to favor one boat line or another...would practically close ports to all but favored vessels").

The Interstate Commerce Commission investigated other rail practices associated with marine terminals. In Discrimination in the Use of Wharfage Facilities, 27 I.C.C. 252 (1913), the Louisville-Nashville Railroad refused to make delivery of cargo destined for points served by the railroad on steamship lines, refused to deliver cargo to a steamship line's warehouse despite the fact that its spur was adjacent to it, and gave preferential berthing to ships consigned to its "agent" transit company. Charges for Wharfage, Handling, Storage, and Other Accessorial Services at Atlantic and Gulf Ports, 157 I.C.C. 663 (1929). The fact that railroads serving North Atlantic ports did not segregate port terminal charges from linehaul rates, and, in fact, absorbed them, was alleged to have hindered the development of South Atlantic and Gulf ports, where municipally owned terminals could not offer comparable rates and compete.
A. CITY OF MOBILE AND ITS PROGENY: A PORTS’ FUNDAMENTAL RIGHT TO CARGO

The applicability of Section 8 to Shipping Act proceedings was a questionable practice back then. The weight accorded Section 8 in another case conducted in 1941, City of Mobile v. Baltimore Insular, could not have been foreseen at the time. As in the The Port Differential Investigation, the rates and practices at issue were broad in scope, and covered the North and South Atlantic ranges as well as the Gulf port ranges in the mainland (i.e., Puerto Rican trade). The allegedly unlawful conduct was that of an “equalization scheme” in which steamship lines were allowed to make deductions in their ocean rates to compensate for higher inland rates to port, thus resulting in equalized “through” rates from each coast. There were no geographical limitations on the practice, a practice which reached deep into the interior of the country. As one defendant in the case was overheard to remark, “everything is equalized against everything.”

81. There have been at least two investigations made pursuant to the mandate of Section 8, reported in Interstate Commerce Commission cases. Maritime Association, Boston Chamber of Commerce v. Ann Arbor Railroad, 95 I.C.C. 539 (1925) (rail rates and geographic position unfavorable to Boston, whose terminal facilities were capable of handling twice the then-current volume of traffic) and Charges For Wharfage, Handling, Storage, and Accessorial Services at Atlantic and Gulf Ports, supra note 80 (noncompensatory railroad terminal charges preventing development of terminal facilities by other interests). See also Interstate Commerce Commission, Annual Report, 1921 and U.S. Army Corps of Engineers, Board of Engineers For Rivers and Harbors, A History of the Board of Engineers for Rivers and Harbors, 115-117 (June 1980) (first report pursuant to Section 8 was made of Portland, Maine, published on April 4 1921).

82. 2 U.S.M.C. 474 (1941). An indication had come in Contract Routing Restrictions Under Agreements Nos. 16, 147, 185 and 4490. 2 U.S.M.C. 220 (1939). North Atlantic conferences required contract shippers, irrespective of origin, to ship through North Atlantic ports. The incentive was a rate discount, which could be lost should a shipment be made through another range in violation of the contract. Patronizing a carrier operating direct services from the Great Lakes ports to Europe was such a violation and seriously burdened Great Lakes ports. Though ultimately striking down the contracts as designed to effect a monopoly, and infringing on the right of choice of shippers, the Board surmised that the Great Lakes-St. Lawrence route is one of our great natural waterways upon which millions of dollars have been expended in the expectation of the actual development and growth of traffic from areas contiguous to its ports. “Economics” and “other advantages inherent” in using the Great Lakes ports had allowed them to remain competitive but the burden of the contractual routing caused the Board to state, uncategorically, we do not look with favor upon the attempt of carrier by artificial means to control the flow of traffic not naturally tributary to their lines.

Id. at 225, 266.

83. 2 U.S.M.C. at 477.

84. Again, the Interstate Commerce Commission faced the mirror image of this problem both prior to the Shipping Act, 1916 (“Since the thing in which the exporter is interested is, . . . the entire through rate, it becomes necessary to examine the ocean as well as the inland portion of the transportation, Differential Rates, 11 I.C.C. 13, 23 (1905) and as late as the 1960’s, Equalization of Rates at North Atlantic Ports, 311 I.C.C. 689 (1960) and 314 I.C.C. 185 (1961) which, of necessity, focused on the competition among Atlantic ports for maritime trade). See generally
The complainant, the City of Mobile, sought to limit the geographical reach that the North Atlantic carrier group had attained through the practices of equalization. The city argued that lower rail rates to the Gulf and South Atlantic ports that had been negated by the practice of equalization, had been established only "after due consideration of factors inherent in the transportation service to facilities for handling cargo at and ocean services available from the respective ports" and with the sanction of a sister Federal agency, the ICC, and [that] therefore [such] should not be nullified. In an argument that would serve as the foundation for the evolution of "port discrimination", complainants asserted further that the continued viability of the nations ports was dependent "upon traffic from inland areas naturally tributary thereto."

The FMC found that the practices in City of Mobile violated Section 16 of the Shipping Act. The Commission further stated in its findings that it could not entirely "ignore [the] complainant's contention that inland rates to seaboard and [the] advantages attaching thereto, should not be summarily nullified by ocean carriers in their rate making [practices]." As the Commission stated, "to condone this practice would wholly ignore the right of a port to traffic to which it may be entitled by reason of its geographical location." This right appeared to be fundamental under stat-

Maritime Ass'n, Boston Chamber of Commerce v. Ann Arbor R.R., 95 I.C.C. 539 (1925) and Rail Service Planning Office, Interstate Commerce Commission, Rail Rate Equalization to and from Ports, Preliminary Report, 1-27 (July 7, 1978). The problem of what was almost concurrent jurisdiction was also recognized at the F.M.C.:

if this case does nothing else, it points up the inefficiency if not absurdity of departmentalizing the regulation of transportation. The problem of cargo diversion is not one that involves water carriers only. Minibridge would not be a factor at all if the rail rates were prohibitive. The basic premises underlying the Shipping Act and the Interstate Commerce Act have never, to my knowledge, been examined one in the light of the other, yet that they do interrelate and at times work at cross purposes has, with cases like this, become increasingly obvious.


85. Proponents of the equalization scheme, notably the Port Authority of New York, urged that it not be condemned because of the length of time it had been observed, that ports and businesses were built upon it, and that shippers and consignees accustomed to it. For the reasons the dominant port of New York would support equalization, see text accompanying notes 74 and 76 supra.

86. The "concept" of territory being tributary to an individual port had been acknowledged by the Interstate Commerce Commission. The prospects of the southern ports "for the future are good, but are dependent upon the development of the resources of the territory which is naturally tributary to them, and of direct and economical routes through these ports to countries which lie to the south, rather than upon the movement of traffic to and from territory which is not geographically tributary to them." Export and Import Rates to South Atlantic and Gulf Ports, 169 I.C.C. 66 (1930) (dissenting opinion of Commissioner Eastman) "...[T]ributary to the port of Boston is a great manufacturing district in New England." Maritime Ass'n, Boston Chamber of Commerce v. Ann Arbor R.R., 95 I.C.C. 539, 555 (1925). Or, "[c]ertain sections of the country are peculiarly tributary to certain railroads" Differential Rates, 11 I.C.C. 13, 30 (1905).

87. 2 U.S.M.C. at 486. The ICC had also faced the task of balancing the right of a port to
utes designed to establish and maintain ports, and it specifically referred to Section 8 of the Merchant Marine Act. Section 8, interpreted as embodying basic Congressional policy in the promotion of port development, had thus been integrated into the Shipping Act.

The decision in City of Mobile however, permitted at least two different conclusions regarding the nature of this fundamental right. The first conclusion is based on the test from the Alaskan Rate and Port Differential cases which balanced the interests of steamship lines, shippers, and ports (as well as the interests of the public). The decisions in these two cases, which permitted carriers to justify otherwise unlawful rates and practices, were abandoned in favor of a "fundamental" and legally unabridgeable right of a port to its naturally tributary cargo.

If the above conclusion would, by analogy to U.S. antitrust doctrine, render cargo diversion a "per se" violation of the Shipping Act, then the second approach, allowing carrier defenses, may best be described as a "rule of reason" approach. Support for this interpretation may be

participate in "export business," with such right served by equalization, while at the same time preserving subsidiary advantages thereto. Differential Rates at 60-76. See generally Maritime Ass'n, Boston, text accompanying note 86 supra.

88. 2 U.S.M.C. at 486. The Commission left no doubt as to the particular statutory source of this right stating, "the contention has been made that Section 8 has no relation to the rate regulatory provisions of the Shipping Act, 1916. But to wholly ignore basic policies of Congress would be unwarranted." Id.

89. The concurring opinion of Justice Goldberg in Griswold v. Connecticut, 381 U.S. 479, 493 (1965) describes the nature of Constitutionally-based fundamental rights: "In determining which rights are fundamental, judges are not left at large to decide cases in light of their personal and private notions. Rather they must look to the 'traditions and [collective] conscience of our people' to determine whether a principle is 'so rooted [there] as to be ranked as fundamental,'" quoting Snyder v. Massachusetts, 291 U.S. 97, 105 (1934). The inquiry is whether a right involved "is of such a character that it cannot be denied without violating those fundamental principles of liberty and justice which lie at the base of all our civil and political institutions ..." Powell v. Alabama, 287 U.S. 45, 67 (1932). Griswold, supra at 493. See also Poe v. Ullman, 367 U.S. 497, 517 (1961) (Douglas, J., dissenting).

90. See United States v. Socony-Vacuum Oil Co., 310 U.S. 150 (1940). "Under the Sherman Act a combination formed for the purpose and with the effect of raising, depressing, fixing, pegging, or stabilizing the price of a commodity in interstate or foreign commerce is illegal per se." Id. at 223. "Whatever economic justification particular price-fixing agreements may be thought to have, the law does not permit an inquiry into their reasonableness. They are all banned because of their actual or potential threat to the central nervous system of the economy." Id. at 224 note 59.

91. The classic "test" for unlawfulness under "rule of reason" was stated by Justice Brandeis in Chicago Board of Trade v. United States, 246 U.S. 231 (1918):

The true test of illegality is whether the restraint imposed is such as merely regulates and perhaps thereby permits competition or whether it is such as may suppress or even destroy competition. To determine that question the court must ordinarily consider the facts peculiar to the business to which the restraint is applied; its condition before and after the restraint was imposed; the nature of the restraint and its effect, actual or possible. The history of the restraint, the evil believed to exist, the reason of adopting the particular remedy, the purpose or end sought to be attained, are all relevant facts. This
gleaned from the Commission’s observation that while equalization, in itself, was not unlawful, neither was it a common practice for ocean carriers\textsuperscript{92} and the lawfulness of port equalization \textit{to the extent [(t)here] in issue}\textsuperscript{93} had not been previously presented for determination. Taken together, these statements support the inference that a “balancing” test \textit{was} applied by the Commission, but that operation of the equalization plan not only fraught with noncompliance and malpractice but made worse by a lack of geographical limitations was clearly unreasonable.\textsuperscript{94} The accurate interpretation of the Commission’s decision in \textit{City of Mobile v. Baltimore Insular Lines} would only await subsequent decisions for clarification.

The first decision rendered after Mobile was handed down only three days subsequent to the Mobile decision. With the parameters of port protection having experienced significant changes in Mobile, the business of ocean transportation itself was in a state of transition. In \textit{City of Beaumont v. Seatrain}\textsuperscript{95} the Commission was confronted with applying its broader port protection responsibility to the emerging technology of a predecessor of containerization, rail car carriage, and to an early “load center”. The new technology, represented by the car-carrying vessels of Seatrain, were primarily utilized in the U.S. Gulf Coast-Havana trade. Because of

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\textsuperscript{92} It was, however, a common practice for railroads. See text accompanying note 84, \textit{supra}, on the notion of rail and ocean rate equalization.

\textsuperscript{93} Earlier, in \textit{Intercoastal Rate Structure}, 2 U.S.M.C. 285 (1940) ocean carriers in the westbound intercoastal trade implemented a scheme to offset differences in rail costs to effect equalization of total transportation costs from interior points through Baltimore, New York and Philadelphia. At the time the equalization plan was implemented, the cost of ocean transportation to Baltimore and Philadelphia were 3 and 2 cents, respectively, more than New York, offsetting rail rate differences among those ports. When the instant case was brought before the Maritime Commission, the rail rates to Philadelphia and New York were one cent more to Philadelphia and three cents more to New York than to Baltimore, the equalization plan then having little relationship to rail differentials. It was asserted, nevertheless, that port equalization afforded inland shippers a maximum number of gateways and promoted competition for lines into central territory. \textit{id.} at 305. Baltimore interests opposed the plan on the grounds that it diverted high value cargo to New York and negated Baltimore’s natural advantage of being close to interior producing points. \textit{id.} at 306. In consideration of the Shipping Act 1916 and the Merchant Marine Acts of 1920 and 1936, the equalization plan was struck down “as primarily designed by the various respondents to entice a larger share of the business away from their competitors’ and not to equalize rail differentials and further confusing an already complicated competitive struggle.” \textit{id.} at 307.

\textsuperscript{94} Such malpractices included deductions in ocean rates made in excess of the 30 percent specified by the conference agreement, 2 U.S.M.C. at 482, the use of unlike rail rates to different ports as a basis for reductions in the port-to-port rates, \textit{id.} at 481, and equalization of rates from traffic local to other ports. \textit{id.} at 477.

\textsuperscript{95} 2 U.S.M.C. 500 (1941), \textit{reconsidered and reversed}, 2 U.S.M.C. 699 (1943).
the high costs associated with the equipment required for loading and unloading the rail cars, a single port in Texas City, Texas was chosen as the operations center through which Seatrain’s traffic would be funneled. As provided under conference agreement, Seatrain agreed to absorb the difference between the shipper’s cost of delivery to the Seatrain load center and to cost of delivery to ship the goods to the ports in Galveston, Houston, or Beaumont. Shippers were not to be penalized by the higher inland cost associated with routing traffic to Texas City. The ports of Galveston, Houston, and Beaumont alleged that this absorption practice and the resulting diversion of cargo violated Sections 15, 16 and 17 of the Shipping Act. In its analysis, the Commission viewed the aggrieved ports as consisting of three distinct interests: one, the interest of shippers who supported the absorption practice; two, the port facilities which had lost some 2673 tons of cargo to Seatrain; and three, the carriers serving the affected ports that had lost cargo to Seatrain and whose bulkbreak service could not compete with Seatrain on parity rates. The Commission noted that the port protection responsibilities enunciated in City of Mobile were to be applied with even greater force to practices which allowed carriers to reach into ports and divert “local” cargo. However, the finding that the Seatrain absorption scheme was unlawful, was based on a warning issued by the Commission in Contract Routing Restrictions. In this case the Commission stated that it did not “‘look with favor upon the attempt of carriers by artificial means to control the flow of traffic not naturally tributary to their lines.’” The Commission was concerned with more than just the injury to the complainant ports; the Commission was also concerned about how the other carriers, who provided essential “water carrier services” to the ports would be crippled by Seatrain’s diversion of cargo and the subsequent rate wars that would be precipitated. The “‘shipping acts’” administered by the Commission, with their declared policy of furthering the development and maintenance of the American Merchant Marine, thus mandated the condemnation of Seatrain’s terminal consisted of “a railroad spur and a loading crane which fastens to a loaded car, picks it up and deposits it on one of the tracked decks in the vessel. The loaded car is strapped to the deck and at the point of discharge is raised, run onto a railroad track and moved intact to the final point of destination.” Id. at 503.

97. The distance via rail to Texas City from Galveston, Houston and Beaumont is 14.2, 42.2 and 91 miles, respectively. 2 U.S.M.C. at 502.

98. Id. at 503-04.

99. 2 U.S.M.C. 474 (1941).

100. See text accompanying note 82 supra.

101. The Commission noted “... a port and its transportation services are indissolubly linked together, are interdependent, and a practice harmful to one injures the other.” 2 U.S.M.C. at 504. Compare with Alaskan Rate Investigation, 1 U.S.S.B. 1 (1919) (practice harmful to shippers in hinterland of port harmful to port).
train's "traffic raiding" absorption practices.  

Undaunted, Seatrain cancelled the absorption provision and the Gulf and South Atlantic Steamship conference filed to remove the Texas ports from the scope of the agreement. This allowed the conference lines, including Seatrain, to set their own ocean rates to those ports. Instead of absorbing additional inland transportation costs to Texas City, Seatrain simply chose to lower its ocean rate to accomplish the same end. A further hearing was ordered by the Commission to bring the record in the matter up to date.

In the second decision rendered by the Commission on the matter, the Commission noted that the service provided by Seatrain had neither the destructive impact that had been ascribed to it by the competing carriers, nor the detrimental effect that had been ascribed to the activity by the Commission in the initial hearing on the matter.

Furthermore, it was determined that Texas City, Galveston, and Houston were considered to be "one terminal district or port" (or all Galveston Bay ports), and that the area comprising the ports of Galveston and Houston and the surrounding territory was "centrally, economically and naturally" served by Seatrain's facilities at Texas City. The three ports were to have shared the same naturally tributary hinterland. The earlier Commission decision was reversed and the proposed modification

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103. 2 U.S.M.C. 699 (1943). Conferences are associations of steamship lines sanctioned by the Federal Maritime Commission in U.S. trades to set rates collectively. This ability to price-fix lawfully is in recognition of the thought the steamship industry is of such a unique nature that unfettered competition is unworkable. See Ellsworth, Competition or Rationalization in the Liner Industry, 10 J. MAR. L. COM. 499 (1979).

104. The Commission found that Seatrain's service was not so advantageous as to command a rate higher than those of breakbulk lines. Id. at 701. This, however, had been brought out in the earlier decision. 2 U.S.M.C. at 503. Also, on reexamination the Commission found it impossible to determine whether one of the principle commodities alleged diverted, rice, originated locally at the aggrieved ports or at interior mills and merely shipped through those ports, thus putting into question the claim of "traffic raiding" of local cargo. 2 U.S.M.C. at 701.

105. Again, highlighting the continuing "interplay" between transportation regulatory agencies, the Maritime Commission relied in part on the Interstate Commerce Commission's description of the three ports as "one terminal district or port" in Rate Structure Investigation Part 3, Cotton, 165 I.C.C. 595, 660 (1930). See text accompanying note 84, supra.

106. Beaumont, having access to the Gulf several miles east of the other ports and 126 miles by rail from Texas City, did not fall within the "Galveston Bay port" designation; its traffic was not
of the conferences’ scope became unnecessary.¹⁰⁷

These two cases (the first of which was decided pursuant to the principles of cargo protection announced in City of Mobile) did not clarify the degree of protection that was to be afforded to naturally tributary cargo, they did demonstrate the difficulties that the Board would encounter in both fulfilling its expanded responsibilities and yet not stifling the innovation that accrued to the benefit of shippers and steamship lines.

The first decision may have merely been a forum within which the Commission would be able to wield its new, stronger port protection duties. Certainly, Seatrian’s “traffic raiding” of cargo not naturally tributary to, but from within the area of the aggrieved ports themselves, provided an ample opportunity for such an exhibit.

The first City of Beaumont decision appears to represent an attempt by the Maritime Commission to expand its authority and responsibility beyond that provided by Section 8 and into the Merchant Marine Acts of 1920 and 1936¹⁰⁸ which promote the American Merchant Marine. The fact that the Commission’s expanded role dominated its initial decision (only to be ignored in the second case) illustrates the “conscious decision” of the Commission to limit the scope of its responsibilities which had already been beyond that of the Shipping Act by Section 8.

This reluctance to further broaden the scope of responsibility was again shown by the Commission’s refusal to adopt Section 8 as a standard in The Port Differential Investigation. On a more practical level, Seatrian’s service, although clearly innovative, was feasible only through the utilization of equalization. The practice of equalization in turn was evoking serious scrutiny by the Commission.

B. CITY OF PORTLAND—LIMITATION OF DEFENSES STRENGTHENS RIGHT

The Commission’s focus then shifted to the West Coast, specifically to the Pacific Westbound Conference that would remain a combatant in the port/carrier disputes over the course of a decade.¹⁰⁹ In City of Portland v. Pacific Westbound Conference,¹¹⁰ the equalization practice of absorption, (as illustrated in Seatrian) permitted member lines to absorb the cost differential between that of the shipper’s cost of delivery to that of the closest port (Portland and Seattle in this instance) and the cost associated

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¹⁰⁷. Id. at 703-04.
¹⁰⁸. See text accompanying note 102, supra.
¹¹⁰. 4 F.M.B. 664 (1955).
with delivery to the port being served by an equalizing line (San Francisco). It is undisputed that the cargo in question, primarily agricultural commodities from the states of Washington, Oregon, Idaho, and Montana, were naturally and geographically tributary to the complaining ports.111

The respondent carriers stressed the various reasons supporting the importance of the indirect service. The diversion of the cargo to San Francisco included the following benefits: more frequent service; the availability of refer space which is crucial for storing perishable products; and the fact that the San Francisco port was accorded "last out" port status among the California ports. The aggrieved ports argued that elimination of the practice would increase service to their ports, thereby benefitting their economies and freeing from jeopardy the heavy investment of the ports in physical facilities and equipment.112

The Commission proceeded to embark on a commodity-by-commodity analysis focusing on the adequacy of service at the Pacific Northwest ports. If the necessary direct service was not available, the equalization practice with indirect service was upheld while remaining under the continuing review of the Commission. Such a practice was permitted until sufficient service became available at the port (in this case Portland).113

The Commission emphasized that Section 8 required "that all other factors being substantially equal, a port should receive the benefits of or be subject to the burdens incident to its proximity or lack of proximity to another geographical area."114

With this the Commission made it clear that the lack of adequate service was the leading of two defenses that were available, and the other remaining defense available only when an emergency situation arose and

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111. The leading cargoes of the Northwest, especially grain and lumber, were not affected by the equalization. 4 F.M.B. at 670. Neither was there any doubt apparently as to the detrimental impact of the practice, depriving Portland and Seattle of cargo that would normally move through those ports but for the equalization. 4 F.M.B. at 677 (emphasis supplied). See text accompanying note 66, supra ("but for" test to establish detrimental impact of practice).

112. This, of course, was prior to the advent of containerization, but the cost of providing specialized equipment was already escalating. Seatrain's unique operation in Texas City required a crane that cost $125,000. Beaumont v. Seatrain, 2 U.S.M.C. 699, 702 (1943). See generally Public Port Financing in the U.S., supra note 26.

113. There was no explanation given for this restriction of the utilization of absorption other than the Commission's own statement, "To the extent, therefore, that the ports of a given geographical area give or can give adequate transportation service, we look with disfavor on equalization rules or practices which divert traffic away from the natural direction of the flow of traffic." 4 F.M.B. at 679. The defense may have grown out of interpretation of a phrase in Section 8 "It shall be the duty of the Board . . . to investigate any matter that may tend to promote and encourage the vessels of ports adequate to care for the freight which would naturally pass through such ports. . . ." See text accompanying note 14 supra.

114. 4 F.M.B. at 677.
precluded a direct call upon the port. A carrier would be allowed to intervene in such a situation only if the carrier normally called at the port and only if the carrier restricted its use of the port during the emergency.\footnote{115}

It remained unclear whether there was a specific basis in Section 8 for a general limitation of defenses. What was clear, however, was that although a port's right to cargo from its naturally tributary areas remained valid, such right was now subject to these two quite restricted “exceptions.” Thus the right was legally surmountable. The fact that the Commission in Mobile neither discussed such defenses nor implied their existence leaves one with the feeling that the Portland case is an interesting if not mysterious refinement of Mobile which contrasts with the more flexible thrust of the City of Beaumont case.

In 1965, the Pacific Westbound Conference was again embroiled in a controversy surrounding port equalization. This time the complaining party was the Port of Stockton, California. In Stockton Port District v. PWC,\footnote{116} conference members were authorized to reimburse shippers for the price differential between shipping to the nearest port of origin for the cargo (in this instance Stockton) and that of shipping to cargo to the actual port of loading (again, San Francisco). As in Portland, and the line of

\footnote{115. \textit{id.} at 678. Interestingly the equalization was practiced almost exclusively by U.S.-flag, subsidized carriers, precluded by their subsidy contracts from serving the Pacific Northwest in addition to San Francisco. Equalization gave them the “tool” with which to serve those markets without necessitating a ship call, clearly unlawful. \textit{id. Compare with Beaumont v. Seatrain, 2 U.S.M.C. 500 (1941) (equalization, deemed harmful to American Merchant Marine, deemed unlawful).}

\footnote{116. 6 SRR 505 (F.M.C. 1965), aff'd, 369 F.2d 380 (9th Cir. 1966), cert. denied, 386 U.S. 1031 (1967) (Initial Decision at 5 SRR 361 (F.M.C. 1964)). Throughout this Paper, the so-called Initial Decisions, those made at hearing-level by the Administrative Law Judges, or Hearing Examiners, will be examined and discussed, such decisions possessing significance as “an important part of the whole record a reviewing court weighs in order to assess substantial evidence.” National Ass'n of Recycling Indus. v. F.M.C., 658 F.2d 816, 824 (D.C. Cir. 1980). The Initial Decisions also, on the whole, tend to be less restrictive discussions more illuminating of policy considerations that justify decisions. This case was not the first port discrimination claim centering on the Port of Stockton. In Sun-Maid Raisin Growers Ass'n and Sunland Sales Coop. v. Blue Star Line, 2 U.S.M.C. 31 (1939), Stockton and its shippers complained of ocean rates of the Pacific Coast European Conference set higher for that port than the many “terminal loading ports” specified under conference agreement. Evidence presented showed that should be accorded the status (and rates) of such a terminal loading port, the volume of cargo through Stockton would increase, forcing increased steamship service. Interestingly, one defendant line contended “that the function of an ocean carrier is to skirt along the coast and pick up cargo gathered there from the interior” and that it would “gladly” withdraw services from some of the ports included in its blanket territory if not for the industry that had been established in reliance upon the continuation of such service. The larger ports such as San Francisco asserted that they had been “developed with the thought in mind that ports such as Stockton, lying behind terminal ports, would not be served by ocean-going vessels, and the large investment of the former, it is urged, should not be jeopardized by disturbing the existing relationship.” Nevertheless, the differential was found violative of Sections 16 and 17.}
prior discrimination cases leading back to *Alaska Rate Investigation*, the
distinct interest of shippers, steamship lines, and ports were to be ex-
amined. The conclusion that was arrived at in this particular case would
leave the Commission bitterly divided.

Consideration of the impact of the equalization yielded what might be
considered representative of the three interests affected (generally) by
such practices—the Port of Stockton, which had spent $23 million on its
facilities since 1964, had lost $232,000 in revenue from the diversion of
cargo, steamship lines had saved both time in not traveling the 8 hours
trek each way to Stockton, and $3,600 per vessel for the additional call,
or $67,000 more than the $113,030 it cost them to equalize, and shippers,
while many preferring the alternative of direct service, strongly fa-
vored having access to more frequent service at San Francisco and its
shorter in-transit time as "last loading" port. Even though there were
ample economic justifications for practicing the discrimination against
Stockton, the Commission "would not save respondents equalization
under the applicable precedents were it established that the practice
drew cargo away from territory which was exclusively and naturally tribu-
tary to Stockton." The Commission reiterated the fundamental nature of a
right of a port to its naturally tributary cargos as espoused in *City of Mo-
bile*, and which was further refined in *City of Portland*. The Commission
had also taken it upon itself to finally clarify the relationship between the
Section 8 based right with that of Sections 16 First and Section 17 of the
Shipping Act.

It was clear from a reading of the Shipping Act provisions that the
provisions proscribed only prejudice and discrimination that was consid-
ered unjust and unreasonable. Since what was "unjust or unreasonable"
were questions of fact which permitted a balancing of the interests of
ports, carriers, and shippers, it was difficult to devise a test that would
fit every case or situation.

Diversion of the naturally tributary cargo of one port to another port
however, allowed for no such considerations of benefits accruing to each
interest, for it triggered a prima facie violation of two of the Shipping Act
provisions. Such violations could be defended only if it was shown

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117. 6 SRR at 511 (F.M.C. 1965).
118. 6 SRR at 513, 518.
119. 6 SRR at 513.
120. *See* The Port Differential Investigation, 1 U.S.S.B. 61, 65 (1925) (It will be observed that
the character of discrimination inhibited by these provisions of the statute is discrimination which
is undue, unreasonable, or unjust. Whether that measure of discrimination is established by this
record is the province of the board to determine.).
121. The Commission asserted "... there is ample economic and cost justification for the
discrimination against Stockton such as it is. But even this would not save respondents’ equal-
ization under the applicable precedents were it established that the practice drew cargo away
that the aggrieved port did not provide adequate steamship service. The focus of alleged port discrimination was not the relatively straightforward demonstration of the benefits that accrued from the equalization practice as weighed against the damage that was inflicted but rather the "test" was based on a delineation of the amorphous boundaries of the ports exclusive hinterland, which provided for a much more complex endeavor. City of Beaumont\(^{122}\) had added the important requirement that the "exclusive" hinterland infringed upon must be just that; exclusive and not shared with other ports.

The shifted focus of the Commission precipitated new and unique theories of defining areas naturally tributary to ports.\(^{123}\) The Commission, however, found that Stockton and San Francisco did not represent separate and distinct geographical areas, with both being "Bay area" ports and drawing from the same hinterland.\(^{124}\) Based on City of Beaumont, there could be no unlawful diversion. Such a conclusion was based, however, on a historical perspective that would remain an element of later tests for determining unlawfulness but which would necessarily prove to be less than determinative as the practice of containerization and intermodalism permanently disrupted the older, established routings of cargo. The Commission had explained that the natural flow of cargo from the San Joaquin Valley, the hinterland claimed to be exclusive to Stockton, had been part of the through-way to San Francisco or from the "Golden Gate to the Pacific Ocean." The Commission declared that "San Francisco did not cease to be such a port merely upon the creation of an additional port at Stockton."\(^{125}\)

There seems to be lingering validity in the charge by Commissioner Hearn\(^{126}\) that by categorizing San Francisco and Stockton as "Bay area ports" the Commission had effectively ignored the fundamental question of whether the "natural flow" of cargo from the San Joaquin Valley was through Stockton and whether the cargo would have flowed through

\(^{122}\) 2 U.S.M.C. 699, 703 (1943) "... the area comprising the ports of Galveston and Houston and the surrounding territory are centrally, economically and naturally served by Seatrain's facilities at Texas City."

\(^{123}\) Stockton argued that a large part of central California, including the San Joaquin Valley, was naturally tributary to the port based on minimum trucking rates, which in turn were based on "constructive mileage," actual mileage weighed by such factors as the number of traffic lights and bridges, the presence or absence of mountainous terrain, the condition of the highways and other factors affecting truck traffic. 6 SRR at 518, note 6 (F.M.C. 1965).

\(^{124}\) Id. at 516. The Commission's sanction of the equalization was not unlimited. Equalization moving cargo tributary to Bay area ports to Los Angeles and Long Beach, California, was disapproved. Id. at 527.

\(^{125}\) Id. at 517.

\(^{126}\) Id. at 530.
Stockton rather than San Francisco if the equalization had not been present. The labeling by the Commission of the Bay area as "centrally, economically, and naturally served by San Francisco" was also quite puzzling.\textsuperscript{127}

More importantly, the separate opinions of both Commissioners (Hearn in dissent and Patterson concurring only in the result) were to frame the policy dilemma that would remain the heart of future port discrimination claims.

Commissioner Hearn judged the majority's decision as, "(1) frustrating the will of Congress in developing new and modern ports and (2) turning over to conference carriers the right to determine which of our ports shall prosper and which shall suffer."\textsuperscript{128} The commissioner surmised that millions of dollars worth of public and private investment would be impaired as a result of the decision that had been rendered.

Commissioner Patterson disputed the Commission's authority to administer the Merchant Marine Acts of 1920 and 1936 and therefore, he did not base his analysis on the "policies"\textsuperscript{129} of such Acts. Instead, the commissioner discounted the interests of Stockton (and the interests of other such aggrieved ports) by succinctly stating that "[a]s long as the purpose and effect of the (absorption) rule are mutual economic advantage[s] of the carriers, and shippers, and localities, ports are not unreasonably disadvantaged."\textsuperscript{130} He likewise countered Stockton's argument that, because of large public investment in the port, the port was entitled to "local tributary traffic." The Commissioner frankly stated that such investments depended on "commercial potentialities" and not on "future rights" and that once made the "investment did not create legal rights to

\textsuperscript{127} This paraphrased Commission's "description" in Beaumont. See note 115 supra and accompanying text.

\textsuperscript{128} 6 SRR at 528 (F.M.C. 1965). Later the conference system itself was assailed in an in depth study by the Justice Department in 1977. Antitrust Division, U.S. Dept. of Justice, Study of the Regulated Ocean Shipping Industry (January 16, 1977) "Justice Dept." An almost point-by-point reply in defense of the system, and a case made for strengthening it, was made by the Council of European and Japanese National Shipowners Association, The University of Wales, Institute of Science and Technology, Liner Shipping in the U.S. Trades, (April, 1978) "CENSA". One of the only points on which the two groups agreed was that the protection of naturally tributary cargo should end, albeit for different reasons. The Justice Department asserted that the concept had "served to inhibit some forms of competition (direct v. indirect service) and shipper choice," Justice Dept. at 162 (parenthetical supplied). CENSA surmised that containerization, with fewer, larger ships plying trades, at fixed schedules, required a port to draw cargo from a "much larger catchment area" than naturally tributary. It found regulatory difficulties with equalization practices utilized to accomplish this illustrating a stark anachronism the (Shipping) Act, which took into account the very different technology and trade patterns of 1916, and therefore ought not to be invoked to prevent potentially beneficial changes in transport technology from being fully implemented. CENSA at 59.

\textsuperscript{129} 6 SRR at 532 (F.M.C. 1965).

\textsuperscript{130} 6 SRR at 532e (F.M.C. 1965).
a flow of business or entitle anyone to anything."¹³¹

C. MAINLAND-PUERTO RICO CASES—ABSOLUTE V. CONDITIONAL RIGHT

A series of cases involving the Mainland-Puerto Rico trade were to soon follow, beginning with Sealand Service v. South Atlantic & Caribbean Line.¹³² Cases centering on this trade route would once again bring the question concerning the strength of a port’s fundamental right to cargo that had been clearly established by the Commission.

At issue in the SACL case was the equalization practice of transshipment,¹³³ rather than the practice of absorption, as SACL accepted cargo at Jacksonville and moved it at its own expense to Miami for direct service to Puerto Rico. The rates for the indirect service from Jacksonville (which was listed along with Miami and San Juan as a terminal port) were the same as that of the direct service from Miami. Sealand alleged that the practice diverted the naturally tributary cargo of Jacksonville, contrary to Section 8 and in violation of Sections 14, 16, and 17 of the Shipping Act.

The Administrative Law Judge, while dismissing the applicability of Section 8 as a standard administered by the Commission,¹³⁴ found that the substituted service permitted SACL to secure substantial additional cargo through Miami from areas “which (because of the) geography (of the area) and (because of) the normal inland routes”¹³⁵ were actually tributary to Jacksonville, and therefore in violation of Section 16, First. The Commission itself also failed to address the mandates of Section 8, although they did manage to apply the test of City of Portland v. PWC.¹³⁶ The test was comprised of the following factors: (1) a diversion of traffic from a port to which the area of origin is naturally tributary, to a port to which the area is not naturally tributary; (2) where the diversion of cargo is not justified, in the shippers interest, by the lack of adequate service out

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¹³¹ 6 SRR at 532g (F.M.C. 1965). Or, as Patterson stated, "The justification for public investment in port construction comes before, not after the investment." id.

¹³² 6 SRR 79 (F.M.C. 1965) (Initial Decision).

¹³³ See text accompanying note 52, supra, for distinction between transshipment and absorption.

¹³⁴ A primary reason was that the functions prescribed by Section 8 were not among those transferred to the F.M.C. by Reorganization Plan No. 7 of 1961, which created the Commission. 6 SRR at 86 (F.M.C. 1965). See text accompanying note 59, supra (detailing governmental reorganization plans impacting "Commission" and predecessors).

¹³⁵ 6 SRR at 89 (F.M.C. 1965). "The traffic accorded 'substituted' service originated or was destined for points in or about Jacksonville or north or west thereof." id.

¹³⁶ 4 F.M.B. 665 (1955). The test was not explicitly established, but rather implied in the then Maritime Board’s statement that "[t]o the extent, therefore, that the ports of a given geographical area give or can give adequate transportation services, we look with disfavor on equalization rules or practices which divert traffic away from the natural direction of the flow of traffic." id. at 679.
of the port from which traffic is so diverted or; (3) emergency or exigent circumstances are not present to preclude a direct call. Evidence showed that the cargo in dispute was "attracted by considerations of time, distance, and cost factors" to Jacksonville, but notwithstanding these logical inducements, moved through Miami. More succinctly, the Commission stated that but for the free inland transportation of the substituted service, the traffic would not have moved through Miami. In establishing this as a standard of proof, it rejected the proposed test that "[a] diversion of traffic [is the equivalent] of traffic that would have moved through Jacksonville instead of Miami but for the substituted rule" and overruled the precedent established in Philadelphia Ocean Traffic Bureau v. Export S.S. Corporation in doing so. The Commission also dismissed SACL's claims that service at Jacksonville was inadequate because Sealant's rates were higher than SACL's. The Commission stated: "We find this service to be adequate in general for shippers who wish or [who] may wish to use Jacksonville." The Commission further stated that, "we do not hold that cargo tributary to Jacksonville must move to this port, nor do we say that service must be adequate to accept all cargo." We simply hold that a carrier cannot utilize a substituted service rule to siphon off cargo, some of which would otherwise move through Jacksonville.

Sealant v. SACL represented a significant expansion of the fundamental right to naturally tributary cargo. The case further weakened both the required standard of proof for unlawfulness and the primary defense of inadequacy of service. The first standard would remain especially troublesome for two specific reasons. One, in discarding the "but for" test of Philadelphia Ocean Traffic Bureau, the Commission adopted an aberration of it: that but for the equalization the traffic would not have moved through the more distant port. This test seems to focus on Section

137. Shipments from Canton, Georgia, 360 miles from Jacksonville, moved instead through Miami, a distance of 700 miles from origin—and time and cost factors were necessarily based on distance. 6 SRR at 1113 (F.M.C. 1965).
138. Id. at 1116.
139. 1 U.S.S.B.B. 538 (1936) (United States Shipping Board Bureau). In that case, members of The West Coast of Italy and Sicilian Ports/North Atlantic Range Conference added a surcharge on the New York ocean rate for cargo destined to Philadelphia. The Shipping Board stated it well settled that the existence of unjust discrimination and undue prejudice and preference is a question of fact which must be clearly demonstrated by substantial proof. . . . It is essential to reveal the specific effect of the rates on the flow of the traffic concerned. Furthermore, a pertinent inquiry is whether the alleged prejudice is the proximate cause of the disadvantage. The Board concluded that more than general representations were needed to prove "that the rate situation is solely responsible" of the disadvantage. Id. at 541.
140. 6 SRR at 1115 (F.M.C. 1965).
141. Id.
142. Id.
First’s prohibition against undue preference rather than on unjust prejudice and detrimental impact of the practice. Previous cases had been virtually unanimous in their attacks on the harm, not the benefit caused by equalization practices and there was no explanation given for the departure in this case. The new test allowed one to conclude that a potential diversion of cargo (cargo that may never have flowed through an aggrieved port) might yet be the foundation for a successful claim of unlawful diversion. Again, there is no requirement that the practice be shown to have caused the diversion from the complainant port to trigger unlawfulness, only that it was somehow artificially induced to another port. It is difficult for one to claim to have been damaged as a result of an equalization practice if the allegedly aggrieved port could not show that it would have served as the outlet for that cargo in the absence of the practice. Yet this is exactly what the Commission sanctioned, the difficulty in such logic notwithstanding. The second case, decided in the same year, involved the same two parties from the initial case, along with other parties who were all involved in a prospective rate war between North and South Atlantic carriers in the same over-tonnaged trade with Puerto Rico. In Reduced Rates on Machinery-Atlantic to Puerto Rican Ports, a 1964 rate reduction by Sealand, serving the North Atlantic range, triggered rate reductions by South Atlantic carriers, TMT and SACL. Another subsequent rate reduction by Sealand was again followed by the same action by TMT and SACL. At this point, the rates were suspended by the Commission; an investigation was ordered and a hearing soon ensued. The primary issue was the extremely low rate of TMT, which had somehow been found to have been just and reasonable. In addressing the allegation that the rate differential favoring South Atlantic ports diverted cargo which was, by virtue of favorable rail rates, naturally tributary to the North Atlantic, Administrative Law Judge Greer qualified that so-called "fundamental right" with the rule (taken from City of Portland) that Section 8 required that a given geographical area and its ports should receive the benefits and burdens of their mutual proximities only with "all other factors being substantially equal." TMT’s inferior service and its need to maintain correspondingly lower rates to meet the competition did not satisfy this standard.

143. 7 SRR 233 (F.M.C. 1966).
144. 9 SRR 175 (F.M.C. 1967).
However, the Commission found the basis for such inequality not with TMT's inferior service, but rather because of the closer proximity of the South Atlantic ports to Puerto Rico than that of the North Atlantic ports. The Commission's conclusion as to the lawfulness of the rate differential was different from that of the administrative law judge. In balancing the "natural distance advantage" of TMT with the "natural advantage" of the North Atlantic ports and their lower inland freight rates, the Commission determined the following factors: one, that neither the level of TMT's rates nor the degree of the differential was supported through either shipper's testimony that their particular rates were necessary; two, that neither carrier presented evidence proving that such rates produced any greater overall revenue for either carrier than a lower rate would have; and three, the carriers had failed to prove that the transportation conditions necessary to justify the diversion of naturally tributary cargo were present.\footnote{146} The difference between North and South Atlantic rates was reduced by the Commission so that carriers and ports could each realize their "natural advantages."\footnote{147}

The final case of the three in this area, Rates From Jacksonville to Puerto Rico,\footnote{148} involved a second prospective rate war between Sealand (serving Puerto Rico from Jacksonville, Fla. and Elizabeth, N.J.) and TMT (with regular service from Jacksonville and alternate voyages via Miami). TMT maintained that rates were lower from Jacksonville than Sealand's rates from Jacksonville (and Elizabeth) on southbound voyages, was again alleged to have diverted cargo naturally tributary to New York.

Once again, Administrative Law Judge Greer asserted that the right to naturally tributary cargo was "not unqualified" and could be lost if a differential having such effect was so justified by transportation conditions. Forcing TMT to raise its rates was likely to drive it out of business and allowing Sealand to lower its rates from Jacksonville so as to meet TMT's competition would most likely divert more North Atlantic cargo through that port. Therefore, transportation conditions prevented enforcement of the right of North Atlantic ports to the cargo naturally tributary to


\footnote{147} TMT appealed successfully to the Court of Appeals for the D.C. Circuit, which remanded the case back to the Commission. The primary issue was the rate setting authority of the Commission and its utilization to protect naturally tributary cargo. Also at issue was the role or importance of distance in ratemaking between ports. 7 SRR 1001 (F.M.C. 1967).

On remand, the Commission held that the "policy of promoting the movement of cargo through ports through which it should normally move applies equally to equalization cases and the instant cases, id. at 1005, and that distance has an "important bearing where because of a shorter distance between transit points a carrier incurs lesser costs." id. at 1006.

\footnote{148} 9 SRR 175 (F.M.C. 1967), petition to reopen and reconsider denied, 9 SRR 339 (F.M.C. 1967).
their range.\textsuperscript{149}

The Commission found that TMT did indeed divert cargo which, based upon inland rail rates, was tributary to North Atlantic ports.\textsuperscript{150} However, the Commission qualified this decision by stating, "Naturally tributary [cargo] is an economic concept. . . .", [dependent upon] . . . the shippers cost, the value of a carrier's service to a shipper or other factors." The Commission went further and cited the test concerning the lawfulness of the rate differential as stated in Reduced Rates On Machinery.\textsuperscript{151} The record was held insufficient to make a determination regarding whether the cargo met the threshold of legally (naturally) tributary cargo. By affirming the initial decision, the diversion was justified due to the transportation conditions and the differential upheld.

These two Puerto Rican trade decisions, which restricted the right to naturally tributary cargo, are in contrast to Sealand v. SACL which broadened the right to naturally tributary cargo. In both Reduced Rates on Machinery and Rates from Jacksonville, the Commission relied on the qualifications of City of Portland which held that Section 8 protection applied only when "all other factors [were] substantially equal." While City of Portland is most significant for establishing inadequacy of service as virtually the sole defense to a charge of diversion of cargo, the Maritime Board had initially appeared receptive to the consideration of other factors that would also serve as a justification for diverting cargo. However, the Board found that the other factors that were preferred, factors which centered primarily on the superior service provided at San Francisco, to be not credible,\textsuperscript{152} unimpressive,\textsuperscript{153} or unjustified.\textsuperscript{154} The Board's "consideration" of both the evidence offered to justify the diversion and the evidence offered to establish the inadequate service at the Pacific Northwest ports was questionable in and of itself. Apparently the Board had neglected to consider applying the concept of "fundamental right" as explicated in City of Mobile to the present case.

The precedential value of Reduced Rates on Machinery and Rates from Jacksonville remained unclear however, because the protection of naturally tributary cargo was not the focus of inquiry in either case. In fact, the test cited in Rates from Jacksonville to distinguish naturally tributary as opposed to merely tributary cargo included the consideration of the cost and the value of the cargo to the shipper. This test was taken from Reduced Rates on Machinery and was based not on City of Mobile.

\begin{footnotesize}
\begin{enumerate}
\item[149.] 7 SRR at 552 (F.M.C. 1966).
\item[150.]  id. at 538 (emphasis supplied).
\item[151.]  id. at 537.
\item[152.]  4 F.M.B. 665, 676 (1955).
\item[153.]  id. at 676.
\item[154.]  id.
\end{enumerate}
\end{footnotesize}
and the concept of cargo diversion, but rather it was based on a Supreme Court decision concerning railroad rate differentials. While Reduced Rates on Machinery and Rates from Jacksonville may be distinguished factually from typical port discrimination cases, (i.e., cases which usually focus on equalization practices and indirect service), the requirement of equality of "other factors" was initially established in City of Portland. City of Portland not only laid the foundation for port discrimination cases through the concept of naturally tributary cargo, but it also appears to have given the Commission the flexibility to weigh policies, which had not been indicated in previous decisions. Whatever the strength of precedent for such an interpretation, the clear thrust of both sets of cases was that the concept of "fundamental right" could fall in the face of certain "transportation conditions."

VII. THE DOCTRINE OF NATURALLY TRIBUTARY CARGO—AS CONTAINERIZATION EVOLVES

By 1967 the Commission had built upon the foundations of decisions beginning in 1941 and had established "law" or principles regarding the diversion of naturally tributary cargo. This included the principle that the right of a port to cargo from areas tributary to it is a fundamental right based upon Section 8 of the Merchant Marine Act of 1920 (City of Mobile). City of Mobile concluded that "all other factors being substantially equal", ports should receive the benefits of proximity to given geographical areas, and violation of this principle is justified only through evidence of inadequate service at that port, an emergency situation (City of Portland) or if the aggrieved and distant ports do not represent distinct naturally tributary areas (City of Beaumont, Stockton Port District).

VIII. THE MODERN CASES OF PORT PROTECTION

A. INVESTIGATIONS OF OVERLAND AND OCP RATES AND ABSORPTIONS

The first of what may be considered the "modern" cases in the evolution of port protection was borne of a historic event which preceded the modern cases by roughly 100 years. The completion of the first transcontinental railroad in 1869 provided the Pacific Coast ports with the means with which to compete with the Atlantic and Gulf ports for the voluminous flow of cargo from the American Midwest to Far East.\textsuperscript{155} Investigation of Overland and OCP Rates and Absorptions\textsuperscript{156} focused on a system of ocean rates through the Pacific gateways which were struc-
tured so that when the ocean rate was combined with the applicable inland rates, such rates approached parity with that of the combined rates charged by their Atlantic and Gulf Coast counterparts. Thus, while the principle aim of Overland/OCP ratemaking was to allow ocean and rail carriers serving the Pacific Coast to meet Atlantic and Gulf competition, the result, which was clearly beneficial to shippers, was to provide shippers with an alternative third coast through which to move their cargo. After no less than 40 years of operation, the Atlantic and Gulf ports challenged the system as one which unlawfully diverted "traffic [which] inherently and geographically" belonged to the Atlantic and Gulf ports.

Assuming that the assertion that Overland/OCP ratemaking could be considered a form of port equalization, the Commission declared that the complainant ports' attempt to claim as their naturally tributary area the entire central portion of the United States would be absurd. The Commission further stated that "naturally tributary cargo" applied to "territory locally tributary to a particular port" or a cluster of ports as in City of Beaumont, rather than to the general territory which an entire range of ports or more than one range or seaboard may serve competitively.

In his dissent, Commissioner Hearn found little distinction between the port equalization of previous cases and the "national equalization" of the Overland/OCP tariffs, tariffs which he termed "the grandaddy" of intermodalism. While agreeing with the Commission's decision limiting application of this right to "naturally tributary" cargo, the Commissioner expressed a disdain for it; "we are now entering [into] an era [of] transportation when concepts such as 'naturally tributary' may no longer suit the needs of transportation. The Commission should make it clear that these concepts cannot prevail if they prevent substantial benefits from accruing to the shipping public or [if they] obstruct innovative action in transportation." The statement of Commissioner Hearn in Overland/OCP

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157. Overland/OCP rates were established using usual ratemaking factors, although an emphasis was placed upon competition. As the Commission explained "the rate necessary to achieve parity with the Atlantic or Gulf gateway is obtained by subtracting the rail charges covering a representative shipment via the Pacific Coast from the sum of the railroad ocean charges for the same shipment via the most likely competitive route. 10 SRR at 912 (F.M.C. 1969).

158. One such agreement was, in fact, filed with the Shipping Board as early as 1917, while the generic PWC agreement was done so in 1923. Id. at 913.

159. This distinction between equalizing inland-ocean rates to and from ports within the same range and that of meeting the same combination of a competitive coast seems to be one without a difference. Steamship lines, in the former, were absorbing inland costs differentials while in the latter they were, in essence, absorbing some of the ocean/rail disadvantage to shippers. The principle is the same and amounted to, as Vice Chairman Hearn described it "national equalization." 10 SRR at 936 (F.M.C. 1969) (dissenting opinion of Commissioner Hearn).

160. Id. at 940 (dissenting opinion of Commissioner Hearn).

161. Id. at 936.

162. Id. at 940. Benefits of overland/OCP rates to exporters and importers primarily stressed
should be contrasted with an earlier statement he made in *City of Stockton*, in which the Commissioner expressed a concern with carrier power over ports. Commissioner Hearn's statement in Overland/OCP would foretell a developing theme in future Commission decisions.

In the past the Commission had not made a serious attempt to delineate zones naturally tributary to either the complainant Atlantic or Gulf Coast or to the defendant Pacific Coast ports. The long unchallenged history of Overland/OCP ratemaking, innovative when it was first devised and initially vulnerable to regulatory attack, had by this time become fundamentally ingrained in the nation's transportation system, and was of such clear benefit to shippers that the Commission could not reasonably refuse to sanction it. The fact that the practice unquestionably involved no diversion of cargo "local" to any of the four ranges as was the case in *City of Mobile* and *City of Beaumont*, along with the fact that the practice fostered "constructive" competition which the Commission has sought to uphold in *Rates from Jacksonville*, further added to the strength of its support. The decision essentially reflected a more liberal approach to port protection.

**B. INTERMODAL SERVICE TO PORTLAND, OREGON—A LOAD CENTER AND CREATIVE REGULATION**

Absorption, a more traditional form of port discrimination, led the Commission to institute an investigation in the case of *Intermodal Service to Portland*. At issue in the case were the tariffs of two Trans-Pacific steamship conferences which authorized cargo to be discharged from member carriers at the Port of Seattle and which was then transported by inland carrier to Portland at the carrier's expense. Perhaps more than in any previous case, the conflict between both the interests of steamship lines in limiting their ports of call and between that of developing ports in

"the desirability of the alternative Pacific Coast routes, providing greater speed and flexibility in meeting sales and production deadlines at competitive cost," [while] allowing reduced inventories and therefore reduced financial costs. Warehousing and national distribution centers had been built to best serve areas in proximity to Pacific Coast ports as had entire systems of merchandizing, distribution and marketing. OCP/overland ratemaking and the increased availability and attractiveness of the Pacific gateway were therefore important in the event of labor strikes. 10 SRR at 503 (F.M.C. 1969).


164. Although the practice at issue was labelled absorption, it was more akin to transshipment as steamship lines arranged inland carriage, paying the applicable charge for motor carrier movement from Seattle to Portland. 12 SRR 601, 611 (F.M.C. 1971) (Initial Decision). See also text accompanying note 52 supra.
seeking their "share" of the flow of containerized cargo would converge. The Administrative Law Judge and the Commission each attempted to fashion compromise solutions that would best serve the competing needs of steamship lines and the needs of a port relegated to the status of a "load center".

Portland was developed as a container port somewhat later than Seattle. Seattle had not only captured its own local cargo but had also managed to reach deep into the interior of the country for Overland/OCP traffic and was what would be termed a "load center". In contrast, Portland had invested in container facilities but primarily handled traffic local to it and did not attract significant amounts of Overland/OCP cargo. In what amounted to a vicious circle, the inability of Portland to compete for the Overland/OCP traffic meant that it could not attract adequate steamship service and consequently it could not compete for traffic from the "common tributary territory" it essentially shared with Seattle. Moreover, the steamship lines could render service legally inadequate at Portland by simply refusing to call there and, following the standards enunciated in City of Portland, could force the Commission to sanction their use of indirect service. Administrative Law Judge Morgan proposed a unique if unconventional solution in this instance. As a compromise, steamship lines serving Portland indirectly through Seattle could do so only by offering such service at a premium of $1.50 a ton more than the carrier's ocean rate from Seattle. The premium sought to encourage shippers to utilize the more costly indirect service only if they deemed the direct service from Portland inadequate, with the hope that additional direct service to Portland would result, based on the cost advantages over indirect service. Subject to this limitation, the absorption practice would be lawful, since it did not appear contrary to Section 8. In addition, such a practice would obviate the need for continuous litigation and would remain consistent with the test for unlawful diversion established in City of Portland.

165. This may have been the initial Commission consideration of a legitimate container load center and its consequences. In its order of investigation, the Commission noted that "the determination of these matters is of prime importance for the guidance of the shipping industry and should be made the subject of a full hearing." 12 SRR at 603 (F.M.C. 1971).

166. Portland and Seattle were found to be in "essentially the same geographic area," serving a "somewhat common tributary territory." 14 SRR at 126 (F.M.C. 1973). See Stockton v. PWC, 6 SRR 505 (F.M.C. 1965); City of Beaumont v. Seatrain, 2 U.S.M.C. 699 (1943).

167. In this manner economics, rather than the Commission, would determine the adequacy of service. 12 SRR at 629 (F.M.C. 1971).

168. The spirit of Section 8 was at least reflected in the Hearing Examiner's statement that "[w]hile no party has mentioned the matter of natural defense, it is always possible that bombs or missiles in the event of world hostilities may destroy some of our port facilities in which circumstances alternate facilities would be essential. The development of port facilities should be encouraged." Id. at 621. See text accompanying note 75 supra (history of Section 8).
Exceptions were filed. The Commission succinctly framed its difficult task as one of "determining how much of our present approach is still of value and, to the extent [that] it is not, how much of it we may discard within the limits of law and of fair and prudent administration."\(^{169}\)

While noting that the concept of naturally tributary cargo had no application to cargo which moved predominantly through Pacific Northwest ports, the Commission found that there was a significantly smaller amount of "local cargo" that moved through Portland from areas where the "proximity of local industries and lower inland mileage suggested the 'naturalness' of movement through one rather than the other port."\(^{170}\) The only defense to a diversion of such cargo, as enumerated in *City of Portland*, was inadequate service at Portland.

While the service at Portland was certainly adequate for such small local cargo flow, the Commission recognized that conference carriers who dominated the trade could easily surmount this "barrier" and could gain access to cargo by simply refusing to call at Portland, thus rendering service inadequate by their very act. The Commission's solution was to require a direct call to Portland on alternate voyages as a condition for allowing lines to continue to provide indirect service there.\(^{171}\) Thus, the Commission attained the same result sought by the Administrative Law Judge, but without the infirmities of a differential, and without penalizing shippers for utilizing an indirect service beneficial to them. The Commission also felt that its solution amply served the policies of Section 8, although the impact of that provision was slight because of the small amount of tributary cargo to which it applied. In any event, Section 8 did not proscribe specific conduct.\(^{172}\)

These exercises of "creative" regulation, both proclaimed as an attempt to reconcile the economics of containership operation with the promotion of port development and as a protection of the competitive interests of ports, were better explained through the Commission's state-

\(^{169}\) 14 SRR 107, 125 (F.M.C. 1973). Again, in recognition of the importance of the principles to be considered, the Maryland Port Administration advocated treating the case as a rulemaking to examine the broader issues. *Id.* at 124. The issue of cargo diversions, complex and controversial, has prompted other such cries for formal rulemaking. See Cargo Diversion Practice at U.S. Gulf Ports, 16 SRR 1265 (F.M.C. 1976), Cargo Diversion—Denial of Petition for Rulemaking, 14 SRR 236 (F.M.C. 1973) clarified 14 SRR 630 (F.M.C. 1974).

\(^{170}\) *Id.* at 126.

\(^{171}\) 14 SRR at 128 (F.M.C. 1974).

\(^{172}\) Hearing Counsel, while acknowledging the policy conflict between the development of ports and of intermodalism, suggested that until Congress made a determination that it favored development of the latter, the promotion of the development ports, as already embodied in Section 8, must prevail. The conferences and Seattle interpreted Section 8 as enunciating a general policy of port promotion only, not to be followed if the result was the hinderance of the development of containerization. This conflict or divergence of opinion, was no more resolved in this case as had been in those previous.
ment that "a major consideration in this proceeding, aside from the matter of the rights of Portland with respect to naturally tributary cargo, is the extent to which each port should be allowed to develop into a container "load center"." Portland's concern, as echoed by the Commission, did not center upon the diversion of its local cargo, but rather upon the hope of attracting what Portland considered its share of the enormous flow of Overland/OCP cargo that flowed to Seattle, a flow that had been established through Seattle's early financial commitment to the development of container facilities. This cargo was naturally tributary to neither port and therefore, based on Commission precedent, did not warrant Commission "creativity" or protection.

Based on City of Portland, indirect service and equalization could be sanctioned only if direct service to Portland was found to be inadequate. This was not found to be the situation. The inquiry could have ended at that point, but Portland would have still faced problems in attracting additional direct service to capture Overland/OCP cargo. The established legal standard was essentially changed to accomplish that objective; the right to provide indirect service was conditioned on the adequacy rather than on the inadequacy of direct service. Portland was therefore assured of some level of direct service.

By clinging to the existing legal standard for unlawful diversion, the Commission both compelled service for all practical purposes (which was beyond its authority) and the Commission also did not consider the more obvious, but difficult solution of prohibiting absorption on cargo it determined local to Portland. This would have provided carriers already serving the port with a larger cargo base and with an additional incentive to remain at Portland. Other carriers would have been faced with the decision of whether a direct call to Portland, as based on the amount of cargo "guaranteed" to the port, was justified.

C. **THE MINIBRIDGE DECISION—A NEW TEST EVOLVES**

In Intermodal Service to Portland, the Commission was confronted with the traditional means of port equalization: the practice of absorption.

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173. Id. at 128.
174. See San Diego Harbor Com. v. Matson Navigation Co. 2 SRR 127 (F.M.C. 1963). See also Scott Paper Co. v. Puerto Rico Maritime Shipping Authority 14 SRR 1616 (F.M.C. 1975), "Unlike sister agencies, the Interstate Commerce Commission and the Civil Aeronautics Board, the FMC does not issue certificates of public convenience and necessity, requiring maintenance of service on listed routes." Id. at 1617.

On August 30, 1985, the Trans-Pacific Freight Conference of Japan petitioned the FMC to set aside restrictions on indirect service to Portland arising from the Commission's decision in Intermodal Service to Portland. The petition stressed the present use of larger containerships that necessitated to an even greater degree limitations of port calls. Petition of Defendants to Set Aside Order in Part, Service to Portland, Oregon, 14 SRR 107 (F.M.C. 1973).
In the past the practice of absorption had been considered the principle evil of port discrimination claims. Now, however, absorption had evolved into a means to an end, with the end being that of the container load centers. The Commission would next examine what was at the time considered a new dimension of intermodalism, the now-familiar minibridge.\footnote{175}{For a definition of minibridge, see text accompanying note 51 supra.} In actuality, the minibridge was really an extension of the equalization practice of transshipment. At the time of its introduction the minibridge was perceived to be such a bold innovation that it would, in principle, be subjected to detailed Commission scrutiny through two major decisions, \textit{Board of Commissioners v. Seatrain} and \textit{Council of North Atlantic Shipping Associations v. American Mail Lines}.\footnote{176}{Of these two decisions, the latter case, \textit{North Atlantic Shipping}, would, in one fell swoop, wipe clean the slate of Commission precedent and would help to formulate a new test regarding the diversion of naturally tributary cargo.} Of these two decisions, the latter case, \textit{North Atlantic Shipping}, would, in one fell swoop, wipe clean the slate of Commission precedent and would help to formulate a new test regarding the diversion of naturally tributary cargo.

In the first case, \textit{Board of Commissioners v. Seatrain},\footnote{177}{\textit{Id.} at 763.} the Gulf ports assailed Seatrain’s European minibridge. Seatrain had established joint rail/water rates with the Southern Railway for service between New Orleans\footnote{178}{\textit{Id.} at 763.} and Europe through Southern’s movement of containers to Charleston, South Carolina and ocean transportation on Seatrain vessels from there. The complainant ports alleged that the minibridge unlawfully diverted their naturally tributary cargo in contravention of Sections 8, 16, 17, and 18. The complainant ports also voiced their concern that the unlawful diversion of cargo placed their current investments in jeopardy by impinging upon the cash flow necessary to service outstanding bonds, by discouraging future investment, and by threatening their very economic existence.\footnote{179}{Administrative Law Judge Levy found both the Gulf ports’ claims of injury\footnote{180}{The Administrative Law Judge concluded that the ports individually had suffered from infirmities unrelated to the impact of minibridge, including export/import imbalance, decreases in military cargo, strikes, insufficient cargo volume to justify a direct call, and competition among themselves. Furthermore, even conceding that some cargo was diverted, the amount diverted, was such an insignificant percentage of the total cargo of the ports as to be unworthy of protection. This was indicated by the complainant’s own statement that their cargo flow had not decreased as a result but rather their \textit{increases} had been spared. Models that purported to assess the overall negative impact of the minibridge on the ports had failed to include both the economic}}
tion'' (i.e., a radius in which the cargo can ipso facto be demonstrated to be naturally tributary)\textsuperscript{181} or any other test for naturally tributary areas that also recognized the public interest as well as innovation.\textsuperscript{182} Judge Levy found the key to lie with the public interest which was perhaps best reflected in a traffic manager's decision regarding how to route his cargo so as to earn the greatest profit for his company. The concept of providing for the public interest flexibly through innovation was something that Congress could not have intended to stifle despite the fact that the Shipping Act of 1916 and the Merchant Marine Acts were conceived prior to intermodal capability.\textsuperscript{183} A balancing test emphasizing innovation along with competition would insure that the best interests of the public would be served.

The Commission adopted the Initial Decision, determining that the concept of naturally tributary cargo could not "be extended to the point where a port or range of ports can claim a multi-state inland region as its exclusive territory"\textsuperscript{184} while no individual port had sought to establish an area locally tributary to it alone. By basing their argument on historical flaws rather than on the basis of fair competition, the Gulf ports sought support for the rather flawed notion that Congress had intended Section 8 to freeze international transportation movement into the pattern found in the 1920's.\textsuperscript{185}

The second of perhaps the two most significant cases with respect to the development of the legal protection of ports (the first being City of Mobile and its establishment of the doctrine of naturally tributary cargo) was the case of Council of North Atlantic Shipping Associations (CONASA) v. American Mail Lines.\textsuperscript{186} In lieu of a requested rulemaking

\textsuperscript{181} 16 SRR at 259 (F.M.C. 1975).

\textsuperscript{182} Id. No definitions of the term "naturally tributary" were submitted which did not ignore the benefits of innovation and technology to shippers, not could ports answer the "obvious" questions proposed by the Examiner which he asserted should serve as basis for consideration of the concept. For example "are the cargo's origin and destination geographically proximate to the port?" In what way is the flow of cargo through that particular port in the public interest? What economic factors ind cargo inextricably to a port?

\textsuperscript{183} 16 SRR at 259-60 (F.M.C. 1975). Competition, to the public benefit, was within the context of those Acts, as were load centers that had altered the bounds of naturally tributary areas established by breakbulk cargo. Cited was Commissioner Hearn's observation in dissent in Overland/OCP Rates and Absorptions that the concept of naturally tributary cargo had perhaps been outmoded by transportation innovation. Supra note 160.

\textsuperscript{184} See Overland/OCP Rates supra note 160. (Claims that cargo of central United States inherently belonging to Gulf and North Atlantic ranges refuted.)

\textsuperscript{185} The importance of historical cargo flow to the determination of naturally tributary status was, in other words, significantly discounted.

\textsuperscript{186} 18 SRR 774 (F.M.C. 1978).
to dispose of all of the "cargo diversion issues," CONASA was designated as the lead case for the establishment of general minibridge principles. The Commission recognized that developments in transportation had sharpened the historical conflict between that of the ports, which sought the maximum amount of carrier calls attainable, and that of carriers, who continually sought to reduce the number of port calls through devices such as containerization, intermodalism, and the minibridge. Thus, these two economic interests were pitted against one another.

Two steamship lines filed a petition for a general rulemaking proceeding to consider absorption and equalization practices, particularly to sanction them as lawful under Sections 16 and 17, 14 SRR 326 (F.M.C. 1973), clarified, 14 SRR 630 (F.M.C. 1974). At the time, twelve cases involving such practices were pending before the Commission, "an aggregate of 29 conferences, about 30 port authorities, port intent groups and labor groups, and 82 steamship lines parties to one proceeding or another." The petitioning parties felt this ad hoc adjudicatory approach unfair, unworkable, and a serious drain on the resources of most ports. Id. at 237. The Commission, however, rejecting the request, noted that the very generality of the explicit standards of Sections 15, 16 and 17 of the Shipping Act, 1916 (undue and unreasonable prejudice, for example) did not permit issuance of general rules but mandated a case-by-case determination. In lieu of instituting a rulemaking, and recognizing the problems attendant with multiplicit litigation, two cases were chosen to serve as vehicles for the development of general principles. Council of North Atlantic Shipping Ass'n v. American Mail Lines 18 SRR 774 (F.M.C. 1978) (minibridge).

One of the pending port discrimination cases at the time of the Commission's denial of rulemaking was Cargo Diversion Practice at U.S. Gulf Ports By Common Carriers By Water Which Are Members of the Gulf-European Freight Assoc., 16 SRR 1265 (F.M.C. 1976). Administrative Law Judge Kline dismissed that adjudicatory proceeding and recommended that the Commission institute a rulemaking to consider the peculiar problems of cargo diversion in the Gulf, an approach "far better than the present state of affairs in which a plethora of such" cargo diversionary "cases have continue to spring up around the country requiring time-consuming litigation." Id. at 1275. His entire action, and rationale is contrary to the earlier Order Denying Rulemaking, to the point of suggesting approaches or standards for consideration. Id. at 1283-84.

Judge Kline saw Intermodal Service . . . at Philadelphia, which had been designated as a lead case, as, too, suffering from "stalemate and old age largely attributable to the use of an adjudicatory procedure" and "paralyzed" as a result. Id. 1281. That assessment appears accurate, in light of a continuing progression of procedural difficulties. 14 SRR 57 (F.M.C. 1973); 14 SRR 435 (F.M.C. 1974); 14 SRR 539 (F.M.C. 1974); 14 SRR 592 (F.M.C. 1974); 14 SRR 664 (F.M.C. 1974); 14 SRR 780 (F.M.C. 1974); 16 SRR 556 (F.M.C. 1975); 16 SRR 1546 (F.M.C. 1976); 16 SRR 1613 (F.M.C. 1976).

17 SRR at 811-12 (F.M.C. 1977); See Cargo Diversion—Denial of Petition for Rulemaking, 14 SRR 236 (F.M.C. 1973). Minibridge does not fit into the traditional "load center" scheme with its foundation the elimination of port calls to "adjacent" ports. See Intermodal Service to Portland, Oregon 14 SRR 107 (F.M.C. 1973). Complainants in CONASA attempted to cast minibridge in light that, however, in alleging that the ocean carrier's net revenue after division of total rate with rail carriers was less than that realized in all-water, OCP or local service. 17 SRR at 835 (F.M.C. 1977). The impact of designation of these lead-cases on the then recently decided case of Intermodal Service to Portland was a source of confusion, 14 SRR at 632 (F.M.C. 1973), prompting the Commission to announce that it was not its "intention to abandon the principles relevant to absorptions announced therein," Id. at 634.

The economic interests of complainant North Atlantic ports presented at hearing were different only in magnitude from those stressed previous cases. More succinctly, port interests char-
The hub of this intense conflict was the use of the minibridge from the Far East to the U.S. Atlantic coast via the Pacific Coast ports. The complainants asserted that by diverting their naturally tributary cargo the "Far East" minibridge was violative of the policies of Section 8, and that this warranted an examination of the doctrine of naturally tributary cargo. Administrative Law Judge Gosgrave concluded that the confusion surrounding the application of Section 8, particularly the availability of defenses, \(^{189}\) was based on a neglect of the fact that Section 8 expressed one Congressional policy that clearly mandated a balancing of interests; \(^{190}\) interests of carriers (often minimized) as well as the interests of ports. As in Seatrain, a balancing of these interests was to establish the lawfulness of the use of the minibridge.

In adopting Judge Gosgraves decision, the Commission formally adopted a new balancing test for adjudging the unlawfulness of cargo diversion, although the Commission acknowledged that it was "not practical or feasible to draw future guidelines...if by guidelines (it) is meant the drafting of precise rules by which a simple determination of legality or illegality could be made." \(^{191}\) The test that did evolve consisted of three parts. First, the threshold inquiry was whether the cargo was within the naturally tributary zone of the aggrieved port, a zone that was constantly

\(^{189}\) Judge Cosgrave surmised that the decision in Discounting Contract/Non-contract Rates, 9 SRR 726 (Initial Decision) (F.M.C. 1967) reversed, 10 SRR 15 (F.M.C. 1968), allowed the conclusion that so-called traditional defenses, including volume of traffic, competition, distance, advantages of location, character of traffic and frequency of service. Surcharge on Shipments from Buffalo, 2 SRR 111, 114-15 (F.M.C. 1962), citing The Port Differential Investigation, 1 U.S.S.B. 61 (1925). See also Alaskan Rate Investigation, 1 U.S.S.B. 1 (1919) (advantage of 171 miles over route of nearly 1000 not sufficient justification for rate disparity were available only if Section 8 was not utilized as the basis for the allegation). In Discounting Contract/Non-Contract Rates the tariff of the India, Pakistan, Ceylon & Burma Outward Freight Conference allowed its members to offer discounts on certain iron and steel items of up to 30% off of the conference rates, which were restricted to certain ports of origin. The port of New York complained that the rates were not applied equally and burdened its flow of cargo.

The Hearing Examiner found that the rates were not the principle cause of the loss of traffic but instead "the preference of shippers for outports," 9 SRR 751 (F.M.C. 1967), "the outports nearness to main producing mills or cheaper inland freight costs, experience of outports in handling steel, outports geared to handle steel in large lots." \(^{190}\) Id. at 750. The Commission, however, found only two of the factors considered by the Hearing Examiner, served to justify...comparative loading costs and carrier competition. 10 SRR at 25 (F.M.C. 1968). If violation of Section 8 was alleged, inadequacy of service at the aggrieved port was the only defense. \(^{191}\) See for example, Stockton Port District v. Pacific Westbound Conference, 6 SRR 505 (F.M.C. 1965).

\(^{190}\) 17 SRR at 833 (F.M.C. 1977).

\(^{191}\) Id. at 778-779 quoting Initial Decision, 17 SRR at 830 (F.M.C. 1977).
changing and which was dependent upon the commodity involved as well as by a consideration of several other factors. These other factors included (a) the flow of traffic through the port prior to the conduct in question; (b) the relevant inland transportation rates; (c) natural or geographical transportation patterns and efficiencies; and (d) shipper needs and cargo characteristics.\(^{192}\) Second, once the diversion had been established, the reasonableness of the diversion would be determined by a consideration of (a) the quantity and quality of cargo being diverted (i.e., is there substantial injury); (b) the cost to the carrier of providing direct service to the port; (c) any operational difficulties or other transportation factors that bear upon the carrier's ability to provide direct service (i.e., lack of cargo volume, inadequate facilities); (d) the competitive conditions existing in the trade; (e) the fairness of the diversionary method or methods employed (e.g., absorption, solicitation).\(^{193}\) Finally, the harm suffered by the port would have to be substantial.\(^{194}\)

This test or balancing of interests was designed to end the utilization of Section 8 so as to protect ports at the expense of or to the detriment of carriers serving those ports. Such a test would guide all future allegations regarding violations of Section 16 First and Section 17 of the Shipping Act of 1916 based on charges of cargo diversion. With this new standard in place, the Far East minibrige was deemed to be lawful.\(^{195}\)

The CONASA/Seatrain decisions, by upholding the Far East and Gulf/European minibrige systems, effectively overruled City of Mobile and the previous line of cases which had awarded ports with a fundamen-

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192. 18 SRR at 77 (F.M.C. 1978).
193. id.
194. The "but for" test, of causation of diversion by the practice, rejected in Sealand v. SACL, 6 SRR 1105 (F.M.C. 1966), was also reinstated by the Administrative Law Judge, 17 SRR at 836 (F.M.C. 1977), note 88 and, thus, arguably, adopted by the Commission, though not explicitly.
195. CONASA had not even sought to delineate the area "naturally tributary" to it, nor to determine the extent of the diversion. While a radius of 50 miles from the port was suggested by CONASA as locally "tributary," 18 SRR at 836 (F.M.C. 1978), it placed its sole reliance on the fact that the container was loaded at the port city at railhead and the case suffered from the same lack of substance as did those of its Gulf counterparts in Seatrain, supra note 166. Suggested, however, was an appeal for retention of the protection of cargo if only in considerably restricted degree, "local tributary cargo," as noted in intermodal Service to Portland, Oregon, 14 SRR 107 (F.M.C. 1973).

To contrast the effect of such a perimeter of protection, in 1976, 53% of the port of New York and New Jersey's export business originated over 50 miles from the port and 26% of the port's imports were destined for areas outside that 50 miles. Effects of Intermodalism—On Cargo Gateway Selection & The Port Industry, WORLD WIDE SHIPPING/WORLD PORTS MAGAZINE 83-84 (Dec./Jan., 1984). The port of Boston draws 76% of its total liner volume from within 55 miles of its waterfront—only 2% of Boston liftings are generated in localities beyond 100 miles from the port. Hearing on April 11, 1984, Notice of Inquiry FMC Docket No. 83-38. Statement of Rino Moriconi, Assistant Port Director, Massachusetts Port Authority at 8.
tal right to naturally tributary cargo. This result occurred a scant two
years after the decision in City of Mobile and City of Beaumont in which
the regulatory flexibility was needed so as to prevent a stifling of innova-
tion. Over a period of thirty years, Section 8 had evolved from a policy
embodying a fundamental right of ports to Shipping Board protection, (as
was illustrated in City of Mobile), to a policy which reflected only a na-
tional concern for ports (as illustrated in Seatrain).196

It also seems clear that even if the complainant ports in both the Sea-
train and CONASA cases had shown the substantial damage found to be
lacking and had ultimately proven this to be fatal in each case, the
minibrige idea would been upheld nonetheless.197 Unlike the previous
cases such as Sealand v. SACL and Intermodal Service to Portland, the
use of the minibrige had such potentially broad application and was of
such clear benefit to shippers,198 let alone carriers, that the past tests for
unlawful diversion were outdated. Even the new CONASA/Seatrain
guidelines somehow seemed inappropriate.

The minibrige concept thus provided an easy application of the new
standards. What remained unclear was the extent to which the guidelines
would lend themselves to the application to a true load center (i.e., a
feeder port battle over “common cargo”). Diversion between adjacent
ports would also demonstrate the extent to which any of the principles
embodied in Intermodal Service to Portland still applied.199 Finally, there
was a need for a demonstration of how effective the new guidelines would
be in providing a more substantial indication as to the parameters of per-
missible practice. By discarding defenses that had severely restricted
carrier flexibility, the Commission had laid the foundation for the potential
chaotic eruption of cargo diversion proceedings. Certainly, the CONASA

196. 18 SRR at 772 (F.M.C. 1978).
197. Administrative Law Judge Levy stated in Seatrain, supra note 166, “Even if the growth
were so great, and even if the service expanded into other trades to the point where the impact
on the ports became substantial, we would then have to ask ourselves why has this come about?
Would it have been caused by an unconscionable, unscrupulous, underhanded, undercutting
competitive methods or because a better mousetrap has been fashioned?” 16 SRR at 273
(F.M.C. 1976). This was echoed by Judge Cosgrave observation in CONASA that “the effect of
the allegedly prejudicial practice on all interests—including shippers must be taken into account
when measuring the substantiality of the prejudice or preference.” 17 SRR at 838 (F.M.C.
1977).
198. Minibrige gives shippers a choice of all-water or joint rail/water, the greater service
frequency and shorter transit time, coupled with the single bill of lading and single rate, at no
greater cost. . . [Additionally, it combines “simplicity of documentation, easy ascertainment of
total transit charges with single bookkeeping and insurance entities. [Further] the shipper need
look only to a single carrier regarding damage claims, [because] the carriers will ascertain liability
as between themselves.” 16 SRR at 274 (F.M.C. 1976).
199. See text accompanying note 188 supra.
categories of "fairness" and "transportation efficiencies" allowed much room for interpretation and therefore the introduction of controversy.

D. DART CONTAINERLINE—THE MISAPPLICATION OF THE NEW STANDARDS

The first test for the new law of port discrimination as developed and represented by the standards in CONASA occurred in North Carolina State Ports Authority v. Dart Containerline. At issue was the utilization of transshipment, a practice virtually identical to that found to be unlawful in the pre-CONASA case of Sealand v. South Atlantic and Caribbean Line. Dart had received cargo at the Port of Wilmington and had shipped it overland to Norfolk at its own expense. The cargo ultimately was destined for direct service to Europe. Wilmington alleged unlawful diversion of its naturally tributary cargo (unmanufactured tobacco) to which Dart's indirect service was limited. Under CONASA guidelines, the first thing that would need to be determined would be the boundary of the areas naturally tributary to both ports. Such a determination would be based on the following factors: historical flow; inland transportation rates; natural or geographic transportation patterns or efficiencies; shipper needs; and cargo characteristics.

The Administrative Law Judge applied the new "standards" and found the following. First, prior to the development of port facilities in North Carolina, the flow of unmanufactured tobacco had been predominantly through Norfolk which still laid claim to 51.7% of U.S. exports of the commodity. Second, an examination of inland rates proved to be difficult to surmise because the transportation of the particular commodity was not regulated and was thus subject only to negotiation between carrier and shipper. An analysis showed that on the average, there was only a slight disparity regarding the inland rates between the two ports and such rates were incapable of absolute determination because of their ne-

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200. 19 SRR 521 (F.M.C. 1979), aff'd sub nom. Dart Containerline v. F.M.C., 639 F.2d 808 (1981). It was clear that the economic basis for interests of the adverse parties had changed in magnitude but not in nature over the years of port discrimination claims. A weekly Dart call at Wilmington would cost approximately $38,291.67; $1,367.56 per box if it could obtain the 28 boxes of unmanufactured tobacco that the major line served Wilmington directly, (which Seatrain did), and $254.63 per box if it could average the 150.4 containers per call overall handled by Seatrain. Balanced against this was the $300 per container cost of Dart's overland truck substitute service.

The port of Wilmington had committed $32 million in development of its facilities, including $8 million for container facilities and was seeking 14 million for more. The loss of all unmanufactured tobacco to Dart's service would cost Wilmington yearly revenues of $80,426 and should loss of that cargo induce Seatrain to cease direct service, $213,455. 18 SRR at 1503 (F.M.C. 1978).

201. 18 SRR at 1510 (F.M.C. 1978). 13.2% moved through Wilmington. Id.
gotiated nature. Third, the determination of what rightfully belonged to a ports' natural or geographical transportation pattern and efficiencies required an examination of such things as the quality of the highways feeding the ports, a look at the surrounding railroad networks, etc. Norfolk's superior highway network was self evident but was apparently of little significance. Finally, an evaluation of the shippers needs and cargo characteristics only served to illustrate that inland rates were important to shippers and that personal relationships between shippers and carrier representatives entered into the final choice of a port.\(^{202}\)

Although the second tier of the CONASA guidelines was applied, it was clearly unnecessary because the threshold test (that of the diversion of naturally tributary cargo) had not been met. Judge Levy found the commodity to have shown "no preference [for any port] whatsoever and [it] is not naturally tributary to any port."\(^{203}\) On the average, the markets that the commodities were bound were equidistant from both ports. Historically, unmanufactured tobacco was more naturally tributary to Norfolk than to any other port. However, even without the implementation of Dart's substitute service, the tobacco would have moved through both ports.

With Seatrain serving Wilmington directly and Dart indirectly, and with competition conducted on the basis of service (rates were at parity), Dart would have a significant impact only if its service better served shipper needs and requirements. To deny shippers such a choice was found not to be in the public interest.

Perhaps the decision best reflects the liberal spirit of CONASA in accommodating the needs of carriers to concentrate on their ship calls and direct service. The indirect service of Dart would have allowed it to compete for cargo with previously established North Atlantic service without facing additional port calls. Ultimately, such competition was to the advantage of shippers. Based on the finding that the cargo was not naturally tributary, however, the port/carrier conflict did not reach the proportion that it would have had Dart been adjudged to have been diverting cargo belonging to Wilmington or to its Norfolk load center. The ultimate conflict between load center and feeder port was averted.\(^{204}\)

Whatever significance that could be attached to Judge Levy's appli-

\(^{202}\) Presumably, such personal relationships were important only if economic considerations were substantially equal, the transportation managers making an "economic judgment of how to make the best profit for his company." Board of Comm'n v. Seatrain, 16 SRR 235, 265-6 (F.M.C. 1975).

\(^{203}\) Wilmington was, in fact, on the average of 11 miles closer to major tobacco markets in North Carolina and Virginia. 18 SRR at 1507 (F.M.C. 1972).

\(^{204}\) That conflict had taken place in Intermodal Service to Portland, 12 SRR 601 (F.M.C. 1971), not resolved but merely addressed by compromise.
cation of the CONASA guidelines in the context of modern intermodalism was short lived, for in a 3-2 decision, the Commission struck down Dart’s transshipment scheme. The majority stated that Dart’s substitute service was premised on an assumption that unmanufactured cargo would naturally move to Wilmington. If the cargo did not move to Wilmington, there would be no need for Dart’s service because the cargo would likely move to Norfolk. Furthermore, regardless of the apparent overlap of the two port’s hinterlands, once the cargo arrived at Wilmington, it assumed the status of being naturally tributary to that port.

In providing two final justifications for the decision, the Commission found that “in this era of inflation and dwindling fuel resources, shippers and carriers ... [of commerce] are best served by competition which increases productivity rather than by competition based upon artificial shipping inducements”. Dart’s backhauling of cargo to Norfolk206 put an additional burden on Dart. The Commission felt that Dart’s failure to prove the cost of service, coupled with the operational and competitive characteristics precluded direct regular containership service and made Dart’s indirect service to the port appear to be inherently unreasonable.207

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205. 19 SRR 521 (F.M.C. 1979).
206. In Sealand v. South Atlantic Caribbean Line, 6 SRR 1105 (F.M.C. 1966), the transshipment scheme involved no such backhauling but actually moved the cargo overland closer to its ultimate destination. Nevertheless, it too, was struck down.
207. The Dart decision was, of course, not only a blow to that steamship line but also to the port of Hampton Roads, Virginia, which would also have been the beneficiary of Dart’s transshipment scheme. As southernmost port in the North Atlantic range, and capturing 75% of its exports and 65% of its imports from the southeastern United States, the port was especially hurt by the growth of South Atlantic competitors, including Wilmington.

In 1981, the Virginia Port Authority (VPA), representing Hampton Roads, challenged the South Atlantic-North Europe Rate Agreement (SANE) as representing the Federal Maritime Commission-sanctioned diversion of cargo naturally tributary to Hampton Roads. The Commission, in its Order approving a three-year extension of SANE in 1978, cited the benefits of the agreement in restoring the flow of containerized traffic that had been diverted through North Atlantic ports with the early advent of containerization at those ports from its “natural” course through those in the South Atlantic. Agreement No. 9984-14, South Atlantic North Europe Rate Agreement, (Order of Approval of Federal Maritime Commission, September 30, 1981). Specifically, challenged was the rate flexibility 48-hour independent rate action provided by SANE as opposed to the cumbersome “North Atlantic Conference” rate machinery. Cargo was diverted, alleged the VPA, to the range of least resistance. If rates are inflexible in one range, it is simple to shift the cargo to another range and service. (The two SANE members, Sealand and U.S. Lines, were also members of the North Atlantic “Conference”) where there is greater rate flexibility. Comments of the Virginia Port Authority, Agreement No. 9984-14, South Atlantic-North Europe Rate Agreement, F.M.C., (July 6, 1981).

The resolution of the controversy that had as its basis alleged diversion of the naturally tributary cargo of Hampton Roads was unconventional: the Virginia Port Authority withdraw its comments in acknowledgement of the “waiting” period for exercise of the right of independent action be lengthened from 48 hours to 30 days (10 days was originally requested by SANE for extension) and the requested extension be shortened from three years to 18 months, moderating
Commissioners Bakke and Kanuk found ample room for dissent from what could best be termed the majority’s substitution of “an ivory tower regulatory theory . . . [in place of] pragmatic commercial judgment.” The dissent cited to fatal inconsistencies inherent in the condemnation of the backhaul of cargo to Norfolk in an era of dwindling fuel reserves. The dissent further alluded to the fact that the majority seemed to ignore the “commercial reality” of the Dart/Seatrain competition. Finally, the dissent questioned placing the burden upon Dart with respect to a showing of “why it is necessary for Dart to compete in . . . this manner.”

In contrast to the Administrative law Judge’s decision, the decision of the majority in Dart did not reflect the Commission policy embodied in CONASA and Seatrain of allowing carriers to realize the benefits derived from increased flexibility and the efficiency of intermodalism. The decision to strike down Dart’s indirect service (clear commercial advantages and the justification of indirect rather than direct service notwithstanding), represented the return to an era of more zealous port protection by the Commission.

The majority also refused to discard Sealand v. South Atlantic and Carribean Lines as being inapplicable by both its decision and through guidelines set in CONASA. In Pacific Westbound Conference—Equaliza-
tion Rules and Practices," the Commission had clearly stated that its analysis in CONASA was not limited to minibrige cases, but that such an analysis had represented "a refinement in the methodology that the Commission will generally apply to all cases of cargo diversion and absorption of inland transportation cost". This methodology is no less applicable to small diversions (i.e., those involving adjacent ports in the same range) than it is to large diversions (i.e., minibrige movements). Such a declaration is certainly broad enough to apply to Dart, despite the Commission's pronouncement that "the actual holdings of the minibrige cases are not precedent for overland cost absorptions intended to attract cargo tributary. . .[to] nearby ports with adequate facilities for handling such cargo." This unjustifiable pigeon-holing of Dart placed Dart back into the rigid, factual pre-CONASA realm of Sealand v. SACL and City of Portland.

Finally, the majority also stated that "[a] different situation would be presented if Dart were to compete for North Carolina tobacco by openly adjusting its Norfolk rates rather than publishing fictitious rates. In any event it would be most appropriate for Dart to publish a true point-to-point intermodal tariff from the major tobacco markets to Europe (e.g. Danville, Virginia to Hamburg, Germany)." Notwithstanding the fact that cargo would be moved either directly to Norfolk or indirectly through Wilmington, in essence the Commission sanctioned the use of the microbridge while condemning the use of the minibrige. This inescapably leads one to the conclusion that the true basis for the decision was the fact that once the cargo moved or was induced to the port of Wilmington, it attained the status of being naturally tributary to that port. This was the situation notwithstanding the fact that the cargo had come from origins in which tobacco had consistently moved to Hampton Roads, and despite the fact that such cargo may have flowed to the port solely to take advantage of Dart's indirect service. This later case spawned the creative means which insured the flow of cargo through a particular port.

The diversion of local cargo had also contributed significantly to the condemnation of equalization schemes in cases such as City of Portland v. PWC and City of Mobile v. Baltimore Insular Lines. Such cargo diversion was labelled "traffic raiding" in the initial City of Beaumont v. Sea-train decision, which was subsequently reversed. In according cargo with

211. 19 SRR at 136 (F.M.C. 1979) note 5.
212. Id.
213. To distinguish "microbridge" from the minibrige tariffs struck down, see text accompanying note 51 supra.
such a status, the Commission had overlooked restrictions that it had previously established in the CONASA case.

In CONASA, the Commission stated that ports must identify naturally tributary areas that were both individual and distinct if they sought to invoke Commission protection. Such individual and distinct tributary areas had not been shown by Wilmington. Furthermore, in the CONASA case, the Commission, held as faulty the idea that cargo loaded within a port area, or railhead was naturally tributary to that particular port. However, the Commission appeared to reverse itself by adopting that very logic in Dart.\textsuperscript{214}

E. \textit{Pacific Westbound Conference—The Law Further Evolves}

The final chapter in the story of the evolution of regulatory protection of the cargo flow from areas naturally tributary to individual ports involved (appropriately enough) the port of Portland, Oregon. Much had changed since 1955\textsuperscript{215} when Portland and Seattle jointly sought to halt the diversion of cargo to San Francisco. By making a significant investment in container facilities during the infancy of containerization in the 1960’s, Seattle had become (to the detriment of Portland) the load center for the Pacific Northwest. The existence of Portland in the shadow of Seattle was made even more burdensome by the equalization practices of the Pacific Westbound Conference (PWC). PWC members were authorized to absorb the difference between a shippers cost of delivery to a port where the lowest inland rates applied (Portland), and the cost of delivery to a port served by an equalizing line (Seattle).\textsuperscript{216} Much had changed since the most recent case involving the “beleaguered” port of Portland in \textit{Intermodal Service to Portland, Oregon}. Portland’s present motive in seeking to have the equalization rules eliminated was not to increase direct service to Portland. This fact compelled the Commission to devise a somewhat “creative” compromise in its decision. In \textit{Pacific Westbound

\footnotetext{214}{The U.S. Court of Appeals for the D.C. Circuit found that the Administrative Law Judge had erred in focusing on the flow of unmanufactured tobacco prior to 1972; noting that tributary zones varied over time and began to shift to Wilmington to an extent at that time. Dart Containerline v. F.M.C., 639 F.2d 808, 813, 816 (1981). In affirming the majority decision, it scored the Commission, too, for considering the inefficiency of Dart’s indirect service in the first-tier of the CONASA guidelines, the delineation of the bounds of naturally tributary cargo. \textit{id.} at 817.}

\footnotetext{215}{City of Portland v. Pacific Westbound Conference, 4 F.M.B. 664 (1955).}

\footnotetext{216}{By Order of September 11, 1978, the Commission instituted an investigation into the absorption practices where allegedly there was unlawful diversion of the naturally tributary cargo of Portland. Most significant was the pronouncement that the guidelines established in the CONASA/Seatrain minibrige cases would govern this non-minibrige case and, consequently, Section 8 would not be a statutory basis under consideration. Pacific Westbound Conference-Equalization Rates and Practices, 19 SFR 133, (F.M.C. 1979) (Order of Investigation). \textit{See also id.} at 133 (confirmation that CONASA guidelines applied).}
Conference—Equalization Rules and Practices. Portland sought to grant to lines that were serving the port the right to carry Portland's "naturally tributary" cargo. Such cargo was presently being equalized through Seattle.

The first inquiry under CONASA (that of the requirement of culpability), was whether or not the cargo that had allegedly been diverted to Seattle was or had ever been naturally tributary to Portland. There was neither a demonstration that the historical flow of the cargo in question had been through Portland nor was there any proof that Portland had been favored over Seattle for certain commodities. At best, inland transportation rates did favor Portland, but this advantage was more than offset or balanced by the closer proximity of Seattle to the Far East markets. Furthermore, Seattle's advantages to shippers accruing from the infrastructure built around its load center status, when contrasted with the various infirmities or disadvantages attending the utilization of Portland, meant that service to Seattle was sine qua non in order for shippers to stay in the "export ball game".

Despite the fact that Portland had, thus, failed to meet the threshold burden of CONASA, the reasonableness of the practice, the second tier of the standard, was nevertheless considered because of the "obvious overlap between the issues of diversion from a naturally tributary zone and justification..." As the economic justification of the indirect service was unquestioned and there was no indication that the practice was unfair in its thrust or manner of utilization, the practice was upheld.

The Commission adopted the initial decision. Of greater significance however, was the way that the Commission addressed the broader principles surrounding the continued viability of the concept of naturally tributary cargo. The Commission did so despite their own assertion that consideration of such issues was more appropriate to rulemaking than to an adjudicatory hearing.

The applicability of Section 8 to Shipping Act proceedings was no longer used as a basis for investigations or for determining unlawful diver-

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217. 22 SRR 946 (F.M.C. 1984).
218. 22 SRR at 66 (F.M.C. 1984).
219. As an example, queuing delays and gang deficiencies at Portland serve both established inadequacies of service or inefficiencies under the "naturally tributary" or initial tier of the CONASA test and also serve to justify carrier decisions not to call at the port under the second tier, reasonableness of the practice.
220. The economic justification was unquestioned. As to the second factor, fairness, Seattle was neither using the equalization as an inducement in its solicitation of traffic, drawing away traffic from Portland that would otherwise have been shipped from there, nor by its substituted service, doing anything independent lines were not. There was little question of fairness.
221. 22 SRR at 961 (F.M.C. 1984). Rulemaking to consider cargo diversion issues was denied in CONASA.
However, the Commission would not discard the notion that ports had a "natural right" to certain cargo. In the eyes of the Commission, ports were still a protected class both under the Shipping Act of 1916 and under the Shipping Act of 1984. The Commission further declined to conclude that carrier equalization practices would never be violative of the Shipping Act. 223

Notwithstanding these caveats, the Commission stated that "the lesson . . . may be that the "naturally tributary" doctrine has become obsolete insofar as it would apply to geographic territory surrounding a port. With the development of intermodalism and load centers, perhaps no particular geographic point is always tributary to a [particular port]. . . ." 224 Perhaps the idea that cargo considered geographically "naturally tributary" coupled with Commission involvement which had arisen from the practice of equalization had been rendered obsolete.

The limitation placed upon the right of a port was explicitly restricted to cargo that was geographically tributary to a port and not to commodities which might be tied to a port for which they were best suited. 225 The Commission found Dart wholly reaffirmed according to these standards—the equalization practice which was struck down was based on a targeted commodity over which the doctrine of captive cargo might retain validity. In addition, the issue of discrimination between shippers, and not ports, was at issue in Dart, thus distinguishing it from the present case. The Commission held that "application of the Dart rationale to this record must therefore lead to a result preserving PWC's practices". 226

The decisions in Pacific Westbound Conference—Equalization Rules and Practices and Dart warrant comparison as each was a "vehicle" for the application of CONASA guidelines. The Administrative Law Judge in each case reached the same conclusion and upheld the practice that was at issue.

In Dart, unmanufactured tobacco had historically flowed to both of the competing ports, seemingly without preference, whereas in PWC, many of the shippers had actually favored Seattle over Portland. The approaches in each case varied significantly when it came to considering the influence or importance of "relevant inland transportation rates". It

222. This was stated in unequivocal terms, "We reiterate now that Section 8 will not be the basis for Commission investigations of carrier equalization practices." Id.
223. Id.
224. Id. at 962. The Commission recognized that the concept of load centers was controversial and still developing. Its statement that Seattle had no legal right to become a load center and that Portland had a right to have a fair opportunity to compete was strangely reminiscent of its edict in Intermodal Service to Portland that Portland should have the opportunity to develop, as had Seattle, into a load center. This concern spawned, as noted earlier, a questionable decision.
225. Id. at 962.
226. Id.
was clear in \textit{PWC} that inland motor carrier rates alone favored Portland. However, other factors favored Seattle and subsequently tipped the balance in its favor. Seattle had closer proximity to foreign destinations, had more numerous transportation options and liner service and offered other advantages that were a direct result of Seattle’s emergence as a “load center”. The inland rate differential was merely one of the elements that was considered by the judge for it was freely admitted that “obviously inland motor carrier rates favor . . . [the Port of Portland] . . . or there would [not] have been [any] equalization or absorption.” In both of the \textit{Dart} cases however, inland rates became the focal point of the decisions, as the exact rates and mileage from the major tobacco markets to both ports were examined. This analysis was performed despite the fact that mileage was not necessarily determinative of rates. Coupled with this was the fact that carriage of the commodity was unregulated by the ICC and rates were therefore matters that were determined through private negotiation between private entities. Thus, rates were not subject to verification by anyone.

The Commission in \textit{Dart}, as in \textit{PWC}, further “assumed that there is a consistent inland cost differential favoring Wilmington,” and that if this was not the situation, shippers would have sent their cargo directly to Norfolk. In \textit{PWC} this fact was balanced by the other advantages that Seattle had to offer over Portland. In \textit{Dart} the Commission found that because “the very nature of Dart’s intermodal service depends upon . . . some unmanufactured tobacco . . . naturally moving to Wilmington”,\textsuperscript{227} the cargo was therefore assured to be naturally tributary to that port. The majority in \textit{Dart} failed to consider the benefits afforded shippers through the use of an alternate gateway (offering the advantages associated with the greater level of activity in Norfolk) or the benefits accruing to steamship lines from their ability to focus their activities to a single port and to thus avoid costly ship calls. The majority in \textit{Dart} recognized Dart’s strategy as that of concentrating its service in Norfolk (or expanding the reach of its Norfolk call) and as being based upon artificial inducements rather than upon productivity. Similar means and ends in \textit{PWC}, with steamship lines funnelling cargo into Seattle, was seen in a more favorable light.

In other words, different tests were applied—a more restrictive, port protective stance was taken in \textit{Dart}, whereas a more liberal, broader standard was applied in \textit{PWC}. Only the later decision seems to be in accord with both the literal \textit{CONASA} guidelines and the intent behind them. That a factual difference may account for part of the discrepancy is indeed arguable: in \textit{Dart} cargo was induced into the port of Wilmington for transshipment to Norfolk while in \textit{PWC} cargo from inland origins (and

\textsuperscript{227} 19 SRR 521, 525 (F.M.C. 1979).
at rates that were favorable to Portland) was routed directly to Seattle. Nevertheless, the failure of the Commission to apply a balancing test to this cargo that it had found to be local to Wilmington indicates that CONASA guidelines were not followed.

As precedent, it is important to note what the Commission’s decision in Pacific Westbound Conference—Equalization and Absorption Practices represents and what it does not represent. The Commission asserted that based on the record before it, it was unable to conclude that ports, as a statutorily protected class, did not have a “natural right” to certain cargo. Therefore the Commission could not label equalization practices as per se lawful. The Commission’s use of equivocal language when it (apparently) discarded the concept of geographically naturally tributary cargo left further room for doubt as to the doctrine’s demise.

The sole exception regarding Commission application of the concept of the right of a port to cargo centers around the idea that certain commodities may somehow be tied to a particular port best suited to meet its needs. Thus a distinction was drawn between geographically and commodity based captiveness, a distinction which was without precedent. It is certainly true that throughout the history of port discrimination, aggrieved ports had been unsuccessful in delineating any firm geographical areas exclusive to them. The Commission had been equally unsuccessful in providing guidance228 and while examining such ill-fated attempts, the Commission developed guidelines in CONASA which were based more on transportation policy than upon strict geographical parameters. Therefore, Commission elimination of such futile and resource-wasting attempts could correctly be viewed as an exercise in “enlightened regulation.”229

There was not a valid reason for retaining a doctrine based upon tying a particular commodity to a particular port. While a commodity may best be suited to a particular port, the entire basis for intermodality (and the circumstances that made the concept of captive cargo obsolete) was based on the standardization or uniformity provided through containerization and the resulting flexibility provided in the handling of cargo. In other words, while cargo may best be suited to a particular port, this is simply one of a number of factors that shippers must consider and which should be balanced against or which should override other advantages such as a tie-in arrangement. Commission investigations of practices singling out

228. As Commissioner Patterson noted in Reduced Rates on Machinery-Atlantic to P.R. Ports, 7 SRR 233, 259 (F.M.C. 1966), “[W]e should consider ourselves totally ill-equipped to draw the necessary lines on a map to fix places where any law of nature implied by naturally tributary characteristics dictates shipments should not be diverted from one port or carrier rather than another...” That such delineation is incapable of demonstration is the basis for the weakness of the entire concept of naturally tributary cargo.

commodities for equalization, *Proportional Commodity Rates on Cigarettes and Tobacco* and *Dart* have ultimately focused not on the specific characteristics of the commodity, but rather the area from which it originated.

Cited in support of the concept of commodity-based exclusivity was the case of *Intermodal Service to Portland, Oregon*. *Intermodal Service* stood for the proposition that, despite the flexibility afforded by containerization, cargo could still be considered naturally tributary or local to a given port. Thus a distinction was not made as to commodity versus geographical characteristics. At best, retention of the concept of commodity-based naturally tributary cargo is itself a return to the arduous examinations surrounding the adequacy of service for specific commodities, a task the Commission appeared ready to avoid.

If the consideration and disposal of the issue of naturally tributary cargo by the Commission is somewhat less than conclusive or satisfying, then its rationalization of *Dart* appears to be even less adequate. "The decision in *Dart* was well within the principles of CONASA, for the backhauling of cargo to Norfolk was operationally and economically inefficient and the equalization was targeted to a specific commodity. Questions were raised regarding unjust discrimination between shippers, an issue that was apart from that [of unjust discrimination] between ports." Preservation of *Dart* in light of the principles enunciated in *PWC* is misguided. As noted earlier, the decision in *Dart* centered around the conclusion that cargo induced into Wilmington for transshipment to Norfolk essentially became geographically naturally tributary or local to Wilmington and its subsequent transshipment was thus unlawful. Economic efficiency was not the primary issue and, although operational inefficiency was never proven by the Commission, the burden of proof regarding the demonstration of operational efficiency was incorrectly placed on the shoulders of *Dart*. The issue of possible discrimination among shippers was a secondary issue at best.

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230. 1 SRR 145 (F.M.C. 1960). In *Proportional Rates*, in the infancy of containerization, respondent steamship line offered service from New York to Puerto Rico, offering so-called "proportional rates" on shipments originating at various Virginia and North Carolina cities. See text accompanying note 53 *supra* for definition of proportional rates. Baltimore's contention that the reduced rates would divert traffic normally following through the port and were, thus, unlawful, was accepted by the Shipping Board, which stressed the inadequacy of the justification offered by the line in support of the practice. Quoted in support was the *City of Mobile* passage that "territorial regions and zones tributary to ports" were statutorily required to be recognized. *Id.* at note 152 (emphasis supplied). The characteristics of the commodity tying them to any of the ports was not an issue.

231. 22 SRR at 962 (F.M.C. 1984).

232. 19 SRR at 526 (F.M.C. 1979).
IX. NATURELLY TRIBUTARY CARGO—REGULATORY REMNANTS AND ALTERNATIVES

Based on the Commission’s latest pronouncement in PWC, it is questionable whether the doctrine of naturally tributary cargo retains any viability at all. There are many obvious reasons why it should not, with the foremost one being that, despite tortuously long proceedings, neither the aggrieved ports, the carriers, nor the Federal Maritime Commission have been able to label cargo in a definitive manner or suggest standards that would provide any degree of guidance regarding the parameters of lawful practice. The first tier of CONASA standards, that of the threshold determination of the status of diverted cargo, can justifiably be disregarded. Perhaps it would be equally justifiable to disregard the second tier of CONASA, that of the reasonableness of carrier practices retaining some validity as a standard for unlawfulness. It is noteworthy that in the Initial Decisions in both Dart and PWC, the reasonableness of carriers’ practices were examined in depth despite the fact that the threshold test was not met (i.e., the cargo diverted was not found to be naturally tributary to the complainant ports). It is at least arguable that the reasonableness of the practice alone was the determining factor regarding the unlawfulness of the practices. The question therefore becomes one of policy; is there some point at which the rights of carriers frantically funneling cargo by whatever means, at various rate levels into larger and larger ships and load centers must bow to the greater public interest encompassing a port and its community? This must be considered in light of the substantial powers which have been given to steamship lines (both individually and collectively), under the Shipping Act, and which can damage ports. Despite the benefits that have accrued from competition, innovation, and from the weakening of port rights that has been precipitated, there is still an ever-present danger surrounding the control of the shipping outlets for this nation’s commerce solely by commercial interests.

Perhaps a balancing test could be utilized where the benefits of the practice or ratemaking device accruing to the shipper (and the need for its utilization by the steamship line) would be weighed against the possible detriment to the complaining port and the surrounding community. Focus should be placed on both the short and the long-term effects of the practice. Positive short term effects surrounding the application of cargo routing should be weighed against the long term instability that may be created throughout the port industry. Cargo routing may render as useless new debt-financed facilities and may necessitate a change of the basic port-carrier relationship from one of a casual commitment to that of a greater commitment (i.e., along the lines of airport-airline bond guarantees). It is policy issues such as this that make consideration of the issue more appropriate for rulemaking and less likely for any satisfactory reso-
lution. Adjudication has already helped to develop guidelines of an ambiguous nature (as was illustrated in PWC) and may return the Commission to its past role as arbiter in massive proceedings.

The most promising approach would combine a Commission rulemaking/balancing test which would utilize, (along with factors previously applied in Section 16, First inquiries),233 the following: trigger events such as intermodal rates which are set suspiciously low from targeted points; higher rates from the hinterland of other ports subsidizing them; the use of independent action so as to discriminate against the shippers of a particular port or equalization practices that subsidize the cost of inland transportation beyond a reasonable distance. The latter standard is especially appropriate for it balances the reasonable expectation of a port to be able to compete for cargo with that of the commercial decision of steamship lines to build larger ships and to concentrate service. Thus, the diversion of cargo closely tied to a port would be a factor to be considered but would not be an overriding one and would not be a “trigger” event.

However, The Shipping Act of 1984 may sporadically change the shipper/carer/port relationship so as to obviate the need to develop port-protection standards, notwithstanding the protected status of ports under it.

X. THE SHIPPING ACT OF 1984—A THREAT TO PORTS

On March 20, 1984,234 President Reagan signed into law the Shipping Act of 1984,235 thus culminating nearly seven years of Congressional and maritime industry effort to supplant the venerable Shipping Act, 1916. Technological development and the evolution of intermodalism in the intervening sixty-eight years had rendered the 1916 Act obsolete by mandating a growing need for both cooperation and a more flexible relationship both among steamship lines and shippers. The declared purposes of the Shipping Act are three fold: (1) to establish a non-

233. Section 16, First standards have permitted introduction of factors to justify disparate treatment, such as “volume of traffic, competition, distance, advantages of location, character of traffic, frequency of service, . . . . Surcharge on Shipments from Buffalo, 2 SRR 111, 114-15 (F.M.C. 1962). For a more recent application of Section 16, First, see Cargill v. Waterman, 21 SRR 287 (F.M.C. 1981).
discriminatory regulatory process. . . with a minimum of government intervention and regulatory costs. (2) to provide an efficient and economical transportation system in the ocean commerce of the United States; (3) to encourage development of [a] U.S. flag liner fleet capable of meeting national security needs.\textsuperscript{236} From a practical standpoint, the primary thrusts of the Act are to reestablish the primacy of the Federal Maritime Commission regulation of ocean transportation while at the same time reducing that role.\textsuperscript{237} The Shipping Act of 1984 produced "a watershed in the evolution of U.S. regulatory shipping policy aimed at reducing excessive, parochial, and protectionist" government regulation.\textsuperscript{238} The Act reflects the Reagan Administration position that "[t]his should not be the responsibility of the Federal Maritime Commission to determine what industry practices might best achieve the efficiencies required the marketplace".\textsuperscript{239} The Act further reflects the carefully balanced interests of two elements of the particular marketplace (steamship lines and shippers), both of which compromised their positions so as to give added flexibility and protection to one another.\textsuperscript{240}

One analyst has stated that under the new Shipping Act, the parameters of permissible conduct merely reiterate the abstract concepts of unjust, unfair, unreasonable, undue preferences or advantages, or prejudice

\begin{itemize}
\item \textsuperscript{236} 46 U.S.C. Appx. §§ 1701-1720 (1985).
\item \textsuperscript{238} This evaluation was made by Conrad Everhard, president of Dart Containerline, a foreign flag carrier. Armbruster, Johns and Everhard Welcome Shipping Act, J. COM., Mar. 22, 1984, at 12A, col. 13.
\item \textsuperscript{239} International Ocean Commerce Transportation Act: Report of Committee on Merchant Marine and Fisheries to Accompany H.R. 1878, 98th Cong., 1st Sess. at 42 at 49 (1983) (Letter to Chairman Walter B. Jones from Drew Lewis, Secretary of Transportation, dated February 5, 1982).
\item \textsuperscript{240} See Shipping Act of 1984: Conference Report on S.47, H.R. No. 600, 98th Cong., 2nd Sess. See also: Morrison, FMC Chief: Ship Act Aids Lines, Shippers, J. COM., Mar. 22, 1984, at 1A, 12A, col. 5. Whether the balance struck is precise has been subject to discussion, especially with regard to the plight of small shippers. See Armbruster, Kanuk, Carey Clash On New Shipping Act, J. COM., Mar. 27, 1984 at 1A, col. 5. See Sher and DeVierno, supra note 235 at 22.
\end{itemize}
or disadvantage of the 1916 Act,\textsuperscript{241} while others have declared that the Act has had little significant impact on the port industry. "[A]s the thrust of the Act was to address carrier and shipper issues,\textsuperscript{242} the increased freedom given [to] steamship conferences [with respect to their] decision-making and operation, [coupled] with freedom from the threat of antitrust laws and much burdensome regulation may have [had a] direct impact on the now-diminished . . . right[s] of a port to exclusive hinterland.

The impact of the Shipping Act of 1984 may be viewed as five fold: one, the increased ability of conferences to coordinate service; two, a decreased opportunity to prevent implementation of potentially damaging agreements; three, sanction of conference intermodal authority; four, sanction of service contracts between carrier and shipper; and finally, the clear intent of Congress as is reflected in the legislation overall and its legislative history in providing steamship lines with significantly less restrained operating flexibility.

A primary purpose of the Shipping Act of 1984 is to provide a legislative vehicle for cutting the costs of carriers, and consumers by encouraging higher utilization of vessels. Greater carrier cooperation and even integration of operation, including the formation of joint ventures, the chartering of space on a competitor’s vessels, and the pooling of cargo or revenue are all protected by the Shipping Act. These practices fall within the “rationalization”\textsuperscript{243} or within the integrated planning in the supply of vessels and equipment. Interpretation of the 1916 Act and the “public

\textsuperscript{241} See Bakke, The Shipping Act of 1984, supra note 237 at 13. These adjectives represent, of course, the thrust for Sections 16 and 17 of the Shipping Act, 1916. See note 60 supra, and accompanying text (excerpts from Sections 16 and 17).

\textsuperscript{242} Sher and DeVierno, supra note 237 at 20. The interpretation that the “Shipping Act of 1982” the predecessor “maritime reform legislation” to the Shipping Act of 1984, and of similar at least in thrust, strengthened steamship conference power at the expense of ports was made more evident by The National Institute of Economics and Law in its Analysis: Potential Effects of the “Shipping Act of 1982” on American Port Cities (August 1982). This view was disputed, however, by a port official, who labeled the paper’s authors “well meaning overly credentialed academics with no port industry experience.” Ship Reform Critics Draw Baltimore Fire, J. Com. Aug. 25, 1982 at 1B, col. 3 (quoting Richard A. Lidinsky, Jr., Maryland Port Administration).

In fact, since passage of the Act, there has been a definite movement toward rationalization of services of steamship lines. See ‘Consortium Fever’ Sweeps Container Shipping Industry Worldwide, J. Com., June 24, 1985 at BC, col. 1.

\textsuperscript{243} Ellsworth, Competition or Rationalization in the Liner Industry?, 10 J. MAR. L. & COM. 497, 498 (1979). For an example of a revenue sharing “rationalization” agreement among North Atlantic steamship lines, along with an examination of the concerns of ports and other controversial issues, see Agreement No. 10,000—North Atlantic Pool, 14 SRR 267 (F.M.C. 1973). See also Pacific Coast European Conference—Tariff Rules, 12 SRR 405 (F.M.C. 1971). Conference rules limited the number of terminals in San Francisco Bay area ports that its members could call on, together with implementing an equalization system between those ports.

See also, Frank, “If you can’t beat them . . .,” Forbes 36, 37 (April 23, 1984) (new Act may lead to steamship consortia and superports).
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interest" standard by which rationalization agreements have been judged in the past are believed to have discouraged\(^{244}\) the development of schemes to coordinate sailing schedules, while at the same time they have controlled capacity, thus eliminating wasteful service competition, and have increased vessel utilization.

Such rationalization may have the potential for the collective assigning to or allotting of ports to specific conference carriers. Ports may lose steamship service not because of the competitive factors of the marketplace, the incentives each port provides or because of the advantages they possess but rather service would be lost based upon the decisions of steamship conferences. Rationalization itself may relegate a port to "feeder" status or may significantly alter its level of service and thus its place in "port rotation" schedules.

The second danger facing the port's is the new, more liberal standard in which situations such as those described above will be judged. Replacing the Svenska "public interest" test that had been widely criticized\(^{245}\) because of the uncertainty of its application and its vagueness is a "general standard" of the new Act which gives presumptive validity to agreements not facially in violation of a list of specific prohibitions. This new standard places the burden upon the Commission\(^ {246}\) to seek an injunction to stop the implementation of an agreement if the Commission determines that such an agreement is likely, through a reduction in competition, to produce an unreasonable reduction in transportation or an unreasonable increase in transportation cost.\(^ {247}\) Clearly, with the burden of proof shifted, and with a much less onerous standard of approval, carrier agreements considered unapprovable in the past will now become facilitated and realized. The instructions given to the FMC by Congress in its Joint Explanatory Statement of the Committee on Conference\(^ {248}\) also

\(^{244}\) See supra text accompanying note 235. This was the conclusion of a study of the United States General Accounting Office conducted at the request of the House Merchant Marine and Fisheries Committee. Comptroller General, U.S. General Accounting Office, Report to the Chairman, Committee on Merchant Marine and Fisheries U.S. House of Representatives Changes in Federal Maritime Regulation Can Increase Efficiency and Reduce Costs in the Ocean Liner Shipping Industry, 50, Appendix II (July 2, 1982). This view was dismissed by the Federal Maritime Commission as inaccurate, that it had approved 20 joint service agreements and over a dozen space charter agreements as well as pooling agreements and those providing for the establishment of consortia. Id. at 40, Appendix II. (Letter of January 22, 1982, from Alan Green, Jr., Chairman, Federal Maritime Commission, to Henry Eschwege, General Accounting Office).


\(^{246}\) 46 U.S.C. Appx. § 1705, g (1985).

\(^{247}\) Id.

made it clear that the new standards are to be applied narrowly so as to not contradict the thrust of the Act in facilitating carrier flexibility. "Reasonableness" is to be understood in a commercial context. The reasonableness will be judged as based upon the change in services provided to shippers which is likely to arise from the agreement; that such change is meaningful and material, and that such change cannot in and of itself be determined to be a per se "impermissible result." 249

A second aspect of the unreasonableness requirement is that the negative impact upon shippers may be offset by the benefits of an agreement, including in specific "any efficiency-creating aspect of an agreement. Congress intends that carrier integration and rationalization are to be considered favorably by the Commission and the courts, [with] the intent being that ocean carriers be free to structure their own affairs..." 250

The third provision of the Shipping Act of 1984 with the potential for an impact upon ports is the grant of intermodal ratemaking authority to steamship conferences. As has been previously noted, such intermodal ratemaking transfers "port of delivery options from the shipper/consignee to the steamship line." "[C]argo is made port blind, [and] ocean carriers [are] given [the] freedom to choose and [to] utilize the port most cost effective to them." 251 While individual lines already possessed such power, the exercise of it independently, outside of collective tariffs, had threatened the very existence of the conference structure. 252 Utilized collectively within the more stable environment of that structure, such authority may serve as the prerequisite for load centering by individual lines and may assist the implementation of rationalization schemes by the conference itself.

The potential for both restraint and the predatory exercise of intermodal ratemaking by the conferences was considered so great that guidelines were considered which were not unlike those developed in CONASA. 253 The recent grant of authority prior to the effectiveness of the

249. Id. at 35; See note 90 supra and accompanying text for analogy of shipping to antitrust laws and "per se" illegality.
250. Id. at 36.
253. The guidelines were announced in U.S. Atlantic & Gulf/Australia-New Zealand Conference (Agreement No. 6200-20—Intermodal Authority) 21 SRR 89 (F.M.C. 1981). As specified in the decision, carriers proponents of conference intermodal would have to demonstrate "the intermodal cargo to be carried would naturally and efficiently move through the ports already served by the conference or rate making group; operational economies and improvements would result; there is a significant shipper demand for the intermodal service being proposed; a more frequent and reliable service would be offered to a broad range of service points; regular
Shipping Act of 1984 to seven North Atlantic-Europe conferences was most likely "the largest single grant of such operational authority ever cleared by the Federal Maritime Commission" and was hailed as "... [one of] the most important decision[s] they've ever made." A port organization representing the North Atlantic range was unable to reach a consensus position supporting Commission approval. A "definite bloc of concern" developed among the members that such authority would facilitate load centering. Three member ports filed separate comments expressing their concern with the FMC-sanction of cargo diversion and this sentiment was later echoed by a port representative of New York in that "It [the authority] could have a great effect on ports because for the first time it could create load centers, [thus] making it difficult to determine whether [such authority] is a blessing [or a curse]."

In its Order of Approval, the Commission acknowledged these fears, stating that such trends may be inevitable in the evolution of modern intermodal transportation systems, but that appropriate remedies were available under the Shipping Act for unreasonable diversion.

service would be available for a broad range of commodities and not just selected high-rated items; commercially attractive rates would be assessed for the proposed intermodal service; and there is relevant competition for the cargo the rate making group proposes to carry. Finally, the member lines should provide sufficient evidence concerning the competitive environment in which they would operate to satisfy the Commission that there is an absence of predatory intent on the part of the conference seeking the authority." id. at 92.
256. North Atlantic Ports Split on Intermodal Proposal, J. Com., Aug. 26, 1983, at 1A, col. 5. A "definite bloc of concern" arose among Philadelphia, Hampton Roads, and Boston port interests on The Traffic Board of the North Atlantic Ports Association. In individual comments subsequently filed, none of the ports opposed the grant of authority, not wishing "to restrict the employment of intermodalism or to impede the furtherance of other technological industry advancement!"—In Re FMC Agreements 9214-31, 7100-27, 7670-23, 7700-24, 8210-47, 5850-39, 9982-18, Comments of Massachusetts Port Authority at 3. See also comments of Virginia Port Authority and Philadelphia Port Corporation. id.
258. The Virginia Port Authority later asked the U.S. Court of Appeals for the District of Columbia to set aside the FMC's final order of December 9, 1983, granting the seven north atlantic conferences intermodal authority. Virginia Port Authority and Virginia Int'l Terminals, Inc. v. F.M.C., appeal docketed, No. 84-1040 (D.C. Cir. 1984). The appeal was made in response to Conference decision to raise the intermodal rates based on that authority, a decision that the VPA said would divert cargo to South Atlantic ports. See Port Authority Appeals Order on Tariffs, The Virginian Pilot, Feb. 18, 1984. The appeal was subsequently dropped after VPA officials met with the Conference officials in London to express their concerns directly. VPA Drops Lawsuit Against Conferences, J. Com., Feb. 23, 1984, at 1B, col. 1. The court held that the FMC did have authority and jurisdiction under Section 15 to accept and approve conference intermodal rates. Judge Wald, while concurring in the result, felt "the question of the scope of Section 15 a
A fourth concern regarding the impact of the new Shipping Act upon ports is the sanction of service contracts between steamship lines and shippers. Such contracts may, by their nature, be discriminatory by offering service and rate commitments to shippers based on volume commitments. An agreement to utilize a particular port can also be a part of such an agreement and, because it is not defined by the Act as an essential term required to be filed with the Commission, it may remain private to the parties and undiscoverable to competing ports.259

Finally, as was noted earlier, while the Shipping Act contains the same prohibitions against unjust discrimination and undue or unreasonable preference as did its predecessor, such provisions must now be interpreted and applied within the context of the entire Act. Since the overriding concern of the present Act seeks to provide carriers with a less intrusive or burdensome regulatory environment within which to operate, the terms "unjust" and "unreasonable" may now present radically different thresholds than before.

XI. LOAD CENTERS TODAY

The scope of the debate in the maritime community concerning load centers has perhaps only been rivaled by the past controversy that surrounded the protection of naturally tributary cargo. Thus, controversy ushers in the new dawn of the Shipping Act.260 For some the load center concept is neither new or inevitable.261 Others feel certain that smaller ports will survive and cite a number of reasons for this belief:262 because
difficult one, . . . [t]oo important to be finally decided . . . on the puny record provided by the Commission." Id. at 900. The decision was subsequently accepted for en banc review and vacated as to the issue of Commission jurisdiction but rendered moot by expiration of conference intermodal authority by terms of the Agreement. See United States v. Federal Maritime Commission, 694 F.2d 793 (D.C. Cir. 1982).

259. 46 U.S.C. app. § 1707(c)(1) (1985). 'Shippers in Driver's Seat' As Huge Containerships, Load Centers Proliferate, J. Com., March 11, 1985 at 13c, col. 5 (quoting Rex Sherman, American Association of Port Authorities, "As long as we have an imbalance of supply [of cargo space, (it is doubtful)] there will be a surge toward load centering.")


261. See Load Center Problems Cited at AAPA Meeting September 26, 1984, at 1, col. 2. (AAPA is the American Association of Port Authorities.); but see A Super Port for Containers, supra note 260 (an anonymous steamship executive noted the concept had been around a very long time, but "[t]here will be no mad rush by steamship lines to set up operations at just a few ports. It's just against human nature.").

262. Will Load Center Ports Crush Competitors?, supra note 260 (quoting M. Fred Whelan, director of trade development for the Jacksonville Port Authority). But see Intermodal Service to Portland, Oregon, 12 SRR 601, 618-19 (F.M.C. 1971) (adequate service to Portland a factor in its
'ships follow cargo'; that larger ports can easily become complacent, inefficient, and expensive; because some ports could become load centers for some lines and feeder ports for others, and finally, because smaller ports will more readily specialize, diversify, and adapt themselves thus attracting lines with the increased negotiating power that they will have.

Debate notwithstanding, load centers have emerged and are here to stay. An example is Philadelphia which has attracted carriers through its central location between New York and Baltimore. This location, historically viewed as a disadvantage is now seen as a distinct advantage as lines further restrict direct calls. Additional evidence is provided by the fact that three steamship lines have recently selected the port as a load center. The port further serves as a load center in conjunction with Boston for a fourth line that purposely bypasses New York and the competition of giant containerships.

The new generation of super containerships are also being placed in service. Atlantic Container Lines recently introduced the largest and most

potential development "to extent cargo follows ships"). Generally intermodal rates give shipper less choice in cargo routing so that cargo can be "pulled" into a given port. See generally United States Ports Vie For Load Center Status, J. Com, December 10, 1984 at 1c, col. 5.

263. A Super Port for Containers, supra note 260, at 56. In December, 1976, the U.S. Maritime Administration released an extensive study it had prepared jointly with U.S. flag carrier Seal Land Service on a waterborne system for feeding cargo to load centers for international shipments. Three combinations of ports were chosen as having "relatively high international market potential." New York would serve as a load center for Boston, Philadelphia and Baltimore; Norfolk for Wilmington, Charleston, Savannah and Jacksonville; and New Orleans for Tampa and Mobile. Despite shipper bias in favor of direct call over the proposed relay system and competition from inland modes, the system was projected as economically feasible.

At the time of the study, there existed an uncertainty as to which agency, (the Federal Maritime or the Interstate Commerce Commission), could or would assert jurisdiction over the waterborne system, and a "substantial" regulatory impediment as to rail and truck alternatives (specifically, but not explicitly mentioned, the use of microbridge tariffs) Mar. Admin., U.S. Dept. of Com. Development of a Domestic Waterborne Feeder System, Final Report (December 1976).

264. "...[S]ome carriers like to go to smaller ports where they gain increased negotiating power by being a big fish in a little pond" (quoting Richard P. Leach, manager, Port of Houston) Will "Load Centers" Crush Competitors?, supra note 260. See also Shipping Industry Mulls "Load Center" Conception, supra note 261 (smaller West Gulf ports protect themselves from the advent of load centers by diversifying); Law, Economic Changes "Threaten" Small Ports, J. Com., May 19, 1983, at 24B, col. 1 (smaller ports urged to specialize and attract cargo best suited for the individual port).


266. See N. Atlantic Service Set For Launch, J. Com., Apr. 18, 1984, at 1A, col. 2 (BCR-Lines offers direct Boston sailings to Europe); Philadelphia Marks Debut of New Ocean Carrier, id., at 1B, col. 5.
technologically advanced cargo ship ever built for the North Atlantic Trade, \(^{267}\) with a capacity of 2,130 20 foot containers and some 600 automobiles. United States Lines has introduced the first of its 4,218 20 foot container "econ" ships which provide around the world service. \(^{268}\) With the first of these giant ships, United States Lines will establish load centers in New York and Savannah. The impact upon Savannah demonstrates the significance. \(^{269}\) The direct impact will amount to $40 million annually, with the indirect impact estimated at $100 million annually. In 1986 more than 200 U.S. Lines' vessels are expected to call on the port of Savannah, picking up and discharging 15,000 40 foot containers weekly. Cargo volume through the use of 150,000 to 175,000 containers may be in the 1.25 to 1.5 million ton range. The advent of super-sized vessels is already creating complications. The vessels' deeper drafts ride closer to the bottom of the ocean floor thus causing vibration and turning difficulties when moving through such premier ports as New York and Baltimore. \(^{270}\) The age of the supership and the load center had indeed arrived.

XII. RAILROADS AND INLAND PORTS

The development of load centers is based on a foundation greater than simply ocean transportation and has consequences extending deeply inland from shore side. Railroads have been called the key to load centers, \(^{271}\) for the ability of steamship lines to gather cargo from distances far beyond the hinterland of its chosen port is dependent on advantageous inland rates. Inland carriers may be encouraged to provide such rates too, benefitting from the control of routing by its steamship "intermodal" partner by a greater likelihood of backhaul cargo, keeping its own costs down. \(^{272}\) It is thought by some that regional monopolies in the form of big railroads and big motor carriers may lead to decreased rail/motor service generally, altering transportation patterns and freezing

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\(^{268}\) Third Generation Ships, supra note 267.

\(^{269}\) USL to Give Savannah A Boost, J. Com., Apr. 16, 1984, at 24B, col. 3; see also Port Gets $40 Million Boost, Savannah Evening Press, Apr. 6, 1984.

\(^{270}\) Bigger Ships Highlight Channel Dept Problem, J. Com., Apr. 6, 1984, at 1B, col. 3 (In New York, for example, a strong wind combined with tides can reduce channel depth by four-five feet); see also United States Lines Leaning Toward Port of Savannah, J. Com., Apr. 2, 1984, at 1B, col. 5 (a selling point of Savannah was pledge of pilots to handle superships of carriers at any time); see supra note 10.

\(^{271}\) See Will Load Centers Crush Competitors, supra note 260.

\(^{272}\) See Law, Economic Changes. . ., supra note 264.
out marginal or smaller ports.273 Ocean carriers may greater utilize unit trains to feed cargo into load center ports, justifying the development by railroads of hub terminals and some rail carriers may spend heavily in developing their own load centers over the next five years to match those of shiplines.274

Ports, warned that foreign oceanborne commerce can and will migrate literally overnight275 "and that clearly carriers and shippers each possess trump cards in the determination of that gateway," have reached further inland, like steamship lines, to gain control of cargo. The most noticeable "device" to do so has been the "inland terminal,"276 primarily designed to entice cargo through their "ocean" terminals by lowering shippers' inland transportation costs. They eliminate for shippers the expense of costly empty container shipments and provide mainland site for marshalling, stuffing, and stripping of containers. Charleston's inland center at Greer, South Carolina allows that "port" to become the second closest Atlantic port to the Midwest industrial hinterland.277 North Carolina's inland port at Charlotte is closer to the entire states of Tennessee and Kentucky than any other "port."278 Atlanta has been suggested as an ideal link with Savannah, and Jacksonville is considering extending the port to that city as well in what may be the first inland terminal developed across state lines.279 The entire basis for the inland terminal or port concept is that "the port that can produce the most tonnage for the ocean carriers will be "relieved of the jeopardy of being rationalized," "cut out by steamship lines from direct service." The concept is that of becoming the "load center of a load center."280

Competition between ports may lay the foundation for them ex-

273. See A Super Port for Containers, supra note 260, at 58.
274. See Shipping Industry Mulls Load Center Concept, supra note 260.
275. Intermodal Carriers "Urged" To Cooperate, J. Com., Apr. 12, 1984, at 1B, col. 3 (port costs, stevedoring costs, interface costs, rail and truck linehaul costs will all enter into gateway collection by ocean carrier).
276. Such facilities have been built contiguous to rail ramps, (South Carolina) or use existing rail terminals, (North Carolina) and serve to eliminate for shippers the expense of empty container shipments. Empty containers are held at the terminals until needed for shipments in the reverse directions. See IS GPA-Owned Terminal in Atlanta Needed?, J. Com., Apr. 18, 1984, at 3B, col. 5.
278. State's First Inland Port to Open Monday at Charlotte, The Virginian-Pilot, Jan. 1, 1984.
279. See IS GPA Owned Terminal in Atlanta Needed?, supra note 276.
280. See supra note 277 (quoting W. Don Welch, Executive Director, South Carolina State Ports Authority).
panding into non-vessel common carrier operators and trucking as well as inland terminal operations.\textsuperscript{281} The New Orleans Traffic and Transportation Bureau, in conjunction with the port of New Orleans, has recently become a shippers' agent,\textsuperscript{282} contracting with railroads for volume movements and corresponding rate discounts.\textsuperscript{283} The ports of Los Angeles and Long Beach have jointly developed a huge intermodal rail facility, four to five miles from the container terminals at both ports, reducing the time and cost of trucking from railhead to terminals.\textsuperscript{284} Development of the $50-million facility has proceeded as an attempt to divert Far East cargo from Puget Sound ports as well as all-water Far East cargo from the Atlantic and Gulf coasts. Other ports are expanding into the interior and beyond with sales offices in hopes of diverting traffic from current routings.\textsuperscript{285}

XIII. CONCLUSION

It is appropriate to conclude this examination of intermodalism today with the perspective of Section 8 and the evolution of the principle of naturally tributary cargo. Section 8 arose from congestion that seized the North Atlantic port range during World War I—those ports had been developed primarily on the monopolistic powers of large railroads, funneling cargo from the interior of the country, largely to the exclusion of other ports and ranges. Section 8 instructed the Interstate Commerce Commission to take action to prevent disruption of the natural flow of cargo so that this state of paralysis would never again occur. This was interpreted by the predecessor to the Federal Maritime Commission not as simply a right of a port to cargo from areas naturally tributary thereto, but, a fundamental one, virtually unsurmountable. Rigid enforcement of the right had the unfortunate consequence of impeding innovation and sacrificing carrier interests as containerization and intermodalism revolutionized ocean transportation. Eventually, the economic pressures of change forced regulatory reconciliation of this right and those carrier needs, which diverged

\textsuperscript{281} Ship Act Seen Catalyst to Port Agression, J. Com., Mar. 30, 1984, at 1B, col. 3. (Port authorities have not abandoned traditional functions such as marketing, but expanded them). \textit{See Philadelphia Port Corp. Takes Sales Pitch West}, J. Com., Nov. 23, 1983, at 12A, col. 6.

\textsuperscript{282} Shippers agents act to consolidate the rail movements of shippers to exact volume discounts from the linehaul railroad. 49 U.S.C. § 10562(4) (1980).


\textsuperscript{284} Johnson, Ports Planning Joint Intermodal Facility, 2 CONTAINER NEWS 37 (April, 1984). \textit{Philadelphia Mulls Rail Yard Benefits}, J. Com., Sept. 21, 1984 at 24B, col. 4 (freight yard to allow easier access of unit trains to waterfront in attempt to facilitate emergence as load center).

so completely that Section 8 and the right to naturally tributary cargo would be largely discarded.

Today, load center ports, based on diverting cargo that has traditionally flowed through other ports and concentrating it, are emerging after twenty years of speculation. The lack of a guarantee to cargo, coupled with the emergence “superport” concept, may have spread apprehension through the port industry but concomitantly fostered competition and innovation. Ports, through inland terminals for example, have attempted to change and make more advantageous that which logically seems immutable—their geographic location. In developing these inland load centers, ports have also attempted to do that which they have complained about for years—encroach upon the hinterlands of other ports and disrupt traditional transportation patterns tying cargo to port. The advent of inland ports may have effectively ended the usefulness of any concept of naturally tributary cargo, if the concept retains any vitality. Given the history of port discrimination claims, it is not difficult to imagine, however,

286. Ports, of course, have sought to restrict the permissible practices of carriers beyond equalization and bridging. Most notable was the attempt of the Delaware Port Authority to keep Transamerican Trailer Transport (TTT) from merely soliciting (advertising and sales calls) cargo naturally tributary to Philadelphia for ocean transport from Baltimore and New York, the carrier’s port of call. TTT did not absorb any inland rate differential nor did it even accept the cargo for transportation other than at the two latter ports. Nevertheless, the court issued a preliminary injunction against the solicitation of cargo by TTT and its agents, citing a possibility of extensive irreparable harm if allowed to continue and a likelihood that the port would prevail before the Federal Maritime Commission. 331 F. Supp. 441 (E.D. Pa. 1971). The court, persuaded by the opinion of the FMC’s General Counsel that the case was based on a novel cause of action and should not be considered as merely another in a long line of condemned equalization cases, and also having little likelihood of success, reversed. Delaware River Port Auth. v. Transamerican Trailer Transp., Inc. (TTT), 501 F.2d 917 (3rd Cir. 1974).

The action then continued at the FMC. The Administrative Law Judge, finding that the statutes regulating shipping, did not “vest a port with monopoly over local cargo,” found that bare solicitation was not unlawful. The Commission adopted this decision, finding that “the time has long since passed for this case to be put to rest.” Delaware River Port Auth. v. TTT, 14 SRR 1468 (F.M.C. 1975).

Nevertheless, the Commission’s decision was appealed and again upheld. “[T]he position pressed upon us... is unprecedented, and amounts to a contention that common carriers cannot engage in lawful competition. ... No transportation regulatory agency has ever held that traffic solicitation of the kind involved here constitutes discrimination or the giving of an undue preference or advantage.” Delaware River Port Auth. v. TTT, 536 F.2d 319 (D.C. Cir. 1976).

Ironically, nearly a decade later, Sealand Service alleged its competitor, American Marine Lines (AML) was engaging in deceptive advertising by failing to indicate that its “service” to New York and Baltimore was not direct but rather through Philadelphia. Sealand further alleged that the service might unlawfully divert cargo naturally tributary to the ports listed in the tariff but not served directly, an argument little used by steamship lines, but rather against them and their practices. American Marine Lines Tariff, FMC-F No. 1 (January 18, 1983). The Maryland Port Administration, representing the port of Baltimore, supported the petition. Statement of Maryland Port Administration in Support of Petition of Sealand Service, Inc., American Marine Lines Co., Tariff FMC-F No. 1 (January 26, 1983). By letter dated April 8, 1983, Sealand was informed of the Commission’s denial of its petition.
a port making the novel complaint that cargo naturally tributary to its inland terminal is being unlawfully diverted to the “inland load center” of another port. 287 The primary point is that lack of a guarantee to cargo has

287. While port discrimination and cargo diversion cases have traditionally pitted port against carrier, two recent actions have involved claims by ports, and port interests, against other ports.

In the first, the Boston Shipping Association, representing steamship and stevedoring interests in that port, alleged that a provision of the so-called master contract with the International Longshoreman’s Union subjected the port to unlawful discrimination by violating Sections 15, 16, 17, and 18 of the Shipping Act, Section 8 of the Merchant Marine Act, 1920, and Section 205 of the Merchant Marine Act, 1936. At issue was Rule 10, providing that royalties collected on container movement for the benefit of longshoremen would be done at port of first unloading, in the instant case New York, and be put into the appropriate fund there for longshoremen, rather than the origin or destination port, Boston, to or from which the cargo was transshipped. Cargo diversion, alleged BSA, was the result of royalties, assessed on each ton, needed to be increased to maintain sufficient benefit funds. The Commission (and on appeal the U.S. Court of Appeals for the First Circuit) denied the claim.

The Court of Appeals found that the primary objective of the laws claimed violated was to protect the industry’s customers, not its members. The prohibition against unfair discrimination between ports was viewed as serving this objective by ensuring fair competition. In the instant case, there was no evidence that shippers were detrimentally impacted by Rule 10 or that the rule represented an artificial inducement aberration to competition of the kind proscribed in Dart Containerline v. FMC, 639 F.2d 808 (D.C. Cir. 1981). interestingly, the test applied was established in Port of New York v. A.B. Svensk Amerika Linien, 4 F.M.B. 202, 205 (1953): (1) that the complaining port and the allegedly preferred port were in competition; (2) that the discrimination complained of was the proximate cause of injury to the complaining port, and (3) that such discrimination was unreasonable. Boston Shipping Ass’n v. FMC 706 F.2d at 1240. (1983) This, of course, is the test applied in the line of port discrimination cases in which a violation of Section 8 was not alleged. See In Re Gulf/Mediterranean Port Conf. Agreement, 5 SRR 247 (F.M.C. 1964); Surcharge from Buffalo, 2 SRR 111 (F.M.C. 1962); West Indies Fruit v. Flota Merchante Gran Colombiana, 1 SRR 433 (F.M.C. 1962).

The latest port versus port controversy is one of the first impression for the Commission and one of the most interesting of cargo diversion. The South Carolina State Ports Authority filed a complaint against the Georgia Port Authority for violation of Sections 16, First, and 17 of the Shipping Act and Section 8 of the Merchant Marine. 22 SRR 1111 (F.M.C. 1984). The vehicle for such violation was a consultant’s report prepared for GPA, in essence weighing the potential of the two ports, Charleston and Savannah, as load centers. Charleston alleged that the report contained gross misstatements of fact, erroneous assumptions, and misleading representations intended to help Savannah be successfully marketed into a load center.

The Administrative Law Judge refused to grant Savannah’s motion to dismiss, unwilling to hold as a matter of law that solicitation or marketing could not be unlawful (that more than the mere solicitation sanctioned in Delaware River Port Auth. v. Transamerican Trailer Train, 501 F.2d 917 (3d Cir. 1974) could be involved or that, based on Boston Shipping Ass’n v. F.M.C., 706 F.2d 1231 (1st Cir. 1983), that a competing port did not have standing to sue another allegedly preferred port under the Shipping Act. 22 SRR at 1116-1117 (F.M.C. 1984). Interestingly also, Charleston would specifically be allowed to introduce evidence on the issue of any claimant “naturally tributary” cargo provided such evidence intended to establish a violation of Section 16, First, or 17 of the Shipping Act 1916. PWC-Equalization Rules and Practices was cited in support. 22 SRR at 1118 (F.M.C. 1984). See also Welch: No More Tears at Charleston, J. Com., Sept. 21, 1984, at 12A, col. 1 (overview by Don Welch, Executive Director, South Carolina State Ports Authority of competition among ports in South Atlantic).

Finally, in another unique action, the Port Authority of New York and New Jersey, in February, 1984, filed a complaint with the Federal Maritime Commission under the Maritime Labor
fostered creativity and hopefully will force more rational development and investment decisions.

The final point is that the load center concept may be of the same nature or evil of undue concentration of cargo that Section 8 sought to remedy. The analogy is more than clear—railroads, which were the root of the congestion in the first two decades of the century, have, through intermodalism, again assumed a pivotal status in the development of superports. Rail mergers and agreements with steamship lines may lead to a protection of interests and once again result in favored ports or load centers. Section 8 itself was a reaction to the consequences of similar concentration, allowed to reach crisis proportion. The Shipping Act of 1984, enacted to reflect the development and radically changed nature of shipping since 1916, instructs the Federal Maritime Commission for 5 years, to collect and analyze “the changes in the frequency or types of common carrier services available to specific ports or geographic regions.” Section 8 gave the original United States Shipping Board similar duties.

The circle may be complete.

Agreements Act of 1980, P.L. 96-325, 94 Stat. 1021 (1980) against the New York Shipping Association, which represented waterfront employers. The thrust of the complaint was than an agreement negotiation between the Shipping Association and the international Longshoremen’s Association, imposed a tonnage assessment on New York/New Jersey cargo to help fund longshore benefits, was unjustly discriminatory and burdened the naturally tributary cargo of the port. Port Auth. of New York v. New York Shipping Assoc., 23 SRR 21 (F.M.C. 1985).

While the parties ultimately reached agreement (1985) on a new formula, it is interesting to note that, in its decision, the Commission stated the “naturally tributary” concept seems to have little continuing validity, and the proper means of determining the lawfulness of port competitive practices in the container age is to examine whether the contested practice is directed against certain commodities or exists at the expense of economic or operational efficiencies. Id at 50.

The case was later settled upon the Georgia Ports Authority’s acknowledgment that the report contained certain errors and would no longer be distributed. See No. 84-5 South Carolina State Ports Auth. v. Georgia Ports Auth., No. 84-5 (F.M.C. 1984) (order dismissing complaint).
Pre-Trial Strategy in American Air Disaster Litigation

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I. INTRODUCTION

Regardless of where an airline disaster occurs, resulting litigation often is brought in the United States due to the attractiveness of American law.\(^1\) Contingency fee arrangements allow most everyone to gain access to the courts without financial burden, especially since the losing party is rarely forced to pay the prevailing party’s attorney’s fees. The right to jury trial and liberal criteria of what are compensable damages result in higher money awards. The American concept of product liability increases the chances that the manufacturer also will be held liable. For these reasons incidents occurring in such places as India, France, Uganda, Tenerife, Yugoslavia, Norway, and Antarctica have been litigated in America.

Like most litigation, many air disaster cases are settled before reaching trial. The amount of settlement often depends upon the forum. Thus, pre-trial strategy concerning forum selection is very important.

II. THE PLAINTIFF’S PERSPECTIVE

A. VARIATIONS IN SUBSTANTIVE LAW

When an attorney files suit, his objective is to obtain the maximum recovery for his client. In order to achieve that goal, he must carefully research the available forums for available theories of liability and the quantum and basis of damages recoverable.

1. BASIS OF LIABILITY

Each of the United States has its own common law which may or may not agree with that of other states. Different standards of care are applied among the states in regard to the duty of a pilot.\(^2\) Most states apply a

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2. In Alabama a pilot is charged with that knowledge which, in the exercise of the highest degree of care, he should have known. Todd v. United States, 384 F. Supp. 1284 (M.D. Fla. 1974). However, under North Carolina law, in the absence of statute, only ordinary rules of
highest degree of care standard to the airline as a common carrier.

The use of statutes in establishing liability also varies dramatically. In Alabama\(^3\) and California\(^4\) violation of a Federal Aviation Regulation amounts to negligence \textit{per se} where it proximately causes the injury. Violation of such a regulation in Ohio may, under appropriate circumstances, be negligence \textit{per se},\(^5\) but Missouri considers this violation only as evidence of negligence and proximate causation.\(^6\)

In products liability actions against the manufacturer, California applies a standard whereby one need only show that the product was defective, and that it caused injury to the plaintiff.\(^7\) Other states require some showing that the product was unreasonably dangerous due to defective design, mismanufacture, or failure to warn.

2. \textit{DAMAGES}

The availability of punitive damages is important to plaintiffs. The litigation from the 1979 crash of a DC-10 near Chicago\(^8\) shows the marked difference among forums in the availability of punitive damages in wrongful death actions.\(^9\) In the case of the 1979 Chicago crash, New York law was found to be controlling against American Airlines since it was then the airline's principal place of business.


5. Todd, 384 F. Supp. at 1294.


contract actions for defective products. This would bar punitive damages from implied or express warranty claims, but not from actions in tort arising from injury by a defective product.

The quantum of punitive damages available is another consideration. Some states require that a reasonable relationship exist between the award of punitive damages and the amount of actual damages sustained by plaintiff, while others hold that there need be no such relationship.

The basis of compensatory damages recoverable under the state wrongful death statutes varies. Under Nebraska law, the measure of damages recoverable is generally limited to pecuniary loss sustained by the statutory beneficiaries. Damages for pain, anguish, loss of society and companionship are not recoverable under this statute. Many states, however, would allow recovery for such non-pecuniary injuries. The calculation of lost future earnings depends on many factors such as present value, inflation and income tax obligations. The states take several different approaches. Pre-judgment interest can sizably increase the amount of the award, especially where the case continues for several years. Many states allow interest to be awarded from the time of death to the date of the judgment, but a few, such as Montana, forbid such a practice.

B. PROCEDURAL AND PRACTICAL CONSIDERATIONS

Choice of forum is also important under circumstances unique to a

15. Wright v. Hoover, 329 F.2d 72 (8th Cir. 1969).
16. Id. at 74.
particular suit. If the case was not received shortly after the accident, the statute of limitations may be a concern.\textsuperscript{20} Breach of warranty actions usually have a four year statute of limitations.\textsuperscript{21} Obtaining jurisdiction over the defendants is not usually a problem, but the plaintiff may want a forum where he can join all of the possible defendants.

Standing to sue may be of concern. \textit{Piper Aircraft Co. v. Reyno},\textsuperscript{22} illustrates this in an international sense. California, as most states, allows an estate to be set up in that state to allow a wrongful death action to be commenced there. This can be done by a next friend, which, in the \textit{Reyno} case was the plaintiffs’ attorney’s secretary. The estate to be administered consisted wholly of the expected recovery from the lawsuit, thus standing to sue is generally not a problem in the U.S. because of the fictional estate or personal representative,\textsuperscript{23} but nationality of the plaintiffs may play a key role in \textit{forum non conveniens} actions, as will be discussed later.\textsuperscript{24}

C. \textbf{STATE VS. FEDERAL COURT}

Air disaster cases are often commenced in state courts due to the belief that the forum state’s law will be more favorably interpreted. Filing in state court also prevents the joinder of cases filed in other states, thus increasing the stakes for the defendant, i.e., the cost of litigation. State procedural law is often less onerous for plaintiffs than the Federal Rules of Civil Procedure. Even if plaintiff’s attempt to keep a suit in state court is unsuccessful, the initial filing will cause that state’s law to be applied if the case is removed to federal court. Cases can generally only be shifted


\textsuperscript{21} U.C.C. Sec. 2-725(1) (1985).

\textsuperscript{22} 455 U.S. 928 (1981). \textit{See infra} notes 98-114 and accompanying text.

\textsuperscript{23} Under Indiana law, only the parents have standing to sue where the decedent is an unemancipated minor. Ruckman v. Pinecrest Marina, Inc., 367 F. Supp. 25, 26 (N.D. Ind. 1973).

\textsuperscript{24} The location of the plaintiffs’ attorney’s office may play a substantial role in determining where a suit is filed. It is no coincidence that substantial aircraft litigation is filed in Los Angeles, Chicago, Washington, D.C. and, to a lesser extent, in New York, where prominent aviation specialists are located. Litigation across the street from one’s office is easier to handle than a thousand miles away. The expenses of trial are also reduced. Where the court is in another state, a local attorney will have to be retained. This will result in some sort of fee arrangement, potentially reducing the original attorney’s income.

The attorney will prefer to argue a motion to a local court where he is known. He is acquainted with the local rules of practice and unwritten codes of conduct. In local courts he also is more likely to know the judges and to have developed a rapport. Law is the art of persuasion and it is usually easier to persuade a judge with whom one already has a working relationship.
between the two by removal. Two exceptions are that Federal courts may abstain from ruling on essentially state law matters or certify such questions of law to the state’s highest court for decision where state law has made provision for such a procedure.

1. **JURISDICTION**

   As a device to obtain *in personam* jurisdiction over a defendant, states have enacted legal fictions known as "long-arm statutes." Most state long-arm statutes are broad enough to allow major airlines to be haled into their courts. The Due Process clause of the U.S. Constitution has been interpreted to require that there be "minimum" contacts between the defendant and the forum state so that "the maintenance of the suit does not offend 'traditional' notions of fair play and substantial justice." Under the *World-Wide Volkswagen* analysis, a major airline can reasonably foresee being subject to jurisdiction in most states.

2. **CONFLICT OF LAWS**

   The federal court in a diversity action must generally apply the conflict-of-laws rule of the state in which it is sitting. The traditional rule of *lex loci delicti* (law of the place of injury) has all but been replaced by the "paramount interest" test or other similar rules wherein the court examines each legal issue to determine which state has the superior interest in having its law applied. Under the "most significant relationship" test, the appropriate forums to be considered are 1) the place of injury; 2) the place of the misconduct resulting in the injury; 3) the domicile and place of business of the parties; and 4) the place where the relationship between the parties is centered. Among these forums the court must attempt to discover and evaluate for each potential source of law: 1) what interest the legislature of that jurisdiction might have in applying its law; 

31. This has also been called the "most significant relationship" test. See *Ingersoll v. Klein*, 46 Ill.2d 42, 262 N.E.2d 593, 595 (1970). California applies a test called "comparative impairment": *Bernhard v. Harrah’s Club*, 16 Cal. 3d 313, 320, 546 P.2d 719, 723 (1976), which usually reaches the same result. *Air Crash Disaster*, 644 F.2d at 625.
32. *Air Crash Disaster*, 644 F.2d at 612.
2) the needs and interests of the parties; 3) the needs of judicial administration; 4) the promotion of interstate order; and 5) the basic policies underlying that field of law. The Ninth Circuit has held that where two states have an equal interest, the law of the state where the injury occurred must be applied.

In the Chicago DC-10 crash, Illinois was deemed to have the paramount interest on the punitive damages issue due to: 1) the shock wave suffered and the expenses incurred by the state on account of the crash; 2) the fact that all but two of the decedents whose suits were filed in Illinois were from the state; and 3) Illinois, as home of one of the world's busiest airports, had a strong interest in encouraging air transportation companies to do business in Illinois. This is a criticizable conclusion, but it does achieve uniformity in that it prevented some plaintiffs from recovering punitive damages in a case where others could not. The end result was that none of the defendants were held liable for punitive damages.

Some courts have avoided the complexities of conflicts cases by novel means. In *Kohr v. Allegheny Airlines, Inc.*, the federal district court applied "federal common law" on the basis that the federal government has primary interest in regulating the affairs of the nation's airways. The Supreme Court, however, has indicated that courts are not free to depart from the applicability of state law in air crash cases, hence the *Kohr* case is restricted to its facts if it has any remaining viability.

The effect of choice-of-law decisions is important in the area of liability, punitive damages, general damages, and statutes of limitation. In *Browne v. McDonnell Douglas Corp.*, California product liability law was found to be applicable, but Yugoslavia's rule of proportionate liability was applied to the claim against the manufacturer. This decision allowed California to protect its interest in regulating resident manufacturers while

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35. *Air Crash Disaster*, 644 F.2d at 621.
36. Id. at 612.
38. 504 F.2d 400 (7th Cir. 1974).
39. This argument has some support in City of Burbank v. Lockheed Air Terminal, Inc., 411 U.S. 624 (1973) (noise pollution; FAA, in conjunction with E.P.A. has full control over aircraft noise, pre-empting state and local control).
41. *Bowen v. United States*, 570 F.2d 1311, 1317 (7th Cir. 1978).
42. 504 F. Supp. 514 (N.D. Cal. 1980).
shielding McDonnell-Douglas from full liability since it could not implead the Yugoslav airline or the Yugoslav government.

In another case, a federal judge in the Western District of Washington refused to dismiss a case arising from an air crash into the sea near Bombay, India because the statute of limitations in India had run.43 However, the court required that Indian law be applied in all other respects, thus depriving the plaintiffs of more favorable American products liability law.

The effect upon outcome of choice of law determination was graphically illustrated by In re Air Crash Disaster at Boston, Mass. July 31, 1973.44 The court found that the wrongful death statutes of the decedents' domicile should apply. Thus, a recovery ceiling under Massachusetts law applied only to decedents from Massachusetts. Others from Vermont,46 New Hampshire,47 Florida48 were not so limited. Also, determination of damages under the wrongful death statutes of Vermont and Massachusetts is based on different principles. Vermont's law is premised on compensation of the victim for pecuniary losses while Massachusetts' is punitive in nature, invoking very different standards of liability.

3. JOINDER

In certain circumstances, plaintiff's attorney may avoid joining all possible defendants.49 If all plaintiffs are of foreign citizenship in an overseas crash, the attorney may sue only the U.S. manufacturer to avoid removal of the case to federal court. Joiner of a foreign airline could provide grounds for removal to federal court.50 The case also may be dismissed on forum non conveniens grounds if plaintiffs and the airline defendant are located overseas as well as most of the evidence and witnesses. The product liability action against the U.S. manufacturer may be seen only as nominal, and consequently inadequate to continue jurisdic-

43. Air Crash Disaster Near Bombay, 531 F. Supp. 1175 (W.D. Wash. 1982).
45. The limit was $200,000. Id. at 1110 (citing MASS. GEN. LAWS ANN. ch. 229, § 2 (West 1981)).
46. Id.
47. Id. at 1114.
48. Id. at 1119.
49. For many reasons, a plaintiff will usually try to sue every possible defendant in one action. First, the plaintiff wants to avoid being faced with evidence at trial which tends to place the blame on an absent non-defendant. See Speiser, Dynamics of Airline Crash Litigation: What Makes the Cases Move?, 43 J. AIR L. & COM. 565, 567 (1977). Second, the government and the manufacturer may be joined in order to obtain access to documents in their possession. Third, the plaintiff wants to create a large enough pool of resources to fund potential settlements. In addition, the larger the number of potentially responsible defendants, the less each would contribute thereby facilitating settlement opportunity.
tion, or, alternatively, the manufacturer may offer stipulations to cure foreign forum considerations.

III. DEFENDANT'S PERSPECTIVE

A. PROCEDURAL TACTICS

The defendants in air disaster cases are, in reality, the insurers. The federal government is also often named as defendant. Reducing risk of exposure to liability both in number and value of claims is the insurer's prime goal. The insurer focuses on probability of success in court and the amount that he could potentially pay if verdict is for plaintiff. Often liability is not contested in airline cases, leaving only the issue of damages to be settled. Thus, airline defendants look from the outset to settle claims quickly and reasonably.

1. REMOVAL

Defense lawyers generally prefer to be in federal court. Federal procedural rules are uniform throughout the country and federal courts are less tainted by local bias. Removal can also facilitate a later change of venue or consolidation of cases. Consequently, one of the defense attorney's first activities is to ascertain if he may remove a case filed in state court to federal court.

A case can be removed from state court to federal court where there is diversity between the parties (i.e. the parties are not residents of the same state); where the action is based on the Warsaw Convention or any other treaty of the U.S.; where there is a claim against the U.S. government; or where the claim arises under a federal cause of action, such as the Federal Aviation Act, Death on the High Seas Act, common law wrongful death, or the Foreign Sovereign Immunities Act. Defendant is precluded from introducing a possible federal issue in order to obtain federal jurisdiction. Also, subject matter jurisdiction cannot be waived by either party in order to place a case in federal court.

The federal court must have had jurisdiction at time the original suit was filed.

2. **CONSOLIDATION AND CHANGE OF VENUE**

Once a case is removed to federal court, defendant may seek a change of venue, to transfer to a more convenient federal forum or to consolidate related cases. Such a transfer can only be to a jurisdiction where the suit could have been originally brought. A transferred case brings with it the law of the transferor state and circuit. A transfer is a "mere change of courtroom." Transfer, however, may still provide a tactical advantage to the defendant where the transferor state law is more liberal than the recipient state.

The consolidation of federal court suits reduces duplicate litigation, but parallel suits in state and federal court cannot be merged since they are in separate systems. Consolidation is normally sought by defendants to reduce the expense of defending claims, but certain plaintiffs’ counsel seem also to support the operation of the Judicial Panel on Multi-District Litigation. Consolidation has reduced the usual period from crash to termination of litigation and it may also serve to equalize the parties by giving plaintiffs the advantage enjoyed by defendants in having specialist counsel and large resources to support the litigation.

A defendant seeking individual case transfer bears the burden of demonstrating that the balance of convenience strongly favors him under 28 U.S.C. 1404(a). In so doing, defendant cannot assert plaintiff’s inconvenience, nor is it enough to show that defendant’s principal place of business or convenient location for counsel is in another district. Yet, it is easier to satisfy the standard to obtain a transfer within the system than obtain dismissal due to forum non conveniens. Due to the harsher result of dismissal, the court’s option to transfer under Section 1404 is exercised more liberally than dismissal.

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65. *Air Crash Disaster*, 399 F. Supp. at 1106.
72. *Id.* at 32.
B. DISMISSAL VIA FORUM NON CONVENIENS

The high point of foreign case jurisdiction in the U.S. was *In re Paris Air Crash of March 3, 1974.* Since then the American courts have increasingly shown a willingness to dismiss cases on the ground of *forum non conveniens* where the air crash occurred abroad, most of the witnesses and evidence are abroad, and the real parties are foreigners. A *forum non conveniens* dismissal presupposes that the court properly has jurisdiction but nonetheless declines to exercise that jurisdiction. "The principle of *forum non conveniens* is simply that the court may resist imposition upon its jurisdiction where jurisdiction is authorized by the letter of a general venue statute."  

1. THE TRADITIONAL ANALYSIS

The test to be used in deciding a dismissal motion for *forum non conveniens* was set out in 1947 in *Gulf Oil v. Gilbert.* Generally, the *Gilbert* approach calls for a balancing of the interests of the plaintiff, the defendant and the chosen forum, with the qualification that the plaintiff's choice of forum should rarely be disturbed unless the balance of convenience factors strongly favors defendant. Within these guidelines, the decision whether to dismiss is a matter of the trial judge's discretion.

Given *Gilbert's* rather broad contours, it is not surprising that a great
deal of uncertainty followed in its wake. One particularly troublesome question dealt with the importance of the citizenship of the plaintiff. Most courts adopted a rule which placed a greater burden upon defendants seeking to dismiss suits brought by American plaintiffs; conversely, suits by foreigners were more readily dismissed. Other courts took a different approach, declaring that a plaintiff's citizenship was irrelevant to the *Gilbert* balance.

Another issue left unresolved in *Gilbert* was whether the possibility of a change in substantive law should enter into the *forum non conveniens* analysis. Once again, the lower courts reached different conclusions.

2. **Piper Aircraft v. Reyno**

The problems discussed above were directly confronted in 1981 in the landmark case, *Piper Aircraft v. Reyno*. The case arose when a small chartered aircraft crashed in Scotland. The pilot and five passengers, all Scottish citizens and residents, were killed. The decedents' heirs and survivors, their estates, the company operating the plane, the company from which it was leased and the accident investigation were all located in the United Kingdom. Nonetheless, a suit was filed in California state court against the manufacturers of the airplane and its propellers. The nominal plaintiff was unrelated to any of the decedents or their survivors; she was a legal secretary to the attorney who filed the suit. Parallel suits by the survivors were brought in the United Kingdom. The only nexus between the U.S. and the American litigation was the American domicile of the manufacturers. The Scottish courts and law were clearly more appropriate, but the case was filed in California admittedly due to more favorable laws. Scotland has not adopted product liability and

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78. See, e.g., Leasco Data Processing Equip. Corp. v. Maxwell, 468 F.2d 1326, 1344 (2d Cir. 1972) (plaintiff's American citizenship precluded dismissal, despite the fact that balance otherwise favored foreign forum).


83. *Id.* at 239.

84. *Id.* at 240.
solely uses the concept of negligence.\textsuperscript{85} Scottish law allows wrongful death actions only by the next of kin and only for loss of support and society.\textsuperscript{86}

On defendants’ motion, the case was removed from California state court to federal court, then statutorily (Section 1404(a)) transferred to the Middle District of Pennsylvania. After the transfer, defendants moved for dismissal on ground of \textit{forum non conveniens}\textsuperscript{87} contending that the case should be heard in Scotland. The district court granted the motion, but the Court of Appeals reversed.

The Supreme Court upheld the district court’s ruling and laid down two important points of law. First, the court held that “the possibility of a change in substantive law should ordinarily not be given conclusive or even substantial weight in the \textit{forum non conveniens} inquiry.”\textsuperscript{88} To do so, would be to lose valuable flexibility under the \textit{forum non conveniens} doctrine and would make the doctrine virtually useless. This results because plaintiff would ordinarily choose the forum with the most advantageous choice-of-law rules,\textsuperscript{89} requiring the trial courts to engage in complex exercises of comparative law,\textsuperscript{90} and substantially increasing the flow of cases into the U.S.\textsuperscript{91} Forum shopping by defendants would be discouraged by not giving substantial weight to the possibility of a favorable change in the law to the defendant.\textsuperscript{92} The court went on to say that an unfavorable change in law “in rare instances” may not satisfy the initial requirement of an adequate alternative forum, but it gave no guidelines concerning when such a condition would exist.\textsuperscript{93}

Second, the court held that a foreign plaintiff’s choice of U.S. forum deserves less deference than that by a U.S. plaintiff.\textsuperscript{94} In \textit{Reyno}, the attorney’s secretary was used as a proxy plaintiff. Earlier appeals court cases had upheld dismissal in such cases, but this was the first endorsement by the nation’s highest court.\textsuperscript{95}


\textsuperscript{86} Casenote, \textit{supra} note 1, at 408.


\textsuperscript{88} \textit{Id.} at 247.

\textsuperscript{89} \textit{Id.} at 250.

\textsuperscript{90} \textit{Id.} at 251.

\textsuperscript{91} \textit{Id.} at 252.

\textsuperscript{92} \textit{Id.} at 252, note 19.

\textsuperscript{93} \textit{Id.} at 254, note 22.

\textsuperscript{94} \textit{Id.} at 256.

The advantages of the Reyno decision, at least from the point of view of defendants, are apparent. First, the mere fact that an alternate forum's substantive law might be less favorable will no longer be sufficient to defeat dismissal. Further, courts will now apply a different standard to cases involving foreign plaintiffs. Reyno rejects the line of reasoning that U.S. law should follow U.S. corporations wherever they go. The policy statement of Reyno is that manipulation of the American judicial system through clever forum shopping by foreign plaintiffs should be discouraged. Finally, Reyno has implications for suits by American plaintiffs as well. While allowing for greater deference to an American plaintiff's choice of forum, Reyno explicitly refuses to go so far as to bar dismissal of such suits altogether. The applicability of the forum non conveniens doctrine is thus clarified.

Given Reyno, the motion for dismissal on grounds of forum non conveniens may be the defendant's strongest weapon in a foreign case. To the defendant, forum non conveniens is a means of obtaining leverage over the plaintiff. Dismissal from U.S. jurisdictions will force the plaintiff to litigate elsewhere, with application of appropriate law, to recover. Plaintiff must then weigh the probable amount of recovery abroad against the settlement offer.

C. THE WARSAW CONVENTION

If an accident occurs in the course of an international flight, it is likely that the resulting litigation will be governed by the provisions of the Warsaw Convention. The Convention was formally adopted on October 12, 1929 as a response to the increasing frequency of international air travel. Its purpose was to create a unified body of law upon which passengers and carriers could rely. The Warsaw Convention is binding upon all nations who have elected to ratify it.

The aims of the Convention are two-fold: to regulate the international air carrier's liability and to regulate the documents of international air

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96. Casenote, supra note 1, at 434-35.
97. Fitzpatrick, supra note 64, at 557.
98. Reyno, 454 U.S. at 256, note 23.
99. Convention for Unification of Certain Rules Relating to International Transportation by Air, Oct. 12, 1929, 49 Stat. 3000, T.S. No. 876, 137 L.N.T.S. 11 (1934) [hereinafter cited as Warsaw Convention]. "International transportation" is defined as air travel in which the place of departure and place of destination are located in different countries or, if departure and destination points are in the same country, there is an agreed stopping place within the territory of another country. Id. art. 1(2).
101. As of January 1981, 113 countries, including the United States, had ratified the convention. Id. at note 1.
transportation.\textsuperscript{102} Of those dual objectives, counsel in air disaster cases are obviously concerned with the former. The Convention has become the source of much, if not all, of the substantive and procedural aspects of suits against international air carriers. Thus, intimate familiarity with the provisions of the Convention can be a decisive advantage in airline cases.

1. \textit{Jurisdiction}

Article 28 of the Warsaw Convention governs jurisdiction over international air cases. It provides that suit may be brought in the territory of one of the contracting states of the convention, "either before the court of the domicile of the carrier or of its principal place of business, or where he has a place of business through which the contract has been made, or before the court at the place of destination."\textsuperscript{103} United States courts have construed this provision in such a way as to limit the exercise of jurisdiction.\textsuperscript{104} First, the term "destination" has been interpreted as a ticketholder's ultimate stopping point. In other words, a round trip from France to the United States and back would have France as its "destination." Accordingly, jurisdiction over cases arising out of such a trip would not lie in the United States unless the ticket was purchased in U.S. or the carrier has his principal place of business here. This is true even if the injury occurs within the territory of the United States.\textsuperscript{105} Thus, defendants in aircraft cases may properly seek dismissal of actions arising out of such a factual setting.

The convention also imposes a time period within which actions must be brought which supersedes the law of the forum. Pursuant to the Convention, "The right to damages shall be extinguished if an action is not brought within two years, reckoned from the date of arrival at the destination or from the date on which the aircraft ought to have arrived, or from the date on which the transportation stopped."\textsuperscript{106}

2. \textit{Limitation on Liability}

The outstanding feature of the Warsaw Convention and its subsequent amendments is the codification of the substantive law to be applied

\textsuperscript{102} Id. at 379.
\textsuperscript{103} Id. art. 28(1); \textit{see also} N. Matte, supra note 100, at 426.
\textsuperscript{104} Article 28(1) has been interpreted as conveying subject matter jurisdiction, as opposed to mere venue. Thus, if the United States is not among the places enumerated by Article 28(1), the district court lacks jurisdiction and must dismiss the claim. Smith v. Canadian Pac. Airways, 452 F.2d 798 (2d Cir. 1971).
\textsuperscript{106} Warsaw Convention, supra note 115, art. 29(1). The method of calculating the period of limitation is left to the law of the forum. Id. art. 29(2).
in international aircraft cases. Simply stated, the Convention created a rebuttable presumption of liability on the part of the carrier, and a monetary limit on the recovery which a passenger or his heirs could obtain.\textsuperscript{107}

The original Convention provided that an air carrier would generally be liable for passengers’ injuries sustained in an accident, so long as the accident took place on board the aircraft or in the course of embarking or disembarking.\textsuperscript{108} However, a carrier could escape liability if it could prove that it took all necessary measures to avoid the damage, or that such measures were impossible.\textsuperscript{109}

The Convention also imposed a ceiling on an air carrier’s liability. Unless the parties contracted otherwise, maximum liability for passenger injuries was limited to 125,000 francs, approximately $10,000.00.\textsuperscript{110} However, this limitation would not apply if injury resulted from willful misconduct on the part of the carrier.\textsuperscript{111}

The Warsaw Convention was modified in 1955 by the Hague Protocol. The Protocol was prompted in part by a desire to clarify certain of the conventions provisions, but was primarily motivated by the need to increase the liability limitations.

Pursuant to the Protocol, the limitation on liability was doubled to 250,000 francs ($20,000.00).\textsuperscript{112} Also, the unlimited liability provision was modified to include both willful and reckless conduct.\textsuperscript{113}

Despite these refinements, the United States declined to ratify the Hague Protocol, based on a belief that liability restrictions were still unreasonably low. Instead, the U.S. eventually participated in the Montreal Agreement. Unlike the Convention and Protocol, which are agreements among nations, the Montreal Agreement is a contract between the United States and the international air carriers who fly into and out of this country. Under the Agreement, the liability ceiling is raised to $75,000. Also, liability is absolute; a plaintiff need only show that damage has occurred in order to recover. Except for those provisions, all other matters, such as jurisdiction, are controlled by the terms of the Warsaw Convention.

From a defendants’ point of view, it is generally desirable to have a case come under the auspices of the Warsaw Convention. Even the liability limitations contained in the Montreal Agreement are low by Ameri-
can tort law standards. Thus, defense counsel should be alert to the coverage requirements of the Convention in order to invoke its provisions when possible.

**D. FOREIGN SOVEREIGN IMMUNITY**

Another potential weapon for defendants in aircraft cases is the doctrine of sovereign immunity. The concept of sovereign immunity—that a foreign state cannot be sued without its consent—developed in the law of nations, including the United States.\(^{114}\) Over the years, application of the doctrine evolved in the United States to permit liability for "private acts" of foreign governments, while retaining immunity for "public" acts.\(^{115}\) Eventually, the doctrine was codified with the enactment of the Foreign Sovereign Immunities Act of 1976.\(^{116}\) As will be demonstrated, this Act may be applicable in certain aircraft cases.

The general premise of the Act is that a foreign state is immune from the jurisdiction of the United States courts, subject to certain exceptions.\(^{117}\) The Act provides that the term "foreign state" includes agencies or instrumentalities of the foreign state,\(^{118}\) defined as "an organ of a foreign state . . . a majority of whose shares or other ownership interest is owned by a foreign state."\(^{119}\) It is a fact that there are many "national" airlines whose stock is owned by the government of a foreign country.\(^{120}\) In cases where one of these airlines is the defendant, the doctrine of sovereign immunity may operate to bar the exercise of jurisdiction by U.S. courts, particularly in foreign crashes.\(^{121}\)

The mere fact of government stock ownership does not automatically convey immunity, however. The Act also contains various exceptions to the general rule of immunity which must be dealt with.\(^{122}\) In the context of aviation cases, the most important exceptions cover certain categories of actions involving commercial activity carried on by a foreign state.\(^{123}\)

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114. See e.g., The Schooner Exchange v. M'Fadden, 11 U.S. (7 Cranch) 116 (1812).
115. Cook, supra note 107, at 691.
116. See id. at 690-94.
117. Id. at 694.
120. See Cook, supra note 107, at 705 note 86 (listing fourteen airlines which are 100% state-owned, fourteen others which are at least majority state-owned and another nine whose state ownership, while unclear, appears to be greater than 50%).
121. But see Sugarman v. Aeroméxico, Inc., 626 F.2d 270 (3d Cir. 1980) (Court acknowledges, in dicta, that corporation wholly-owned by Mexican Government was an "agency or instrumentality of a foreign state," but defeated the claim of immunity on other grounds).
123. 28 U.S.C. § 1605(a)(2). That section provides:
"(a) a foreign state shall not be immune from the jurisdiction of courts of the United States or of the States in any case . . . (2) in which the action is based upon a com-
The first two clauses of Section 1605(a)(2) cover actions based upon commercial activity carried on in the United States or upon specific acts performed in the U.S. in connection with commercial activity conducted elsewhere. These two clauses have generally been interpreted to require that the specific act complained of take place in the United States.\textsuperscript{124} Thus, under this interpretation, claims arising out of aircraft accidents occurring outside the United States may be barred by immunity.

On its face, the third clause of Section 1605(a)(2) is more troublesome. It denies immunity for claims based upon acts occurring outside the U.S., but which "cause a direct effect" in this country. Arguably, that language could encompass claims for personal injuries suffered by Americans abroad, since such damages might be said to have an "effect" in the United States. However, the "direct effect" language has been interpreted rather narrowly.\textsuperscript{125} The mere fact that a plaintiff has suffered an injury has been held to be insufficiently "direct" to satisfy the requirement.\textsuperscript{126}

Thus, the doctrine of sovereign immunity can be a formidable weapon for defendants as long as certain criteria are met: (1) the defendant airline must be state-owned; (2) the accident must have occurred outside the territory of the United States; and (3) there must be no other "direct effect" on the United States which would give rise to the 1605(a)(2) exception.

\textbf{E. \textit{Ticket Limitations}}

Perhaps the most straightforward source of limitations on liability and special procedural requirements is on the flight coupons, or passenger tickets, themselves. It is not uncommon for airlines to impose certain conditions of carriage, and to list such conditions on the coupons. Failure of

\textsuperscript{124} See, e.g., Yessinin-Volpin v. Novosti Press Agency, 443 F. Supp. 849 (S.D.N.Y. 1978) (Clauses inapplicable to libel action in which alleged libel was not published in U.S.); Upton v. Empire of Iran, 459 F. Supp. 264 (D.D.C. 1978) (Clauses held inapplicable to claim arising from collapse of roof at Tehran, Iran airport). \textit{But see} Sugarman v. Aeromexico, 626 F.2d 270 (3rd Cir. 1980) (holding that injuries occurring in Mexico were "based upon a commercial activity carried on in the United States" because plaintiff was at mid-point of a round trip, commenced and ticketed in the U.S.).

\textsuperscript{125} See, e.g., Upton v. Empire of Iran, 459 F. Supp. 264 (D.D.C. 1978); Harris v. Vao Intourist, 481 F. Supp. 1056, 1062 (E.D. N.Y. 1979) ("Indirect injurious consequences within this country of an out-of-state act are not sufficient contacts to satisfy the direct requirement of section 1605(a)(2). ")

\textsuperscript{126} Upton, 459 F. Supp. 264; Harris, 481 F. Supp. 1056.
a complaining passenger to comply with required procedures listed on the contract for carriage can give defendants an advantage in aircraft cases.

For example, a ticket may impose limitations on the time period or the location for filing claims. If a plaintiff overlooks these restrictions and fails to comply, he of course may challenge their validity in court. However, the burdensomeness of doing so, as well as the uncertainty of success, gives defendants an enhanced bargaining position in settlement discussions.

Moreover, tickets may impose limitations on the amount which can be recovered. This is especially likely where a passenger is flying on a "free pass," such as those often given to airline employees. Such passes may also include waivers of a cause of action for the airline's negligence. In any event, flight coupons should be carefully reviewed by counsel for the air carrier, for they will often relate to important matters of substance and procedure.

**Conclusion**

The quantum of recovery in the U.S. is extremely dependent upon where a claim is brought and where trial is held. The plaintiff and defendant will engage in extensive pre-trial efforts to gain the most advantageous position possible. The plaintiff will usually file suit in the state which will optimize his chances of receiving the largest recovery. Defendant will attempt to dislodge the case from state court by such devices as removal to federal court or dismissal due to *forum non conveniens*. If successful in removing to federal court, defendant may wish to move the case to a different venue or consolidate all of the related suits stemming from an air crash, or assert *forum non conveniens* if appropriate.

Most motions are decided by a judge applying balancing tests. Due to the subjectiveness of these tests, the outcome of these motions is not always predictable. In the end, the maneuvering is done to maximize each party's position in litigation and settlement negotiations. Needless to say, the strategy employed at the outset of litigation is critical to the result at the end of the day.
The Right-to-Know and the Trucking Industry:
Regulating Regulations

ALAN E. SENECZKO*

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INTRODUCTION

The presence of toxic substances in the workplace is becoming a very popular subject of legislation, federally and on a State and local basis. As a result, numerous laws are now being proposed and enacted regulating the right of both employees and local communities to know what hazardous substances they may be exposed to during the normal course of their employment or as a result of an accident.

The laudable objective of such legislation is to keep workers and communities informed as to the hazards to which they may be exposed, and to provide training in proper handling of hazardous substances. Consistent with this purpose, the laws focus on chemical manufacturers and other employers who regularly maintain a constant inventory of toxic substances, creating a potential hazard for both employees and the community. However, it is now urged that these originally narrow laws be expanded to cover all employers, including those in the industry. This rapid expansion has widespread ramifications for employers in the industry.

Although the Department of Transportation ("DOT") currently regulates the transportation of hazardous substances across the nation, trucking companies may now be faced with the regulation of similar matters by other federal agencies (e.g., the Occupational Safety and Health Administration or "OSHA"), by individual states and by local ordinances.

The rapidly expanding scope of these laws, and the ever-growing number of governmental entities seeking to regulate this issue, create serious problems for the trucking industry, pragmatically and logistically. As
the substance of each of these laws is considered, the need for a uniform federal standard preempting all other laws becomes readily apparent.

This article will review the current legislation governing the right-to-know issue, the practical effects of that regulation on the trucking industry and a proposed solution to the problem. Among the issues to be considered are:

1. The Federal Hazard Communication Standard and the difficulties inherent in its application to trucking industry employers;
2. Preemption of state and local laws by the Hazardous Communication Standard;
3. Preemption of the Hazard Communication Standard by other regulatory agencies;
4. Existing Department of Transportation regulations and their effects on similar state or local laws;
5. The relationship between Department of Labor regulations and Department of Transportation regulations; and
6. A proposed right-to-know regulation for the trucking industry.

I. THE FEDERAL HAZARD COMMUNICATION STANDARD

A. PURPOSE

On November 21, 1983 the Assistant Secretary of Labor for Occupational Safety and Health promulgated what has become known as the Federal Hazard Communication Standard ("HCS"). This statutorily authorized standard was the response of the Department of Labor ("DOL") to the long-recognized need for apprising workers of the hazards of the chemicals with which they worked. This standard was originally conceived with a very narrow purpose: "[T]o establish uniform requirements for hazard communication in one segment of industry, the manufacturing division." Under the provisions of the standard, manufacturing sector employees who are exposed to hazardous chemicals are to receive information about the chemicals through a comprehensive hazard communication program. This program requires all covered employers to provide hazard information to their employees by means of labels on containers, material safety data sheets and training. For the most part, all of these procedures already exist in the trucking industry. However, to more fully

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2. Under 29 U.S.C. § 655(a) (1982) the Secretary of Labor is granted the authority to promulgate standards to assure the greatest protection of the safety and health of employees.
4. Id.
5. The Secretary recognized the existence of at least some of these requirements in § 1910.1200(f)(2) of the standard, which relates to the labeling requirement: Chemical manufacturers, importers, or distributors shall ensure that each container of hazardous chemicals leaving the workplace is labeled, tagged or marked in accordance with this section in a manner which does not conflict with the Hazardous Materials
understand the similarities between existing Department of Transportation regulations and the provisions of the Department of Labor’s Hazard Communication standard, the provisions of the HCS and their implications for the trucking industry must be further examined.

B. SUBSTANTIVE PROVISIONS

1. HAZARD DETERMINATION

The first substantive provision of the HCS requires chemical manufacturers and importers to evaluate the chemicals produced in their workplace or imported by them to determine if they are hazardous. Employers are not required to evaluate chemicals unless they choose not to rely upon the evaluations performed by the chemical manufacturer or importer. Although this provision is obviously not applicable to employers in the trucking industry, it operates to clearly illustrate the intent of the present OSHA communication standard.

2. WRITTEN HAZARD COMMUNICATION PROGRAM

The HCS also requires employers to develop and implement a written hazard communication program for their workplace, describing how the labeling, material safety data sheet and training requirements of the standard will be met. This program also requires employers to:

1) List the hazardous chemicals known to be present in the workplace, using an identity that is referenced on the appropriate material safety data sheet;

2) Detail the method the employer will use to inform employees of the hazards of non-routine tasks and the hazards associated with chemicals contained in unlabeled pipes in their work area; and

3) Detail the methods that will be used to inform any contractors and their employees working in the employer’s workplace of any hazardous chemicals to which they may be exposed and of any suggested protective measures.

The absurdities created by the application of the above requirements to employers in the transportation industry are glaring. How, for example, is a major trucking firm to maintain a readily available, continuously updated “list” of all hazardous chemicals known to be present in the workplace? Such a list would be hundred of pages long in a matter of months, since literally hundreds of thousands of items of cargo pass through the premises of trucking firms in just a few months.

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7. 29 C.F.R. § 1910.1200(e)(1). These requirements are discussed in detail infra.
3. **LABELS AND OTHER FORMS OF WARNINGS**

One of the most important provisions of the HCS is its labeling requirement. Under this provision chemical manufacturers, importers, employers and distributors are to ensure that each container of hazardous chemicals found in or leaving the workplace is labeled, tagged or marked with the identity of the hazardous chemical and the appropriate hazard warnings. However, recognizing the preexisting DOT regulation of this area, the HCS provides that the above labeling must be accomplished in a manner that does not conflict with the Hazardous Materials Transportation Act ("HMTA") and with any regulations issued under that Act by the Department of Transportation. By specifically carrying out this exception, the Department of Labor impliedly acknowledged that existing Department of Transportation labeling regulations are sufficient to satisfy the requirements of the HCS.

4. **MATERIAL SAFETY DATA SHEETS**

The HCS also requires chemical manufacturers, importers and employers to have available a material safety data sheet (MSDS) for each hazardous chemical which they use. Copies of material safety data sheets are required for each hazardous chemical in the workplace and must be readily accessible during each work shift to employees when they are in their work areas. Chemical manufacturers and importers are also required to ensure that distributors and purchasers are provided with an appropriate MSDS with each initial shipment, either providing it with

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8. 29 C.F.R. § 1910.1200(f).
10. However, on September 11, 1985, Jennifer Silk, an occupational health specialist with OSHA, stated that "DOT labeling will not suffice for purposes of hazard communication." *Chemical Makers, Users Urged to Interpret Coverage and Scope of OSHA Standard Broadly*, 15 O.S.H. Rep. (BNA) No. 16 at 327 (Sept. 19, 1985).
12. 29 C.F.R. § 1910.1200(g)(8). Information required to be found on the MSDS for each hazardous chemical includes, among other minimum requirements:
   a) the identity used on the label;
   b) the chemical and common names of the substance, mixture and/or any hazardous ingredients of the same;
   c) the physical and chemical characteristics of the substances;
   d) the physical hazards of the substance;
   e) the health hazards of the substance;
   f) the primary routes of entry;
   g) any generally applicable precautions for the safe handling and use of the substance;
   h) any generally applicable control measures;
   i) emergency and first aid procedures; and
   j) the name of the party responsible for preparing the MSDS and having knowledge of any additional necessary information about the substance.
29 C.F.R. § 1910.1200(g)(2).
the shipped containers or sending it prior to or at the time of shipment.\textsuperscript{13} However, if the MSDS is not provided with the shipment, the purchaser is responsible for obtaining one from the manufacturer.

The MSDS requirement is also illustrative of the problems inherent in any attempt to apply HCS to the trucking industry. As will be discussed in greater detail later, the information to be contained in each MSDS is duplicative of much already required to be found on the bill of lading.\textsuperscript{14} In addition, the HCS makes no mention of the duties of the shipping company, only those of the shipper (manufacturer) and purchaser/distributor. If the HCS is extended to apply to all employers, it could arguably be a trucking company's duty to ensure that there is a MSDS for every hazardous substance it ships and to determine which items of cargo need material safety data sheets.

5. \textit{Employee Information and Training}

The employee information and training provisions of the HCS are the focal point of the entire standard; they reflect the purpose of the standard and the manner in which employees are to benefit from it. This provision\textsuperscript{15} requires employers to provide employees with information\textsuperscript{16} and training\textsuperscript{17} on the hazardous chemicals introduced into their work environment.

Similar procedures have been implemented by trucking industry employers through existing DOT regulations, although not to the same extent.\textsuperscript{18} More disturbingly, the HCS training requirements, as written, could be extremely burdensome. For example, the training provisions re-

\textsuperscript{13} 29 C.F.R. § 1910.1200(g)(6).
\textsuperscript{14} See, e.g., 49 C.F.R. § 172.200 (1984). In addition, many employers utilize the Emergency Response Guidebook, which provides easily comprehended information regarding the health and physical hazards of substances being transported through commerce. See infra, Section IV(B).
\textsuperscript{15} 29 C.F.R. § 1910.1200(h) (1985).
\textsuperscript{16} The employee information provisions of the HCS require employees to be informed of:
\textsuperscript{a} the requirements of the HCS;
\textsuperscript{b} any operations in their work area where hazardous chemicals are present; and
\textsuperscript{c} the location and availability of the written hazard communication programs, the required list of hazardous chemicals, and the material safety data sheets.
\textsuperscript{29} C.F.R. § 1910.1200(h)(1).
\textsuperscript{17} The training provisions require that employees be trained regarding:
\textsuperscript{a} the methods and observations that may be used to detect the presence or release of a hazardous chemical in the work area;
\textsuperscript{b} the physical and health hazards of the chemical in the work area;
\textsuperscript{c} the measures employees can take to protect themselves from the hazards;
\textsuperscript{d} the details of the employer's hazard communication program, including explanations of the labeling system, material safety data sheets, and how to obtain and use the appropriate hazard information.
\textsuperscript{29} C.F.R. § 1910.1200(h)(2).
\textsuperscript{18} See infra, Section IV(C).
quire additional training every time a new hazard is introduced into the work area. Applied literally, this could require trucking industry employers to hold weekly, daily or even hourly training programs.

C. Remedies

The Hazard Communication Standard provides employees with certain rights, but no specified remedies. This leaves open a number of questions for the trucking industry; for example, what recourse is available to an employee if an employer refuses to provide him or her with information on a substance believed to be hazardous? Similarly, may an employee unloading trucks refuse to work with or unload any materials not having a required label, but believed to be hazardous? Recourse in any given situation will primarily lie in Section 11(c) of the Occupational Safety and Health Act. However, trucking industry employees might also be allowed to rely upon the more liberal remedies available under the Surface Transportation Act.

1. O.S.H. Act Section 11(c)

Section 11(c) of the Occupational Safety and Health Act prohibits an employer from discriminating against any employee for exercising any right afforded by the Act. Under Section 11(c), employers discharging an employee in violation of the Act can be held liable for reinstatement and back pay. Employees exercising their rights under the HCS would presumably be protected by the provisions of Section 11(c). However, before an employee could refuse to perform work believed to involve hazardous substances, the Whirlpool "reasonable person" standard would first have to be met.


22. In Whirlpool v. Marshall, 445 U.S. 1 (1980), the United States Supreme Court defined the circumstances under which an employee's conduct will be held to be "protected," thereby entitling him or her to the remedies of Section 11(c). Examining the ability of an employee to refuse to perform work believed to be dangerous, the court set forth the following standard: Before an employee can refuse to perform a work assignment, that employee must have a reasonable fear of death or serious physical harm, coupled with a reasonable belief that a less drastic alternative is not available to avoid the danger or safety hazard. In refusing to perform the work, the employee must act in good faith and the apprehension must be such that a reasonable person under similar circumstances would conclude that there is a real danger of death or serious injury. Finally, there must have been insufficient time to eliminate the danger by other alternatives.

23. Id.
2. Surface Transportation Act Section 405

Another remedy arguably available to a trucking industry employee for a violation of the Hazard Communication Standard lies in Section 405 of the Surface Transportation Assistance Act of 1982. Under Section 405(a), an employer is prohibited from discriminating against employees who have filed complaints or instituted any proceedings relating to the violation of a commercial motor vehicle safety rule, regulation, standard or order. Section 405(b) further prohibits an employer from discriminating against an employee:

[F]or refusing to operate a vehicle when such operation constitutes a violation of any federal rules, regulations, standards, or orders applicable to commercial motor vehicle safety or health, or because of the employee's reasonable apprehension of serious injury to himself or the public due to the unsafe condition of such equipment.

Although the above provisions were originally envisioned to encompass situations in which employers required employees to operate unsafe trucks, and this is the way the Act has traditionally been interpreted and applied, Section 405 could be applicable to situations in which employ-

25. id.
26. An examination of the legislative history of the statute shows that Congress' main concern was reducing the number of fatalities caused by the operation of unsafe vehicles (e.g., accidents involving overloaded, improperly balanced or defective equipment). S. 3044, 97th Cong., 2nd Sess., 128 Cong. Rec. 14028 (1982), Comm. on Commerce, Science and Transportation; 96th Cong., 1st Sess., Report on Truck Safety Act (Comm. Print 1979):

[It] is important to note the respective rules of the Departments of Transportation and Labor. The Secretary of Transportation, for example, in protecting the public from unsafe commercial motor vehicles, in assuring that commercial motor vehicles are safety maintained, equipped, loaded, and operated, is responsible for the manner in which brakes are repaired, the manner in which a load is distributed in a vehicle, the design and equipment of the vehicle, and related matters insofar as failure to observe his regulations would adversely affect the safety of the public or the health and safety of operators of commercial motor vehicles. The Secretary of Transportation is not responsible for protecting employees from asbestos fibers, and toxic fumes involved in the course of properly repairing a brake, nor for the protection of employees from slippery walking surfaces or for inadequately braked fork-lift trucks. These activities continue to be the responsibility of the Department of Labor.

At the same time, the Committee believes that both Departments must focus more attention upon the hazards that commercial motor vehicle drivers face in the course of their work. As efforts to permanently reduce or eliminate specified health hazards may ultimately require changes in commercial motor vehicle design, which is generally the expertise of the Secretary of Transportation, this bill therefore directs the Secretary of Transportation and the Director of the National Institute for Occupational Safety and Health, in consultation with the Secretary of Labor, to conduct a study of safety and health hazards to drivers. . . . This section requires the Secretaries and the Director to make every attempt to avoid overlap or duplication of activities and to coordinate their efforts. S. 2033, 97th Cong., 2nd Sess., 128 Cong. Rec. 14027 (1982).
27. See, e.g., McKenzie Tank Lines, Inc., No. 4-0280-83-03E (Oct. 20, 1983) (employee refusal to operate vehicle with unsafe tires); Polkville Milk Haulers, Inc., No. 2-6010-84-502 (April
ees refuse to operate or unload trucks containing hazardous substances. This is especially true considering the broad "any proceeding," "safety regulation" and "any federal rules" language contained in Sections 405(a) and (b). An employee might, for example, refuse to operate a truck unless copies of the material safety data sheets are provided for each item of cargo believed to be hazardous.

The availability of a potential Section 405 remedy for violations of the HCS is an important consideration that must be reckoned with when considering the scope of the Hazard Communication Standard. This is because the remedial provisions of Section 405 are much more broad than those of Section 11(c) of OSHA, the existing HCS remedy. For instance, under Section 405 an employee has 180 days to file with the Secretary of Labor a complaint alleging a discriminatory act. Under Section 11(c) an employee has 30 days. More importantly, Section 405 expressly provides for immediate reinstatement, back pay, compensatory damages and attorney fees, as opposed to the traditional remedies of reinstatement and back pay available under Section 11(c). As a result, any sweeping, short-sighted extension of the HCS to trucking industry employees is destined to create expanded remedial rights, which may force compliance by trucking industry employers with the logistically impossible requirements of the Hazard Communication Standard.

3. **Deferral**

Another issue that must be addressed when considering the scope of the HCS and the remedies available for its violation concerns the matter of deferral. Since a great number of employers in the trucking industry have labor agreements with the International Brotherhood of Teamsters which provide for final and binding arbitration, it would seem patently unfair to require employers to relitigate matters that have already been resolved through the contractual grievance and arbitration procedures. Yet, this is a distinct possibility. Consider the situation of the unionized dock worker who refuses to unload material believed to be hazardous. He is terminated as a result of his refusal and files a grievance contesting the discharge. Although he loses the grievance and arbitration, he subsequently files charges seeking recourse under Sections 11(c) and 405. The entire process is not only duplicated as a result of these charges, but the employee also now gets another "kick at the cat." The question that

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12, 1984) (employee refusal to operate vehicle with cracked axle); Roberts Trucking Co., Inc., No. 5-0170-84-501 (Dec. 28, 1984) (employee refusal to operate vehicle with defective brakes); Transport Service Co., No. 5-6850-84-504 (Dec. 28, 1984) (employee refusal to drive in excess of DOT maximum daily driving time); Sun Supply Corp., No. 6-4140-84-501 (employee refusal to falsify driver logs).
arises is whether deference will be paid to the results of the arbitration process.

a. National Master Freight Agreement

Under the National Master Freight Agreement employees are protected from being discharged in retaliation for refusing to drive an unsafe vehicle. An employee may refuse to operate a vehicle not “in safe operating condition,” or not equipped with a prescribed “safety appliance.”

It can be argued that this provision would also apply to situations envisioned by the HCS. Is a vehicle in “safe operating condition” if its drivers are not provided with material safety data sheets for its cargo?

b. Section 11(c) Deferral

Assume a driver is discharged for refusing to accept a load without a material safety data sheet for a questionable substance. He challenges his discharge through the contractual grievance procedure, but ultimately loses in arbitration. He then files a charge with OSHA alleging a violation of the HCS.

Under current procedures, OSHA may defer to the decision of an arbitrator, but only under prescribed circumstances, and then on a case-by-case basis.

Similarly, OSHA recognizes that the situation may occur in which a Section 11(c) complaint is filed simultaneously with a grievance or a complaint with another agency. Under such circumstances, OSHA may

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28. The National Master Freight Agreement, art. XVI, § 1 provides that
The employer shall not require employees to take out on the streets or highways any vehicle that is not in safe operating condition, including but not limited to acknowledged overweight or not equipped with the safety appliances prescribed by law. It shall not be a violation of this Agreement where employees refuse to operate such equipment unless such refusal is unjustified. All equipment refused because it is not mechanically sound or properly equipped, shall be appropriately tagged so that it cannot be used by other drivers until the maintenance department has adjusted the complaint. (Emphasis added).

29. Historically, if an employee entered in good faith into grievance arbitration proceedings, the 30-day limitation period for filing an 11(c) complaint with OSHA would be tolled. This procedure has been changed quite recently. On August 15, 1985, OSHA announced that an ongoing grievance arbitration proceeding will no longer suspend or “toll” the 30-day limitation period, meaning that any employee desiring to file a complaint with OSHA must do so within 30 days of the alleged discriminatory conduct. DAILY LAB. REP. (BNA) No. 154 at A-10 (August 9, 1985).


31. It must be clear that the proceedings dealt adequately with all of the factual issues; the proceedings must have been free of procedural infirmities; and the outcome of the proceeding must not have been repugnant to the purpose and policies of the Act. 29 C.F.R. § 1977.18(c) (1985).

32. 29 C.F.R. § 1977.18(a)(3) provides that “[w]here a complainant is in fact pursuing remedies other than those provided by Section 11(c), postponement of the Secretary’s determination and deferral to the results of such proceedings may be in order.” (Citations omitted).
postpone its determination of the matter (and later defer), but only if cer-
tain procedural requirements are met.\textsuperscript{33}

This deferral policy, while satisfying generally accepted standards for
deferring to the decisions of other proceedings,\textsuperscript{34} creates a practical
problem. Frequently, the decisions of the contractually-agreed upon joint
grievance committees are not detailed and often only state "grievance
denied" or "grievance upheld." This creates a problem when OSHA at-
ttempts to examine the procedure and the facts presented to determine
whether deferral is appropriate.

c. \textit{Section 405}

The issues that arise with respect to the HCS, Section 11(c) and
deferral will also inevitably arise with respect to any attempted enfor-
cement of the HCS through Section 405 of the Surface Transportation Act.
Although there are no existing procedures under Section 405 calling for
deferral, the Surface Transportation Act authorizes the Secretary of La-
bor, not the Secretary of Transportation, to enforce its provisions. There-
fore, an argument can be made that the deferral policies set forth by the
Secretary of Labor for Section 11(c) deferral also govern claims arising
under Section 405.

D. \textit{The Application of the HCS to the Trucking Industry}

Since the extension of the HCS to all employers has now become a
reality,\textsuperscript{35} the effects of a sweeping extension of its provisions to the truck-
ing industry become more and more important. If trucking industry em-
ployers are required to comply with the requirements of the HCS, freight

\textsuperscript{33} The factual issues in the proceeding must be substantially the same as those raised by
the Section 11(c) complaint; the proceedings must not violate the rights guaranteed by Section
11(c); and the forum hearing the matter must have the power to determine the ultimate issue of
discrimination. 29 C.F.R. \textbf{\textsuperscript{\textsuperscript{\footnotesize{§}}} 1977.18(b)} (1985).

\textsuperscript{34} \textit{See}, \textit{e.g.}, United Technologies Corporation, 268 NLRB 557 (1984) (National Labor Re-
lations Board will defer an investigation to the grievance-arbitration procedure upon the satisfac-
tion of certain standards recognizing the validity of the arbitration process and the arbitrariness
of the dispute); Olin Corporation, 268 NLRB 573 (1984) (NLRB will defer to the award of an arbitra-
tor where the proceedings appear to have been fair and regular, the parties agreed to be bound
by the award, the award was not clearly repugnant to the purposes and policies of the Act, the
issues addressed were factually parallel and the arbitrator was presented generally with the facts
alleged in the "deferred" complaint).

\textsuperscript{35} On August 20, 1985 the acting Assistant Secretary of Labor stated that OSHA \textit{would}, in
fact, be extending the provisions of the HCS to all employers. \textit{OSHA Plans to Extend to All
at A-7 (August 20, 1985). \textit{See also}, United Steelworkers v. Auchter, 763 F.2d 728 (3rd Cir.
1985) in which the Third Circuit directed OSHA to explain why the HCS should only apply to
manufacturing sector employers.
terminals will become largely storage facilities for material safety data sheets.

This raises a number of practical questions. Will these employers be required to keep a file of data sheets for each hazardous substance passing through their terminals? Will these employers be required to update, on a daily basis, the hazardous chemicals list required by the current HCS? Will drivers be responsible for determining which data sheets are to go with each piece of cargo, especially if the data sheets refer to components of existing cargo? Can trucking employers be held responsible for erroneous information? How will the detailed training procedures required by the HCS be implemented? Will trucking industry employees have to be trained on a daily, if not hourly basis, due to the fact that a new hazardous substance may be sitting on the dock?

The above questions illustrate just a few of the unsolved (and perhaps unsolvable) problems created by the extension of the HSC to the trucking industry. The entire situation is further complicated by the fact that the Department of Transportation has already promulgated a number of regulations governing areas covered by the HCS.36 Recognizing this, OSHA could take the position that the DOT has exclusive jurisdiction to prescribe or enforce hazardous substance standards as they relate to the trucking industry.37 The solution, however, is not as simple as the statute would make it appear. For instance, the Department of Transportation's preemptive authority is not as strong as that of OSHA.38 This creates a very serious problem when attempting to deal with state laws having more stringent requirements than the DOT. Will drivers be required to carry material safety data sheets with them in some states, but not in others? In addition, which agency will govern "right-to-know" situations not traditionally regulated by the Department of Transportation? For example, what if a freight handler refuses to unload a substance believed to be hazardous until he is provided with a material safety data sheet relating to that situation?

Herein lies the problem. How many regulations can there be in this area? While one uniform federal standard presents the most desirable solution, which governmental agency is to promulgate and enforce that standard, and what of more demanding state laws? The sections to follow address these questions and culminate in a proposed solution: OSHA adoption and enforcement of existing DOT regulations, but only as they relate to hazardous materials communications.

36. See infra, Section IV, in which DOT regulation of hazardous substances in the trucking industry is discussed.
38. See infra, Section V, in which DOT preemption of state laws is discussed.
II. OSHA PREEMPTION OF STATE RIGHT-TO-KNOW LAWS

A. SURVEY OF STATE LAWS

The need for uniform regulation of employee, and community, "right-to-know" is made evident upon an examination of the wealth of state laws currently dealing with this issue.\textsuperscript{39} Several states have essentially incorporated the federal hazard communication standard into their own statutory provisions, requiring employee education and training, the provision of material safety data sheets and hazardous chemical labeling.\textsuperscript{40} Other states adopt some, but not all of the requirements imposed by the Hazard Communication Standard. Some of these states, for example, require employee training and education, including the provision of information regarding hazardous chemicals, but do not necessarily contain the labeling and/or material safety data sheets requirements of the OSHA standard.\textsuperscript{41}

\textsuperscript{39} For a general survey of the various State Right-to-Know laws, see, \textit{Right-To-Know: A Regulatory Update on Providing Chemical Hazard Information} (BNA, 1985).

\textsuperscript{40} See, \textit{e.g.}, Illinois, ILL. REV. STAT. ch. 48, §§ 1401-1420 (1983) (employers must label containers of toxic substances used in the workplace and provide chemical information to employees exposed to toxic substances); Iowa, IOWA CODE ANN. §§ 455D.1-455D.19 (West 1985) (federal OSHA standard adopted); Massachusetts, MASS. GEN. LAWS ANN. ch. 111F, §§ 1-21 (West 1985) (employers must maintain material safety data sheets supplied by manufacturers or sellers of toxic or hazardous substances used in the workplace; provide annual education and training programs on the nature and location of the substances; and label each container with the substance's chemical name); and Oregon, OR. REV. STAT. § 654.025(2) and § 656.726(3) (1983) (adopting HCS, but applying it to all employers, except those in construction and agriculture).

\textsuperscript{41} See, \textit{e.g.}, Alaska, ALASKA STAT. §§ 18.60.065-18.60.068 (1983) (employers required to conduct education programs, post safety posters or a list of chemicals and provide access to information on listed substances); California, CAL. LAB. CODE §§ 6360-6399.9 (West 1985) (employers in manufacturing sector required to provide information on chemical substances); Connecticut, CONN. GEN. STAT. ANN. §§ 31-25j-31-25p (West 1985) (employers required to provide employees with lists of hazardous chemicals used or produced by the employer and to conduct an education program); Florida, FLA. STAT. ANN. §§ 442.101-442.127 (West 1985) (employers required to provide employee education and training, to provide notice regarding toxic substances and to keep material safety data sheets on file); Maine, ME. REV. STAT. ANN. tit. 26, §§ 1709-1725 (Supp. 1985) (employers required to provide information to employees about hazardous chemicals used in the workplace and to institute education programs for those employees exposed to the substances); Minnesota, MINN. STAT. §§ 182.65-182.675 (Supp. 1985) (employers must train employees on a yearly basis and provide material safety data sheets and information to any employees who request it); New Hampshire, N.H. REV. STAT. ANN. § 277-A (1983) (training, material safety data sheets and posting of notices regarding toxic substances required); New York, N.Y. LAB. LAW §§ 875-883 (McKinney 1984) (employers required to provide information on the identity and hazardous effects of toxic substances in the workplace, including a requirement to post notices); Rhode Island, R.I. GEN. LAWS §§ 28-21-1-28-21-21 (Supp. 1985) (employer required to provide a list of hazardous or toxic materials to the employees and to institute employee education and training programs with regard to those substances); Washington, WASH. REV. CODE ANN. §§ 49.17.050-.080 (Supp. 1986) (employers required to post warning labels on hazardous substances, conduct education and training programs and provide material safety data sheets); West Virginia, W. VA. CODE § 21-3-18 (Supp. 1985) (em-
Conversely, there are states which require the labeling of hazardous chemicals in the workplace and/or the provision of material safety data sheets, but do not contain educational or training requirements.\textsuperscript{42} Other states not only adopt some or all of the HCS requirements, but also extend its provisions to employers in the nonmanufacturing sector.\textsuperscript{43} Additionally, several states have adopted community right-to-know standards, providing communities with access to workplace hazard information.\textsuperscript{44} Finally, two states allow for employee access to company records of employers required to disclose information about hazardous or toxic chemicals used in the workplace and to post warning notices where ten or more employees work; and Wisconsin, Wis. Stat. §§ 101.58-59 (Supp. 1985) (employers required to inform employees of the right to information on hazardous substances in the workplace and to provide education and training programs to those employees routinely exposed to hazardous materials).

42. See, e.g., Delaware, Del. Code Ann. tit. 16, §§ 2401-2417 (1984) (chemical manufacturers and distributors are required to provide material safety data sheets to all companies purchasing hazardous materials); and Michigan, Mich. Comp. Laws Ann. § 408.1011 (West 1985) (employers are required to post material safety data sheets that specify each substance’s chemical name and other relevant information where chemical mixtures are used in a hazardous quantity).


44. See, e.g., Delaware, Del. Code Ann. tit. 16, § 2406 (1984) (employers that store hazardous chemicals in excess of 55 gallons or 500 lbs. must provide the local fire department with names and telephone numbers of knowledgeable company officials who may be contacted if further information is required); Iowa, Iowa Code Ann. §§ 455D.1-455D.19 (West 1985) (provides for the dissemination of information to the community at large); Maryland, Md. Ann. Code art. 89, §§ 32A-32N (1985) (information regarding hazardous and toxic substances must be provided to the Maryland Department of Health and Mental Hygiene); Massachusetts, Mass. Gen. Laws Ann. ch. 111F, §§ 1-21 (West 1985) (copies of data sheets should be made available to citizens where the request is not frivolous or intended to harass employer); North Dakota, N.D. Cent. Code § 19-21 (1981) (information regarding hazardous substances must be provided to local fire departments, offices of state fire marshals and other governmental emergency response departments); Oregon, Or. Rev. Stat. § 654.025(2) and § 656.726(3) (1983) (State Fire Marshall to conduct survey of employers and compile a list of hazardous chemicals to be distributed to local public health organizations and fire jurisdictions); and Pennsylvania, Pa. Stat. Ann. tit. 35, §§ 7301-7320 (1985) (safety data sheets must be provided to employees, the community and the state Department of Health).
ployee exposure to toxic and hazardous substances.\textsuperscript{45} As the above summary of state laws indicates, the abundance and diversity of state right-to-know laws creates serious problems for employers attempting to comply with the requirements of multiple states. In addition to this, many states allow employees to refuse to work with hazardous substances until the identity of the substance is obtained—even absent the traditional Section 11(c) \textit{Whirlpool} "reasonable person" standard.\textsuperscript{46} In sum, the difficulties created by attempting to comply with the varying requirements of state law calls into question their efficacy in achieving their purpose. ""The fundamental reason for legislating a hazard communication program, i.e. worker safety and health, is lost in the shuffle of attempting to comply (in form) with the multitude of hazard communication regulations."\textsuperscript{47}

\textbf{B. \textit{LOCAL LAWS}}

Further exacerbating the lack of conformity in right-to-know laws is the increasing number of communities enacting local right-to-know ordinances. A 1983 study conducted by the Chemical Manufacturers Association disclosed 34 communities which have already passed right-to-know laws.\textsuperscript{48} Moreover, a Federal District Court recently rejected a claim that a county-wide right-to-know law ""irreparably harmed business"" and authorized the implementation of Michigan's first local right-to-know law.\textsuperscript{49} The local enactment of right-to-know ordinances exemplifies the rapid expansion of this area, as well as the swelling public interest in it.

\textbf{C. \textit{PREEMPTION ANALYSIS}}

With the number of governmental entities jumping on the right-to-know bandwagon increasing, and the entire hazard communication area becoming regulated by a growing number of differing laws and agencies, one obvious question arises: Can there be uniform regulation of this subject matter? One possible answer to this question lies in the field of pre-

\textsuperscript{45} See, \textit{e.g.}, Michigan, \textit{Mich. Comp. Laws Ann.} § 408.1011 (West 1985) (employees are permitted access to records of employee exposure to toxic substances or harmful physical agents and employee access is required to be monitored by law); and New Mexico, \textit{N.M. Stat. Ann.} § 50-9-11 (1978) (employees required to maintain accurate records regarding employee exposure to potentially toxic materials or harmful physical agents and to grant employees access to their own records).


emption. Does OSHA’s Hazard Communication Standard preempt any State or local law seeking to regulate right-to-know issue?

1. OPERATION OF THE OSHA STANDARD AND THE EFFECT OF HUGHEY AND AUCHTER

In promulgating the Hazard Communication Standard, OSHA itself recognized the inconsistent compliance requirements resulting from the wealth of state and local right-to-know laws.\(^{50}\) To alleviate this problem, OSHA explicitly provided for the preemption of state and local regulation of hazard communications between employer and employee.\(^{51}\) This preemption is intended "to reduce the burden on interstate commerce produced by conflicting state and local regulations and will ensure that all employees in the manufacturing sector are accorded the same degree of protection."\(^{52}\)

Under this provision any state or local right-to-know law will be preempted by the federal HCS—at least with respect to employees working in the manufacturing sector. Individual states may still regulate issues covered by OSHA standards, but only if the state’s plan is approved by OSHA.\(^{53}\) In order for OSHA to approve a state’s plan, its protections must be at least as comprehensive as those contained in the federal standards regulating the same issue.\(^{54}\) Still, OSHA has stated its reluctance to grant approval to individual state plans: "OSHA will examine carefully any state requests to regulate in this area to determine any potentially burdensome impact on interstate commerce as well as to ascertain whether there is a compelling need for a separate regulation."\(^{55}\)

It must be remembered, however, that individual states are free to exercise jurisdiction over any occupational safety or health issue where OSHA has not asserted its own jurisdiction (i.e., where no valid OSHA

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Several state and local right to know laws have been prescribed to deal with [the failure of the marketplace to correct] the problem. The coverage and requirements of these laws, however, are consistent only in their inconsistency. The consequent cost and ineffectiveness of this decentralized effort has been well documented in the public record . . .

This occupational safety and health standard is intended to address comprehensively the issue of evaluating and communicating chemical hazards to employees in the manufacturing sector, and to preempt any state law pertaining to the subject. Any state which desires to assume responsibility in this area may only do so under the provisions of Section 18 of the Occupational Safety and Health Act (29 U.S.C. § 651 et seq. [1982]) which deals with state jurisdiction and state plans.


54. 29 U.S.C. § 667(c).

standard is in effect). For example, individual states may legislate rules pertaining to community hazard communications, since the HCS does not regulate this area, or establish regulations protecting employees in the non-manufacturing sector. This "separate" jurisdictional authority creates the exact problem sought to be prevented by the HCS: The creation of a morass of different laws governing the same area, hazard communication. As a result, the need for extending the OSHA standard to cover all employers grows more evident.

The problems of preemption and separate jurisdiction have been examined in two recent decisions, both of which have held that the federal HCS preempts comparable state right-to-know laws, but only with respect to their regulation of the chemical manufacturing sector of the workforce.

In New Jersey State Chamber of Commerce v. Hughey, the United States District Court for the District of New Jersey reviewed the constitutionality of New Jersey's Right-to-Know Law, which is considered to be one of the most stringent State laws in the nation. The New Jersey law gave employees the right to obtain information about hazardous chemicals found in the workplace and imposed upon employers the duty to compile and periodically update comprehensive written information on all such chemicals, their storage, production, emissions, etc. Employers were also required to label hazardous chemicals and to conduct educational and training programs for the employees' benefit. Employers had two years from the effective date of the legislation to label all chemicals in the workplace, whether they were hazardous or not. More importantly, the New Jersey statute extended its coverage to employers in the non-manufacturing sector, as well as those in the manufacturing sector. Finally, employers had the additional duty to file a list of all hazardous chemicals with State and local health departments and with local fire and police departments; in other words, the law contained a community right-to-know provision.

57. The Macomb County, Michigan Community Right-to-Know law, referred to in note 55, supra, was held not to be preempted by the HCS. In Michigan State Chamber of Commerce v. Macomb County Board of Commissioners, et al., No. 85-CV-71844DT, the Michigan Chamber of Commerce attempted to enjoin enforcement of the community provision, but was denied. Relying upon the New Jersey District Court's Hughey decision, the District Court for the Eastern District of Michigan ruled that the Macomb County regulation fell within the perogative of State and local government. This decision is currently being appealed to the Sixth Circuit. Michigan County Regulation Challenged by Industry Group; Preemption Argued, 15 O.S.H. Rep. (BNA) No. 12 at 258, 259 (Aug. 22, 1985).
Analyzing the relationship between the New Jersey law and the Federal Hazard Communication Standard, the court noted that the State of New Jersey failed to submit its right-to-know plan to the Secretary of Labor for approval. Absent the federal approval required by the Occupational Safety and Health Act, the court held that the HCS preempted the New Jersey statute, due to the fact that the New Jersey statute covered the same issues as the federal standard. Since the HCS directly and exclusively dealt with employer-manufacturers, an OSHA-regulated area, the New Jersey Right-to-Know Law was entirely preempted—but only as it applied to employer-manufacturers. The court upheld the New Jersey law as it applied to non-manufacturing employees, an area not regulated by the HCS. Rejecting the plaintiff’s argument that OSHA’s exclusion of non-manufacturing employers in the HCS represented a deliberate choice by OSHA, the court held that “no OSHA communication standard is in effect for nonmanufacturing employers. Consequently, New Jersey is free to act as to those employers.” The lower Hughey court did not address the issue of whether its community right-to-know provisions were preempted by the HCS.

In United Steelworkers of America v. Auchter, various plaintiffs instituted an action challenging those provisions of the HCS which excluded non-manufacturing employees from its information disclosure protections. Although the Third Circuit concluded that the HCS preempted state right-to-know laws as they applied to the manufacturing sector employees, the court directed the Secretary of Labor to explain why the Hazard Communication Standard should only be limited to employees

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60. 29 U.S.C. 667(a) (1982).
62. The Third Circuit Court of Appeals found the District Court’s resolution of the preemption issue overbroad. N.J. State Chamber of Commerce v. Hughey, 774 F.2d 587 (3d Cir. 1985). The Appeals Court affirmed the earlier ruling preempting the New Jersey right-to-know law, but only as it purported to regulate hazard communication to employees in the manufacturing sector. 774 F.2d 587, 592. With respect to community disclosure, the court found OSHA without authority to preempt:

The Secretary has authority to promulgate standards only as to occupational safety and health and those standards cannot have preemptive effect beyond that field. Indeed, the Secretary argued in Steelworkers [supra at note 58] that the Hazard Communication Standard should not preempt state laws addressing “general environmental problems originating in the workplace, but whose effects are outside it . . .”

774 F.2d 587, 593 (emphasis added).

Thus, the New Jersey Act was held not preempted as it applied to the community right-to-know aspects of the New Jersey Act, even as it would affect manufacturing sector employers; the New Jersey Act in this respect was severable, and continued in effect. 774 F.2d 587, 598.

63. Id. at 621.
64. Id.
65. 763 F.2d 728 (3rd Cir. 1985).
66. Plaintiffs in the action included the states of Connecticut, Illinois, Massachusetts, New Jersey and New York, the United Steelworkers of America and Public Citizen, Inc.
in the manufacturing sector.\textsuperscript{67} The court indicated that if the Secretary failed to adequately justify this position, it would direct extension of the standard to all employers. The court did not conclude that the HCS Standard preempted those portions of state laws which extend coverage beyond the manufacturing sector, nor did it address the question of federal preemption of community right-to-know provisions.

Both the Hughey and Aucht\textsuperscript{er} decisions indicate that the HCS is a standard which entirely preempts state laws which relate to chemical manufacturers, but that states are free to expand hazard communication protection to employees working in other sectors of the economy. This expansion will create the same problems that the HCS was originally intended to remedy: numerous state laws whose primary consistency is their inconsistency. However, until OSHA acts in this respect, the state laws will stand.\textsuperscript{68}

Perhaps recognizing this potential, and/or acting upon the Aucht\textsuperscript{er} court's direction, the Department of Labor has decided to open a public comment period for addressing the issue of extending the provisions of the HCS to all employers.\textsuperscript{69}

2. \textit{Importance of the Preemption Issue for Trucking Employers}

Considering the recent activity of the courts, various state and local governments and the Department of Labor itself, extension of the HCS to all employers is inevitable—if not desirable. However, if the standard is extended to all employers in its current form, the trucking industry would be required to comply with the same communication standards that now regulate manufacturers in the chemical industry. This would require trucking industry employers to label hazardous chemicals, conduct informational and training programs for their employees and provide employees with access to material safety data sheets.\textsuperscript{70}

As discussed previously, the logistics of complying with the HCS make its application to the trucking industry extremely costly if not completely unfeasible. The standard’s record keeping and administrative burdens alone exemplify these concerns. OSHA has also indicated that the scope of the training requirement is intended to be quite broad. Beyond

\textsuperscript{67} 763 F.2d 728, 736.
\textsuperscript{68} 29 U.S.C. \S\ 657(a) (1982) provides that “[n]othing in this Act shall prevent any state agency or court from asserting jurisdiction under state law over any occupational safety or health issue with respect to which no standard is in effect under section 6 [29 U.S.C. \S\ 655].
\textsuperscript{69} See \textit{supra} note 35 and accompanying text.
\textsuperscript{70} The International Brotherhood of Teamsters has publicly supported the extension of the HCS to all employers, arguing that individual state laws extending right-to-know protection to non-manufacturing sector employees should be supported in the absence of federal protections. \textit{Teamsters Union Initiates Second Attempt for NACOSH Support of State Law Protections}, 15 O.S.H. REP. (BNA) No. 7 at 107 (July 18, 1985).
simply providing employees with written information, OSHA has stated
that employers should use additional training methods such as audio-vis-
ual programs, classroom instruction, videos, and training workshops with
management, which would include an opportunity for questions and an-
swers.\footnote{OSHA Issues Revised Version of Guidelines for Enforcing Hazard Communication Stan-
dard, 14 O.S.H. Rep. (BNA) No. 46 at 918 (April 25, 1985).} When these points are considered with the fact that compliance
costs are already expected to exceed original OSHA estimates,\footnote{Compliance with Federal Standard Could Exceed OSHA Estimates, Meeting Told, 14 O.S.H. Rep. (BNA) No. 35 at 701 (Feb. 7, 1985).} the
need for some type of modification of the existing standard becomes
readily apparent—at least with respect to its application to the trucking
industry. Absent any such reforms and given a broad application of the
HCS, the difficulties now being experienced are miniscule compared to
those to be expected in the future.

These concerns with federal compliance, however, are only the tip of
a regulatory iceberg. Trucking industry employers, in the absence of a
uniform federal standard, may be forced to comply with a vast number of
differing state and local right-to-know provisions. Given the interstate
nature of the trucking industry, the burden of complying with a different law
in every state—and quite possibly, every community—would be an exer-
cise in logistical gymnastics. As a result, the issue of federal preemption
of state and local laws is of critical importance.

Not only is preemption a critical issue with respect to the actual re-
quirements of the HCS, but it is also of vital concern when potential em-
ployee remedies are considered. Under the HCS, an employee is limited
to the remedies available under Section 11(c) (reinstatement and
backpay) and is also subject to the "reasonable apprehension of death or
serious bodily harm" requirements of the Whirlpool decision.\footnote{See supra note 22 and accompanying text.} Trucking
industry employers would also be subject to other general enforcement
provisions of OSHA.\footnote{See, e.g., 29 U.S.C. § 658(a) (1982), which authorizes the Secretary, or his representa-
tive, to issue citations to an employer when a violation of an OSHA standard has occurred, and
29 U.S.C. § 659(b) (1982), which authorizes the imposition of penalties for failure to correct a
violation for which a citation has been issued. The various penalties for violations of OSHA re-

Thus, assuming employees are not afforded the additional remedies
of Section 405 of the Surface Transportation Act\footnote{See supra Section I(C)(2).} for exercising rights
under the HCS, only the traditional OSHA remedies would be available.
However, if the various state right-to-know laws are not preempted, addi-
tional remedies may be available to employees and employers may be
subjected to even more stringent sanctions. Unless there is a uniform federal standard preemption state and local regulation of the right-to-know issue, trucking industry employers will be subjected to a patchwork of varying substantive, procedural and remedial requirements.

III. PREEMPTION OF THE HCS BY OTHER REGULATORY AGENCIES

The right-to-know issue is not resolved by merely examining OSHA preemption of state and local laws. Even assuming OSHA extends the HCS to all employers, therefore preempting any state law seeking to govern the issue, the trucking industry has another hurdle to overcome: Department of Transportation preemption. Under a provision of the Occupational Safety and Health Act, Section 4(b)(1), Department of Labor jurisdiction over a matter may be preempted by other federal agencies.

While such a provision would appear to exclude OSHA from areas subject to regulation by the Department of Transportation, additional factors must be considered. As will be discussed more fully in a later section, the DOT’s preemptive authority over state law is not as strong as OSHA’s. Thus, DOT assumption of authority over this matter could still subject trucking industry employers to more stringent state laws in right-to-know areas actually regulated by the DOT. However, in areas not actually regulated by the Department of Transportation, OSHA standards would apply. As a result, trucking industry employers could be required to comply with a mass of DOT, OSHA, state and local regulations, depending upon the employee involved, the nature of the work performed, the area regulated and the nature of the regulation.

The scope of § 4(b)(1) and the relationship between OSHA regulations and those of other governmental agencies has been defined by the courts. For example, in Southern Railway Co. v. OSHA, the Fourth Circuit held that OSHA’s regulative authority extended to employees generally covered by the Federal Railway Safety Act, since the Federal Railway Administration had not exercised its authority to regulate the area of employee safety sought to be governed by OSHA. Where such authority

76. See, e.g., Illinois Toxic Substance Disclosure Act, ILL. REV. STAT., ch. 48, § 1417(17)(e) (Smith-Hurd Supp. 1985), providing for punitive damages of up to $20,000 per violation to be imposed on employers who “knowingly and wilfully” violate the Act.

77. “Nothing in this Act shall apply to working conditions of employees with respect to which other Federal agencies . . . exercise statutory authority to prescribe or enforce standards or regulations affecting occupational safety and health.” 29 U.S.C. § 653(b)(1) (1982).


79. See, e.g., Consolidated Freights Worp., 5 O.S.H. Cas. (BNA) 1481, 1482 (1977) (Section 4(b)(1) interpreted to exempt from coverage of the Act only those working conditions that are actually subject to regulation by a sister agency).

remains unused, the court found § 4(b)(1) inapplicable.81

The exclusion of OSHA authority under § 4(b)(1) was further examined in Southern Pacific Transportation Co. v. Ussery.82 In this case, the Fifth Circuit restricted OSHA's authority to regulate areas not already regulated by another government agency, holding that an agency need not "encompass every detail" of the OSHA provision in order to displace an OSHA standard. Instead, another agency's "comprehensive" treatment of a general problem regulated by an OSHA standard would be sufficient to exclude OSHA from regulation of that condition.83

"Industry-wide" exemptions, however, are not granted, nor was § 4(b)(1) intended to establish industry-wide exemptions for industries otherwise regulated by the federal government.84 Also defining the scope of § 4(b)(1), the Occupational Safety and Health Review Commission in Mushroom Transp. Co.85 stated that, "§ 4(b)(1) does not require that another agency exercise its authority in the same manner or in an equally stringent manner."86 In Herman Forwarding Company,87 OSHA issued a citation against an employer whose employees charged that they were required to handle leaking bags of hazardous materials. The citation involved violations of various OSHA standards relating to respirators, but the employer argued that the DOT hazardous substance, loading and broken container regulations already governed the matter, thereby exempting it from the OSHA standards. Finding the employer exempt from OSHA regulation under the above circumstances, the Review Commission set forth a three-part test to determine whether the OSHA exemption is operative: the agency (other than the Labor Department) must have statutory authority to regulate the specific working conditions; the other agency must exercise that authority; and the enabling statute under which

81. The court articulated the following reason for so limiting the § 4(b)(1) exclusion:
While § 4(b)(1) may not be entirely self-defining, it is clear that the exemption applies only where another federal agency has actually exercised its authority. It does not apply where such an agency has regulatory authority but has failed to use it. This is clear not only from the statutory language but from the legislative history as well. Earlier versions of the legislation had provided that the mere existence of statutory authority in another federal agency was sufficient to invoke the exemption, but they were rejected by Congress.
539 F.2d 335, 336.
82. 539 F.2d 386 (5th Cir. 1976), cert. denied 429 U.S. 999 (1976).
83. 539 F.2d 386, 391.
84. Id. at 390. See also, Lee Way Motor Freight, Inc., 4 O.S.H. Cas. (BNA) 1968, 1969 (1977) (Section 4(b)(1) does not exempt entire industries from its coverage); O'Boyle Tank Lines, Inc., 9 O.S.H. Cas. (BNA) 2000, 2002 (1981) (all working conditions in an industry are not exempt under Section 4(b)(1) merely because another federal agency has adopted standards or regulations covering some working conditions in the industry).
85. 1 O.S.H. Cas. (BNA) 1390, 1392 (1973).
86. Id.
87. 3 O.S.H. Cas. (BNA) 1253 (1975).
the other agency regulates that working condition must purport to assure
safe and healthful working conditions for employees.88

Thus, before it can be determined whether the HCS would protect the
rights of any particular trucking industry employee in any given situation, it
must first be determined whether the Department of Transportation has
issued regulations governing the hazard communication area. With re-
spect to the application of the HCS to the trucking industry and the exclu-
sion of § 4(b)(1), the DOT has affirmatively exercised its authority to
regulate matters relating to the transportation of hazardous materials.89
However, both the scope and purpose of this regulation create some very
serious questions. The Hazardous Materials Transportation Act
("HMTA"),90 which governs this area, was enacted "to protect the nation
adequately against the risks to life and property which are inherent in the
transportation of hazardous materials in commerce."91 Its original intent
was not that of hazardous communication to employees, but rather, en-
suring the safe passage of hazardous materials through commerce.
Under the HMTA, the Secretary of Transportation is authorized to issue
"regulations for the safe transportation in commerce of hazardous
materials."92

Clearly, the DOT has exercised its regulative authority as applied to
the transportation of hazardous materials and the regulations it has
promulgated in this regard have numerous "communicative" aspects.93
However, it is not clear whether those provisions regulate, for example,
the presence of hazardous substance on a loading dock, and whether a
dock worker would have the "right-to-know."94 Questions also arise

88. Id. at 1254.
89. See, e.g., 49 C.F.R. §§ 170-189 (1985), which will be discussed in more detail in Sec-
tion IV, infra.
91. Id.
92. 49 U.S.C. app. § 1804 (1982). Any such regulations issued by the Secretary are to be
applicable to:
[A]ny person who transports, or causes to be transported or shipped, a hazardous
material, or who manufactures, fabricates, marks, maintains, reconditions, repairs, or
tests a package or container which is represented, marked, certified, or sold by such
person for use in the transportation in commerce of certain hazardous materials.
Id. (emphasis added). § 1804 further provides that
such regulations may govern any safety aspect of the transportation of hazardous
materials which the Secretary deems necessary or appropriate, including, but not lim-
ited to, the packing, repacking, handling, labelling, marking, placarding, and routing of
hazardous materials, and the manufacture, fabrication, marking, maintenance, recondi-
tioning, repairing, or testing of a package or container which is represented, marked,
certified, or sold by such person for use in the transportation of certain hazardous
materials.
(emphasis added).
94. For example, in Chief Freight Lines, Inc., 3 O.S.H. CAS. (BNA) 2083 (1976), the Review
whether drivers themselves are entitled to additional information about the materials they transport.

Interestingly, OSHA addressed the dual jurisdiction of the DOT and the DOL in the labeling requirement of the present Hazard Communication Standard. Yet, instead of simply not regulating the "labeling" issue because of preexisting DOT regulations, as § 4(b)(1) might suggest, OSHA mandated that all labels must be consistent with DOT requirements.95

Recognizing the similar results of regulations promulgated for different purposes, OSHA avoids conflict with the existing, and arguably preemptive DOT regulations by impliedly adopting them.96 A similar approach could be taken with respect to the entire area of hazard communication and its relationship to DOT requirements and employers in the transportation industry.

IV. EXISTING DEPARTMENT OF TRANSPORTATION PROCEDURES RELATING TO AN EMPLOYEE'S RIGHT-TO-KNOW

Having discussed the relationship between OSHA standards and existing DOT regulations, it is important to examine just what, if any, DOT regulations govern those areas envisioned by the HCS, therefore excluding OSHA from regulating that area. Existing Department of Transportation regulations, enacted pursuant to the Hazardous Materials Transportation Act, regulate the packaging, labeling, documenting and vehicle placarding of hazardous materials transported in commerce.97 These regulations parallel the requirements of the HCS in many ways.

Commission refused to apply the Section 4(b)(1) exemption to employees working on the dock of a trucking facility, concluding that the DOT had not acted to regulate the working conditions of freight handlers. 95. 29 C.F.R. § 1910.1200(f)(2) (1985):

Chemical manufacturers, importers, or distributors shall insure that each container of hazardous chemicals leaving the workplace is labelled, tagged, or marked in accordance with this section in a manner which does not conflict with the requirements of the Hazardous Materials Transportation Act (18 U.S.C. 180 et seq.) and regulations issued under that act by the Department of Transportation.

(Emphasis added). The legislative history of the HCS further illustrates OSHA's recognition of existing DOT regulations:

No explicit exclusion [in the HCS] is provided for substances regulated by the [DOT] under the [HMTA]. This standard is directed towards hazard communication within the workplaces of covered employers ... whereas the [DOT] regulations are directed toward the packaging and labeling of hazardous materials while they are being transported in commerce. Therefore, although both sets of requirements apply to many, if not all, of the same substances, there should be no unnecessary duplication of regulatory effort.


96. OSHA has indicated, however, that DOT labeling requirements will not suffice for purposes of hazard communication. See supra note 10 and accompanying text.

A. LABELING

Both the DOT regulations and the HCS provide for labeling. Under the HCS, chemical manufacturers, importers or distributors must label containers of hazardous materials with information concerning the identity of the hazardous chemicals, appropriate hazard warnings, and the name and address of the chemical manufacturer, importer or other responsible party. The HCS further provides that the labels or warnings used must not conflict with any DOT labeling requirements.

DOT labeling regulations, on the other hand, are much more extensive, requiring not only the above information, but also requiring, among other things, hazard identification numbers, placards, color codes, special placement and a requirement that they be affixed to a background of contrasting color.

B. SUBSTANCE INFORMATION

Although there is no precise counterpart in the DOT regulations for the HCS requirement of Material Safety Data Sheets, existing provisions regarding labeling and shipping papers, and the availability of Emergency Response Guidebooks (ERG) and the Chemical Transportation Emergency Center (CHEMTREC), provide employees with information pertaining to the hazardous substances present in their work environment.

Under the HCS, employees are provided with information on substances present in the workplace, including the identity of the chemicals, physical and chemical characteristics of the hazardous chemicals, physical hazards associated with the substance, and health hazards of the chemical.

In contrast, under the requirements of the HMTA, "each person who offers a hazardous material for transportation shall describe the hazardous material on the shipping papers in the manner required by this subpart." The description required by this section is composed of the proper shipping name of the material, the hazard class, i.e., key words identifying hazards, the quantity of the hazardous materials shipped, and the name of the shipper. However, the above DOT regulations provide information primarily relating to the physical hazards of the materials

100. These requirements are all set forth in 49 C.F.R. § 172 (1984), the regulations for hazardous materials communication.
103. Id.
(e.g., flammable or corrosive properties), as opposed to the health hazards required to be described under the HCS.

Additional information regarding hazardous substances in the workplace is available through the use of CHEMTREC and the Emergency Response Guidebook. CHEMTREC, a public service of the Manufacturing Chemist Association, provides particularized 24-hour, toll-free information on hazardous substances in the event of a major accident or spill. CHEMTREC will also "network" information, contacting the shipper of the substance for detailed assistance and follow-up procedures.

In addition to the immediate information available through CHEMTREC, hazard information is also available in the Emergency Response Guidebook (ERG). The ERG is a DOT publication\(^{104}\) which provides information critical to the identification of the hazards of various substances and the proper administration of first aid. The ERG uses the DOT's numerical hazard identification system and references it into easily understandable information pertaining to: "health hazards," "fire and explosions," "spill or leaks," and "first aid." The use of the ERG, however, is not mandated by a specific DOT regulation.

C. TRAINING

Comparable to the distinction between the DOT regulations and the HCS with regard to employee information are the differences pertaining to employee training. The HCS requires employers to "provide employees with information and training on hazardous chemicals in their work area at the time of their initial assignment and whenever a new hazard is introduced into their work area."\(^{105}\) Under the information provision of the HCS, employees must be apprised of the requirements of the standard, any operations in the workplace where hazardous chemicals are present, and the location and availability of written hazard communication materials.\(^{106}\) The training provision of the standard calls for instruction regarding the methods available for the detection of hazardous materials in the workplace, the physical and health hazards of the chemicals in the work area, and the measures employees can take to protect themselves from the hazards.\(^{107}\)

Under existing DOT regulations, before a driver can be certified, he or she must pass a written examination which requires knowledge of the information contained in the hazardous materials regulations\(^{108}\) when the

\(^{104}\) 5800.2.
\(^{106}\) 29 C.F.R. § 1910.1200(h)(1).
\(^{107}\) 49 C.F.R. § 1910.1200(h)(2).
driver will be transporting hazardous materials.\textsuperscript{109} DOT regulations also require instruction for any drivers transporting a flammable cryogenic liquid.\textsuperscript{110}

In addition, drivers of trucks transporting radioactive materials are required to receive, every two years, training with regard to general procedures for radioactive material, the properties and hazards of the radioactive materials being transported, and accident procedures.

The above materials provide only a summary of existing DOT regulations and a comparison of their provisions with those of the HCS. Given the clear intent not to grant industry-wide exemptions under § 4(b)(1), it is unlikely that it can be argued that the DOT has already successfully regulated this issue, especially in view of the purpose of the DOT regulations and portions of the regulations themselves. Considering the exhaustive requirements of the HCS, in many areas the DOT regulations would likely be deemed insufficient, if not nonexistent. The result is a patchwork of DOT and OSHA regulations governing the right-to-know.

V. DEPARTMENT OF TRANSPORTATION PREEMPTION OF STATE LAWS

Assuming OSHA would grant the trucking industry an exemption to the requirements of the HCS, due to the presence of similar DOT regulations, another problem would still be present: Preemption of state laws seeking to regulate the right-to-know area. As discussed previously, OSHA's preemptive powers are quite strong. In fact, as the court in 
\textit{Auchter} stated, with respect to state right-to-know laws in the manufacturing sector, they are preempted \textit{in their entirety} by the HCS.\textsuperscript{111} A question remains as to whether the DOT's preemptive powers are this strong. In other words, if the DOT assumes regulation of the right-to-know issue, will trucking industry employers still be faced with a plethora of state and local regulations? The current status of the law would indicate that this is a distinct possibility.

Section 1811 of the Hazardous Materials Transportation Act sets forth the preemptive powers of the Department of Transportation with respect to hazardous substance regulation: "Except as provided in subsection (b) of this section, any requirement, of a state or political subdivision thereof, which is inconsistent with any requirements set forth

\textsuperscript{109} 49 C.F.R. § 391.35(e) (1985).
\textsuperscript{110} Such instruction must include information regarding:
1. The properties and potential hazards of the particular material to be transported;
2. The safe operation of the vehicle;
3. Procedures to be followed in case of accident or other emergency; and
\textsuperscript{111} See \textit{supra} notes 65-67 and accompanying text.
in this title, or in a regulation issued under this title, is preempted."\footnote{112} In other words, unlike OSHA, in which the mere presence of an OSHA regulation will preempt all other regulations on that matter, in order for a DOT regulation to preempt a state requirement, there must be a finding that the state regulation is "inconsistent" with the federal standard. Are more stringent state laws "inconsistent" with a federal standard governing the same issue?

This question is resolved, in part, by the provisions of the statute itself. Section 1811(b) of the Hazardous Materials Transportation Act provides that such a state regulation, if it affords an equal or greater level of protection compared to the federal counterpart and "does not unreasonably burden commerce," is not preempted.\footnote{113}

Section 1811(b) therefore establishes a balancing test in which a state regulation deemed to be inconsistent may nevertheless be exempted from preemption.\footnote{114} As a result, all consistent and exempted inconsistent state laws will remain in effect. In addition, while the exemption determination under subsection (b) is expressly delegated to the DOT, it has been held that questions of inconsistency under subsection (a) may be resolved by the courts, as well as by the DOT.\footnote{115}

In order to more fully understand the scope of the DOT's preemptive powers, it is necessary to review prior case law examining those powers. Upholding a preliminary injunction enjoining the State of Rhode Island from enforcing certain rules pertaining to the transportation of liquid energy gases, the First Circuit Court of Appeals in National Tank Truck Carriers v. Burke\footnote{116} found that "the word 'inconsistent' in the Act's preemption clause implies that the state laws which merely vary from federal law—as opposed to those which conflict with federal law—are not preempted."\footnote{117}

However, the court further stated that the legislative history of the Hazardous Materials Transportation Act also suggests that the primary congressional purpose was to secure a general pattern of uniform national regulations and "to preclude a multiplicity of state and local regulations

\footnote{113}49 U.S.C. app. § 1811(b) (1982) (emphasis added):
   Any requirement, of a state or political subdivision thereof, which is not inconsistent with any requirement set forth in this title, . . . is not preempted if, . . . the Secretary determines . . . that such requirement (1) affords an equal or greater level of protection to the public than is afforded by the requirement of this title, and (2) does not unreasonably burden commerce.
\footnote{114}National Tank Truck Carriers v. Burke, 608 F.2d 819 (1st Cir. 1979). According to the legislative history of the HMTA, § 1811(b) was enacted to allow state laws to govern in "certain exceptional circumstances" necessitating immediate action. S. Rep. No. 1192, 93rd Cong., 2d Sess. 37, 38 (1974).
\footnote{115}National Tank Truck Carriers, 608 F.2d 819, 822.
\footnote{116}608 F.2d 819 (1st Cir. 1979).
\footnote{117}Id. at 823, 824.
and potential for varying as well as conflicting regulations in the area of hazard materials transportation." \(^{118}\) The court further recognized that the preempted State standards' additional requirements might indeed conflict with federal regulations, if the federal regulations were to be construed as embodying a balancing of competing interests. \(^{119}\)

Later, in *National Tank Truck Carriers v. City of New York*, \(^{120}\) the Second Circuit upheld a New York City regulation prohibiting the transportation of hazardous gases by tank truck within the City of New York. The ruling turned upon the court's determination that the State regulations were entirely "consistent" with and in furtherance of the federal regulations and the underlying purpose of the federal provisions: "to protect against the risks to life and property from the transportation of hazardous materials." \(^{121}\) Rejecting the argument that the local regulation should be preempted under § 1811(a), the court found that the State regulation was not inconsistent with the federal requirement with the meaning of § 1811(a), since compliance with the State regulation did not render concurrent compliance with the federal regulation an impossibility. \(^{122}\) The court further held that the local regulations did not stand as an obstacle to the accomplishment and execution of the full purposes and objectives of Congress. \(^{123}\)

The scope of DOT authority was further examined in *City of New York v. U.S. Dept. of Transp.* \(^{124}\) Reviewing the validity of a routing regulation promulgated under the HMTA and challenged by the City of New York, the Second Circuit Court of Appeals was required to analyze the purpose and intent underlying § 1811. Regarding DOT preemption of inconsistent state laws, the Court stated that "Congress included [§ 1811(a)] 'to preclude a multiplicity of state and local regulations and the potential for varying as well as conflicting regulations in the area of hazardous materials transportation.'" \(^{125}\) The Court further said that:

To ameliorate the sweep of Section 1129a, Congress wrote into HMTA a procedure whereby local jurisdictions could apply for non-preemption rulings for their own regulations . . . . This non-preemption procedure [of § 1811(b)] was added to the HMTA so that in "certain exceptional circumstances" DOT could limit the preemptive force of federal regulations "to se-

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118. *id.* at 824 (citing Senate Committee on Commerce, Report No. 93-1192, September 30, 1974).

119. *id.*

120. 677 F.2d 270 (2nd Cir. 1982).

121. *id.* at 274, 275.

122. *id.* at 275.

123. *id.*

124. 715 F.2d 732 (2nd Cir. 1983).

125. 715 F.2d at 740 (citing S. REP. No. 1192, 93rd Cong., 2nd Sess. 37 (1974)). (Citations omitted).
cure more stringent regulations" by local authorities.126
In concluding its disposition of the case, the court stated, "'[n framing
HMTA, Congress decided that federal regulations would presumptively
preempt inconsistent local regulations and that the local authorities would
then have the burden of demonstrating to DOT that their local regulations
provided greater safety without burdening interstate commerce."127
Thus, while it would appear that the DOT favors uniformity, it is by no
means averse to allowing the passage of more strict state and local
laws128—especially if they do not impose a great burden on commerce.
Tangentially related to the issue of the federal preemption of state
laws under § 1811 of the HMTA, and similarly indicative of the court’s
recognition of Congressional intent to establish uniformity in the regulation
of the transportation of hazardous materials, is the court’s invocation of
the doctrine of primary jurisdiction when an action is brought under the
Hazardous Materials Transportation Act. For example, in Kappelmann v.
Delta Air Lines, Inc.129 the court refused to issue injunctive relief under the
Hazardous Materials Transportation Act, finding that the issue was more
properly one to be decided by the Secretary of Transportation—given
congressional intent to consolidate authority into one agency in order to
promote uniformity of regulation.130
All of the above cases lead to two conclusions. First, it is clear that
the DOT regulations and its preemptive powers are intended to ensure a
uniform body of regulations in the transportation industry. However, it ap-
pears equally as clear that the federal regulations are only to be a mini-
mum—if a state can prove that its more stringent regulations do not
impede interstate commerce. As a result, placing right-to-know regulation
into the hands of the Department of Transportation exposes the truck-
ing industry to one great risk—that the numerous states now passing
more stringent laws will be granted non-preemption under § 1811(b),
thereby returning trucking employers to their original dilemma—having to
deal with the vast body of state and local right-to-know legislation. The
only possible solution to this problem would be for the DOT to promulgate

126. Id.
127. Id. at 752.
128. See, e.g., 49 C.F.R. § 390.30 (1985), which provides that the provisions of the Federal
Motor Carrier Safety Regulations are not intended to preclude states or subdivisions thereof from
establishing or enforcing state or local laws relating to safety, the compliance with which would
not prevent full compliance with the DOT regulations.
129. 539 F.2d 165 (D.C. Cir. 1976).
130. Id. at 170. See also, Consolidated Rail Corp. v. City of Dover, 450 F. Supp. 966 (D. Del.
1978), in which the court refused to enjoin the "marshalling, storing and switching of [railroad]
cars containing hazardous freight and toxic chemicals," in a state court nuisance action. The
court found that the regulation of the transportation of hazardous materials was properly within
the authority of the Secretary of Transportation.
a separate "inconsistency" regulation, declaring all state right-to-know laws inconsistent. 131

VI. THE RIGHT-TO-KNOW: A PROPOSED UNIFORM FEDERAL STANDARD

Prior to August 20, 1985, the extension of the Hazard Communication Standard to all employers was speculative, albeit inevitable. Now, however, extension is certain. 132 The Assistant Secretary of Labor, recognizing there may be "problem areas" in expanding the standard to all employers, has asked for recommendations on how to best accomplish this task. 133 This section, with all of the considerations previously discussed in mind, is intended to present a proposed position with regard to the hazard communication issue.

The goals of hazard communication would be most effectively achieved if OSHA regulates the right-to-know issue, but only if the present HCS is modified to recognize certain existing practices, especially given the difficulties of complying with the HCS in its present state. The purpose of the HCS, hazard communication, is quite different from the purpose of the DOT regulations, assuring the safe transportation of hazardous materials in commerce, although both regulations use similar means to achieve different goals. This fact, already recognized by OSHA, would allow OSHA to evade the preemptive provisions of § 4(b)(1), much like it did when it dealt with labeling requirements.

However, just as it recognized that existing DOT labeling requirements are sufficient to satisfy the communicative purpose of the HCS, OSHA should recognize that many other existing procedures under the DOT regulations are sufficient to satisfy the provisions of the HCS. For example, certain training requirements already exist under the DOT regulations; they may only need slight modification to ensure that the purposes of the HCS are satisfied. In a similar fashion, the DOT's Emergency Response Guidebook not only provides employees with information paralleling that required to be found in an MSDS, but it would also resolve the logistical problem of having to maintain vast file banks of data sheets and continually having to update hazardous substance lists. As a result, the purpose of the HCS could easily be satisfied by many procedures originally established to ensure safety in another area.

If OSHA takes full responsibility for regulating hazard communication in the trucking industry, the industry will be relieved of one potentially

131. See, e.g., 49 C.F.R. § 177 (1984), Appendix A, wherein the DOT declares particular aspects of state routing requirements "inconsistent" with its regulation.


133. Id.
costly problem: attempting to comply with scores of differing, more stringent state and local right-to-know laws will be preempted in their entirety—something that DOT regulation could not guarantee. It must also be recognized that simply arguing that DOT preempts OSHA in this matter may not extricate the trucking industry from OSHA jurisdiction. The HCS may still apply to employees not subject to DOT regulations (e.g., dock workers) and to areas not regulated by existing DOT rules (e.g., material safety data sheets). This could result in trucking industry employers still having to deal with the logistical and costly problems related to material safety data sheets and other existing HCS requirements.

When considering this position, it is important to recognize the "downside" of OSHA regulation. First, it is clear that all employers will have to adopt the use of the ERG and possibly implement additional, minor training requirements. Furthermore, employees exercising hazard communication rights would be afforded Section 11(c) remedies—but they still would be held to the existing "reasonable person" standards for refusing to perform work (unlike current laws in some states which allow an employee to refuse to handle hazardous substances until hazard information is obtained). Similarly, employers would be required to be in compliance with these standards in the event of an OSHA inspection, but this, again, is nothing new or exceedingly burdensome, especially if OSHA can be convinced to adopt many existing DOT procedures. Overall, the fallout to be expected from the passage of a trucking industry standard would not be that great—particularly if the industry will be relieved of the ominous state law problem.

Another facially attractive alternative would be to argue for the exemption of the trucking industry from the OSHA standard. Such an argument, however, would realistically have to coincide with an expansion of DOT regulation in this area. One such area would be the codification of the ERG requirement in the existing regulations. It may also require expansion of DOT regulation to all employees working in the transportation industry. In addition, while such DOT regulation may allow employers to escape the 11(c) remedial provisions of the Occupational Safety and Health Act, it could inevitably lead to the actual expansion or more liberal interpretation of the scope of Section 405 of the Surface Transportation Act—the DOT’s remedial arm. The ramifications of such an expansion are severe: potential remedies and procedures available under Section 405 are much more broad and are much more burdensome than those available under Section 11(c).

DOT preemption of state law is also not as clear cut as that of OSHA. If the DOT exercised jurisdiction in this area, there is no guarantee that more stringent state laws would not remain in full force and effect. Similarly, absent a DOT regulation defining an "inconsistent" state rule, 50 or
more potential "consistency" rulings may result. The effect of not only the prospect of consistent state and local laws, but also inconsistent, exempted state and local laws must be considered. Even if many State laws might otherwise be deemed "inconsistent," if their standards were equal to or greater than those of the HCS, and no undue burden was placed upon commerce, an exemption would be granted. Under the HCS, states would have to submit their individual plans to OSHA for approval, and OSHA has already expressed its reluctance to grant approval to more stringent, differing state laws. Thus, the DOT exercise of authority in this area would leave the entire preemption issue unresolved.

Considering these factors, it appears that a well-drafted OSHA regulation applying the Hazard Communication Standard to the trucking industry is the most desirable option to solve the many thorny problems addressed in this article. Such an approach best accomplishes the desirable goals of HCS without excessively burdening trucking employers.