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THE SECRETARY OF TRANSPORTATION  
WASHINGTON, D.C. 20590

DEC 15 1978

MEMORANDUM FOR THE PRESIDENT

THROUGH: Mr. Rick Hutcheson  
Staff Secretary

SUBJECT: Surface Transportation Deregulation

With this memorandum, I submit papers describing options for the deregulation of the rail and truck industries.

In preparing these papers, we have engaged in an extensive consultation process with every affected group -- truckers, railroads, large and small shippers, labor, farm groups, investors, State government representatives, and others. These meetings were also attended by representatives of other executive departments and by key Congressional staff. With respect to rail, we have held a series of meetings around the country to discuss the preliminary legislative recommendations contained in our report entitled A Prospectus for Change in the Freight Railroad Industry.

As a result of this process, we believe we now have an understanding of where changes are needed in the current system and how proposals for change are likely to be received. Additional meetings are yet to be held, however, with utility companies, port authorities and others. The first phase of this consultative process will end on December 19. Shortly after that time I will send you a summary of the opinions heard in that process. Our next step will be to incorporate these comments into the options contained in this package and make recommendations to you.

The rail paper is the result of a zero-based look at the current regulatory system. We are proposing sweeping changes in railroad regulatory legislation. They would result in a coherent, economical, efficient, but more limited system. Some of the options discussed in the attachments propose total deregulation. Other options, although also designed to provide significant change, nonetheless permit considerable regulatory control. We have learned in preparing these options that it is very difficult to have just a little regulation.

We can expect two major sources of opposition to the rail proposals: labor will seek protection from the potentially adverse effects of abandonments and mergers; and many shippers will seek to continue rate regulation by raising the emotional captive shipper argument. I believe, however, that we can present the benefits of our proposals -- less bureaucracy, less waste, less subsidy -- in a bold and imaginative way. While not underestimating the political difficulties, I am convinced that we have the opportunity to persuade the Congress and the country of the need for innovation and change.

The truck paper presents three generally framed options for legislation, ranging from total deregulation, phased in over a transition period, to legislative consolidation of ICC reforms. DOT was the lead agency in an interagency task force effort to develop this paper. To the extent possible, the paper incorporates the view of all the participating members of the task force, indicates the pros and cons of each option, and includes a description of the anticipated opposition to truck deregulation.

I recommend a parallel approach to the rail and truck industries. The two modes compete in many markets and reforms in one industry will have an impact on the other. This approach will prevent severe competitive inequities from immediately confronting the railroads and avoid shifting inequities from one mode to another. By eliminating similar restrictions on both industries, we also expect to enlarge the areas of intermodal competition, thereby multiplying the benefits of the program.

Currently, nearly every facet of rail operations is regulated by the ICC, about 40 percent of the trucking industry is regulated, and only about 10 percent of the barge industry. The rail legislation will remove restrictions that have inhibited the railroads from competing with less regulated or unregulated truckers and that have caused a substantial loss of rail traffic.

Trucking legislation and rail legislation are extensively linked as shown by the following examples:

First, as the rail legislation would give the railroads more rate flexibility, the truck legislation would give trucks additional entry and rate freedom to compete with the railroads. This intermodal competition should keep rates competitive and offer shippers greater rate/service options.

Second, to the extent the rail legislation would allow more abandonments, the truck legislation would provide the entry and rate freedoms that can provide service to areas where rail abandonments occur.

If there is a choice as to which legislation should proceed first, it should be the rail legislation. The railroads are in great difficulty, and to proceed with trucking legislation alone would exacerbate the inequities mentioned above and put the railroads at an even greater disadvantage vis-a-vis the trucks. This would lead to either more railroad bankruptcies or greater and greater Federal subsidies.



Brock Adams

TRANSPORTATION REGULATORY REFORM

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## EXECUTIVE SUMMARY

The Department of Transportation bases its rail regulatory proposals on four premises:

There is a fundamental crisis in the rail industry that could paralyze the system by 1985;

This crisis can and should be solved in the private sector;

Absent changes in government and private sector policies, the Federal Government could be forced to spend at least \$20 billion to perpetuate an inefficient system; and

Deregulation is the essential first step in a private sector solution.

In 1976, the railroads carried 35.3% of all ton-miles of freight carried in this country, including 70% of the ton-miles of coal and 60% of grain ton-miles. In 1977, the railroads received more than \$20 billion in operating revenues and employed over 500,000 people.

Two-thirds of this rail traffic is carried on only one-fifth of the system's 193,500 route miles. But each mile of excess track has been estimated to cost \$4,600 per year to maintain and operate. Even though Class I railroads have spent approximately 40 percent of total annual operating expenditures on maintenance of plant and equipment, deferred maintenance in the past decade has accumulated to \$5.4 billion. This has resulted in a quadrupling of accidents caused by defects in rights-of-way or fixed structures in the last decade and in fifteen percent of the track operating under orders to reduce speed.

Because of the industry's financial difficulties, the Federal Government has been pouring over \$1 billion annually into the preservation of the freight rail system (with the largest share, by far, going to Conrail). Yet the industry's rate of return on investment this June reached a dismal 0.24%. In addition to Conrail, three railroads are already in reorganization, and several others face huge financial difficulties. The low rate of return has led to the almost total inability of the industry to attract new equity capital, and new debt requires payment of high interest rates. The industry's estimated capital shortfall between 1976 and 1985 (exclusive of Conrail) is between \$13.1 and \$16.2 billion, on an overall capital requirement of \$42.5 billion.

Continuation of these trends of the postwar period would result within the next ten years in an industry facing huge capital shorgates, lacking the resources needed for safe operation and dependent on the financial support of the Federal Government. Even the currently healthy Western railroads may well, by 1985, fall prey to the problems that already exist in the East and Midwest.

A major contributor to the industry's problems is that railroad rates and services are completely regulated by the Interstate Commerce Commission, whereas there is virtually no regulation of competing barges and minimal regulation of the truckload motor carriers that are most competitive with railroads.

In October of this year, the Secretary of Transportation issued a report on the condition of the nation's freight railroads titled "A Prospectus for Change in the Freight Railroad Industry." That report analyzes the causes and implications of these facts, and concludes that substantial changes are necessary if a privately-owned railroad system is once again to function as an efficient, energy-saving method of moving large, heavy, and bulk commodities over long distances.

Direct Federal assistance cannot be the answer. First, the budget implications are enormous, and the capital shortfall figures cited above (\$13.1 to \$16.2 billion) do not even include the estimated \$5.9 billion in Federal subsidy that the United States Railway Association believes Conrail, in its present configuration, could require between 1976 and 1985. Second, the railroads' debt-equity ratio is now such that they cannot handle more debt as part of their capital structures. Third, because of the interrelated nature of the system, Federal grants to weak railroads will artificially sustain them as competitors to the stronger carriers, thereby further weakening those companies. Finally, effective use of new funds requires fundamental changes in physical plant, labor productivity, pricing policies, and management techniques that cannot be expected to occur quickly.

More than Federal aid, regaining a healthy rail system requires:

- Reductions in costs through:

Reductions in unnecessary plant;

Better management of equipment;

Decreases in time and energy spent in dealing with the regulatory system; and

Improved labor productivity.

- Increases in revenue through:

Pricing strategies that take account of service demand;

Elimination of below-cost pricing; and

Attraction of new capital, including increased shipper ownership of equipment.

Better overall management in the industry is required. But such management will be attracted only by an industry in which risks can be taken and, when taken, rewarded. The present regulatory system stifles innovation by:

- prohibiting abandonments of lines when the ICC finds that "public convenience and necessity" require continuation of service, even where the line does not pay its own costs;
- regulating charges and rules for movement of equipment;
- restricting pricing flexibility by equalizing rates even where costs and competitive circumstances differ, requiring at least 30 days notice to change rates in response to changing demands, setting minimum rates (sometimes in excess of the rate offered by competition), and setting maximum rates insufficient to provide an adequate rate of return on investment;
- effectively requiring and sanctioning collusive ratesetting; and
- slowing down implementation of all business decisions from the largest (such as mergers) to the smallest (such as discontinuance of publication of an obsolete rate).

It is time to take a zero-based look at the system that produces such results. While quite a bit can be done by the Interstate Commerce Commission through administrative action, the statutory framework discourages significant change. As one shipper stated in a recent filing before the ICC, regulation's "function is to restrain competition, not to promote it."

### Summary of Regulatory Reform Options

#### Abandonments and Other Cost-Cutting Structural Changes

A more liberal abandonment process could allow abandonment on notice (either of any line or of lines shown to be unprofitable), with provision for continuation of service in the event of local full-cost subsidy or purchase of the line. Any of these provisions can become effective with a delay to allow a transition and to coordinate with other parts of the proposal.

Consolidations, joint trackage rights, and market swaps, useful means of continuing service while cutting costs, could be evaluated according to the standards in the Airline Deregulation Act - a balancing of anticompetitive effects with transportation benefits - in an expedited procedure in which the views of the Secretary of Transportation are given particular weight.

#### Ratemaking

After a transition period during which a growing range of rate changes would be completely freed of regulation, rate regulation could

be eliminated. Alternatively, some regulation could be retained, but it must be limited to those rates applicable to shipments without reasonable transportation or market alternatives, a difficult task, as shown by the failure of the 1976 rail legislation. Rate levels could be determined either by the ICC or by commercial arbitration according to statutory standards. During any transition period, the number, type and problems of "captive shippers" could be studied to assure that total deregulation would not cause undue or unfair damage or that residual ratesetting authority is restricted to those situations in which competition--actual or potential--does not in fact set the rate. In addition, railroads and shippers could be encouraged to enter into long-term contracts to protect themselves against sudden shifts in demand or price.

### Antidiscrimination

The prohibition against rate discrimination should be rewritten to assure that it deals only with price discrimination not justified by cost or competitive differences. Enforcement could continue in the ICC (although any discrimination provision could be used by the ICC as a substitute for maximum rate regulation), or be transferred to the Department of Justice or the Federal Trade Commission, or be left to private suits brought in Federal Courts. Transferring this function from the ICC could be accomplished immediately or at the time rate regulation ceases if that option is chosen. Alternatively, the railroads could be subjected to the discrimination standards of the Robinson-Patman Act that apply to all other (non-transportation) industries, but that also present difficult enforcement problems.

### Rate Bureaus

To a degree commensurate with ratesetting freedom, today's collective ratesetting practices should be curtailed. Railroads must, however, retain the right to set joint rates for movements that involve more than one railroad. Some rates of this type may require antitrust immunity. Options for reforming rate bureau activities include continuing and solidifying the ICC's recent changes in this area, requiring the Justice Department to evaluate rate bureau agreements or to issue guidelines on the antitrust implications of collective ratemaking, or removing the antitrust exemption for such activities altogether.

### Mergers

Mergers between healthy direct competitors (railroads with parallel lines) are no less anticompetitive in the railroad industry than in other industries, yet they have been permitted in the recent past. On the other hand, mergers that would meet the antitrust standards have been stifled by the lengthy and costly ICC procedures required before they can be consummated. One possibility for improving merger regulation is to speed up the procedures, another is to adopt the standards of the Airline Deregulation Act that permit balancing of transportation needs against

effects on competition. Another option is to subject rail mergers to the antitrust laws that facilitate end-to-end mergers and mergers with failing companies, but that inhibit mergers between healthy competitors.

#### Other Issues

Provisions in the attached proposal deal with publication and notice of rates, specialized types of rates, ICC authority over securities issuances and quality of rail service, and the nature of the railroads' common carrier obligation. The themes that dominate these proposals and that should govern any future regulatory system are equalization of the regulatory burdens on competing modes of transportation, and removal of prior restraints on carrier activity. Establishing a system that corrects abuses if they occur, and encourages innovation and flexibility, would be a significant step toward financial improvement for the railroads and toward decreased bureaucratic interference and massive federal subsidy.

OPTIONS PAPER

Tab B

## I. PROPOSED NEW NATIONAL TRANSPORTATION POLICY

A new preface to the Interstate Commerce Act would be enacted generally as follows:

To assure the development and maintenance of an efficient freight surface transportation system, in the private sector, it is the policy of the United States to provide for the impartial regulation of the various modes based on the following principles:

- (1) Maximum reliance on competitive market forces and on actual and potential competition to provide needed transportation services and to enable efficient and well-managed carriers to earn adequate profits and to attract capital;
- (2) Prevention of predatory practices and avoidance of undue concentrations of market power;
- (3) Reduction of regulatory barriers to entry into and exit from the industry;
- (4) Encouragement of fair wages and working conditions; and
- (5) Operation of a limited, but efficient and economical regulatory system responsive to the needs of the public, in which decisions are reached fairly and expeditiously.

### Explanation

The proposed new statement, which builds on the present statement and the policy statement of the airline deregulation bill, would emphasize free and fair competition among and between modes. It would also orient the focus of regulatory policy on the whole freight surface transportation system, rather than on individual modes.

## II. MAXIMUM RATE REGULATION

### Background

Maximum rate regulation is needed only if there are shippers who are "captive" to a railroad in the sense that they cannot depend on competition to force the railroad to set reasonable prices. The Department concluded in its report entitled A Prospectus for Change in the Freight Railroad Industry that the rail market share of freight traffic had declined precipitously in recent years because of effective intermodal competition. Ongoing, in-depth research will provide further detail on the nature and extent of the captive shipper problem. For purposes of this paper, however, there follows a brief description of what we consider "effective competition" to be.

We believe that effective competition exists if any of the following situations exists:

1. Other transportation modes (e.g., trucks or barges) already carry or stand ready to carry a sufficient share of the traffic affected by a particular railroad rate to provide an efficient transportation alternative;
2. A shipper could sell enough of its products from the affected plant in cities other than those affected by the proposed railroad rate to be able to assert a viable threat of shifting traffic to another market unaffected by the proposed increase.
3. A shipper has leverage with respect to the proposed rail rate because of the size or frequency of its shipments from the affected plant or any other plant or because it can shift at least a significant portion of the output of the affected plant to another carrier.

### OPTION A: Phased-In Deregulation

1. All ICC authority over maximum rates would be repealed after a five-year transition period.

2. During the transition period, a zone of reasonableness would be used. Rate increases falling within the zone would be totally deregulated. Rate increases outside the zone would be regulated in the current manner.\* The zone would increase in size each year.

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\*An alternative would be to regulate rates outside the zone in accordance with one of the new tests proposed as options B and C below. The advantage of using the current system is that shippers would not be required to learn a new, and complicated, regulatory system at the same time they were adjusting to the zone of reasonableness concept and planning for the end of the transition period. The disadvantage of the current system is that it has been used by the ICC to extend its regulatory jurisdiction inappropriately. While the zone of reasonableness concept would eliminate some possibilities for abuse, the ICC would still have wide discretion.

3. At the end of the second and fourth years, DOT would submit studies to the Congress describing experience under the zone of reasonableness and the nature and extent of any problems expected at the end of the transition period. The reports would focus on the experience of shippers who believe they are subject to rail monopoly power.

#### Pros

1. This proposal encourages price and service competition and substitutes such competition, and the already pervasive intermodal competition, for regulation by government bureaucracy.

2. This proposal phases in total rate deregulation--eliminating the ICC's power to impose rates on rail management, enforce cross-subsidies, and hold rates artificially high to subsidize other industries or other transportation modes.

3. This proposal eliminates the possibility that the ICC could unfairly extend its regulatory jurisdiction after the transition period.

4. The phase-in period would allow shippers to assess their transportation alternatives, amortize existing investment in rail-related facilities, enter into long-term contract rates minimizing the impact of rate changes, and otherwise plan for eventual deregulation.

5. The proposed study would assure constant monitoring and thorough study of the effects of deregulation on shippers in all locations and industries.

6. Shippers would be free to negotiate with railroads for prices and services that reflect the timing, amount, and value of transportation.

7. Rail management would have an incentive to offer a wide variety of price and service options in accordance with demand, efficiency, and car utilization, thus attracting new profitable traffic, eliminating cross-subsidy, raising their rates of return and attracting capital investment, and reducing the possibility of more massive federal subsidy.

8. The availability of a wide range of prices and services suited to individual shippers assures that each shipper will buy only what is needed (rather than a single package of services with an all-encompassing rate), thus reducing some rates and reducing the inflationary effects of others.

#### Cons

1. This proposal would arouse the greatest amount of opposition from shippers and Congress.

2. If a shipper has no alternative to shipment by a single railroad, rail rates may rise to a level just short of causing diversion. This could result in higher costs to consumers.

3. If railroad management miscalculates a shipper's ability to absorb price increases, or ship to new markets, or find alternate transportation, the shipper could be irreparably harmed.

[NOTE: Options B and C both contemplate ongoing ICC protection of shippers demonstrated to be captive. Both options contain a two-part test: (1) a test to determine whether the railroad has effective competition; and (2) if there is no effective competition, a test to determine whether the railroad abused its market power (that is, a rate reasonableness test). Both options also contain a limit on how low the ICC could set a rate, even if a shipper were found to be captive.

The principle difference between the options is that Option B is essentially a "verbal" test, leaving considerable discretion with the ICC to apply statutory standards to individual shippers in administrative proceedings. Part 3 of Option B imposes a floor on rates rolled back by the ICC. This would obviously not be discretionary and could be deleted if a pure "verbal" test were desired. Option C is a more "mechanical" test, screening out categories of shippers or types of commodities, before ICC authority could be exercised. It is possible to mix the various parts of the two options to create additional options.

If either Option B or Option C is selected, the amount of pricing freedom accorded the railroads will be reduced substantially. In an effort to mitigate this effect, we propose coupling both options with a zone of reasonableness within which rate increases are deregulated. This could minimize the adverse effect of a captive shipper provision on railroad pricing flexibility, without doing harm to the purpose of such a provision.]

The major advantage of Option A is that it is highly unlikely that a limited deregulation standard can be designed and enacted in a truly limited form and in a way that precludes ICC abuse.

#### OPTION B: ICC Protection of Some Shippers: The "Verbal" Test

A zone of reasonableness would be created and expanded each year for four years. The zone set for the fourth year would remain in effect thereafter. Rate increases falling within the zone would be totally deregulated. Rates outside the zone would be regulated in accordance with the three-part test that follows.

##### Part 1: Effective Competition Test

1. All movements by rail are rebuttably presumed to face effective competition. A shipper or other protestant wishing to rebut the presumption must demonstrate, by clear and convincing evidence, that there is no reasonable alternative to shipping via the railroad proposing the increase. In so demonstrating, the protestant must specifically address the following:

- a. intramodal competition
  - i. availability
  - ii. associated rate;
- b. nearest rail connection (i.e., the closest point at which traffic could be shifted from the proponent railroad to another);
- c. intermodal competition (all forms)
  - i. availability
  - ii. associated rate;
- d. rail/water and rail/truck connections
  - i. availability
  - ii. associated rate;
- e. the possibility of shipping to a new market; and
- f. the closest geographical point at which alternative (non-rail) transportation is available; and
- g. the estimated cost of shifting to private carriage, and the basis for the estimate.

2. The proponent railroad may respond to the protestant's evidence on any point listed above, including a showing of the transportation modes and markets used by the shipper's competitors.

3. The ICC must make a specific finding on each of the statutory criteria listed above. Inter- or intramodal competition must be found to be a reasonable alternative if the associated rate is not more than 25 percent (in the case of motor carriers) or 10 percent (in the case of another railroad or in the case of rail/water or rail/truck) above the rail rate before the proposed increase.

4. The ICC's power to suspend, and to initiate its own investigations, would be terminated immediately. Before initiating an investigation, the ICC must find that the shipper seeking the investigation would be damaged by the proposed rate and would be likely to prevail on the merits of the investigation. The burden of proof in this respect would be on the shipper. Provisions for damages and attorneys' fees would be added to preclude railroad abuse of the no-suspend feature.

#### Part 2: Rate Reasonableness Test

1. The ICC would reject a proposed rail increase only if it found on the evidence of record in a proceeding that the proponent railroad had "abused" its market power.

2. The shipper would have the burden of proving abuse by clear and convincing evidence, and could submit any evidence it deemed probative.

3. The shipper would also be required to prove, by clear and convincing evidence, the nature and extent of damage it will suffer if the proposed rate were put into effect.

4. The ICC would be required to accept any evidence offered by either party and could not issue implementing regulations.

5. Tight time limits would be imposed on the duration of the ICC investigation and the time available for ICC decision.

6. The rate could be changed if either party presents evidence of a significant change in facts or circumstances relied on by the ICC in setting the rate.

### Part 3: ICC Action

If the ICC finds that the proponent railroad has no effective competition, and has abused its market power, the ICC may set the rate for the traffic of the protesting shipper(s), subject to the following limitations:

1. the rate must be set at a level necessary to assure that this rate, when weighed proportionately with the railroad's other rates, assures a rate of return of not less than 11 percent;

2. the protesting shipper(s) must agree to ship all output at the ICC-set rate until such time as it is no longer captive.

### Pros

1. This proposal would allow a case-by-case determination that considers all the facts relevant to a particular situation, and, if properly implemented, protects only the truly captive shipper.

2. The proposal would place a heavy burden of proof on the shipper, first in seeking an investigation and then in overturning a proposed increase, thus minimizing frivolous protests.

3. The zone of reasonableness and the heavy burden of proof requirements combine to remove many rates from regulation.

4. The proposal avoids fixed numbers and inflexible standards, resulting in decisions that reflect particular circumstances, not general rules.

5. The limitation on how low the ICC can set a rate would assure the railroads of an adequate rate of return, if they are operated by efficient, competent management.

6. The requirement that decisions be made on the evidence of record in a proceeding makes ICC decisions more easily reviewable in the courts than are current ICC decisions.

7. Shippers would far prefer this over Option A.

Cons

- 1. The first two steps of the proposal give the ICC substantial discretion and could be easily abused.
- 2. Step one of the proposal would involve a full and complex antitrust market analysis that makes imposition of short time limits difficult.
- 3. Step three of the proposal necessitates establishment of complex and uniform ICC accounting and costing systems far more accurate and sophisticated than those used by the ICC today.
- 4. The railroads would oppose this as compared to Option A on the grounds that they face effective competition on all routes and that the ICC has abused tests of this kind in the past.
- 5. Part 3 of the test could result in unexpectedly high rates for captive shippers if rail management fails to price competitive traffic optimally.

OPTION C: ICC Protection of Some Shippers: The "Mechanical" Test

A zone of reasonableness test would be created and used in the same way as in Option B. Rates outside the zone would be regulated in accordance with the following two-part test.

Part 1: Effective Competition Test

- 1. Every three years the government would conduct a census of transportation on every commodity on a state-by-state basis. The census would show the market share (per commodity) moving by rail, motor, water, and air.
- 2. If the total railroad industry has less than a 70 percent market share of any commodity moving between an origin and a destination state, effective competition would be conclusively found to exist for movements between that origin and destination.
- 3. If the rail industry market share is above 70 percent, a rebuttable presumption is created that there is no effective competition to rail. The railroad proposing the increase could overcome the presumption by showing effective railroad-to-railroad competition or by any other evidence it thinks convincing. In making the rebuttal, the railroad would follow the procedure described in Part 1 of Option B, but with the burden of proof on the railroad.

## Part 2: Rate Reasonableness Test

If the railroad has no effective competition for a particular movement, the shipper need not prove the rate unreasonable. Rather, the ICC would automatically set the rate in accordance with the following procedure.

1. Congress, or DOT or the ICC at the direction of Congress, would set either a specific, desirable rate of return for each railroad, or a statutory standard for setting a rate of return (e.g., the average return of a New York Stock Exchange firm).

2. The ICC would then calculate the average ratio of rate to variable cost that each railroad is actually earning on deregulated traffic moving under competitive conditions (as determined under the effective competition test).

3. The ICC would calculate what percentage of the railroad's total traffic is competitive.

4. The ICC would then be able to calculate what ratio of rate to variable cost must be earned by captive traffic if the railroad is to meet the desired rate-of-return figure.

### Pros

1. The zone of reasonableness would completely remove some movements from regulation.

2. Part one of the proposal would automatically remove other commodities from regulation, for at least three years, without possibility of ICC abuse, while protecting shippers in situations of rail market dominance.

3. Part one of the proposal necessitates preparation of a complete and up-to-day data base useful for all regulatory purposes.

4. Part one of the proposal can result in a case-by-case determination of market power even after a presumption of power is created, if the railroad wishes to rebut the presumption created by the results of the census.

5. Part two of the proposal would assure the railroad of the chance to earn (but does not guarantee) a rate of return sufficient to attract private investment and remain privately owned.

6. Part two of the proposal would assure that while the prices on any captive traffic would be regulated, ICC discretion in judging rate reasonableness would be more limited than in Option B.

7. Shippers would prefer this proposal to Option A (but would be divided as between B and C).

### Cons

1. Part one of the test does not provide for changes in market situations during the three-year period.

2. Rail market share may change from one census to another causing confusion and inability of shippers and railroads to plan on a long-term basis.

3. The census may be expensive, would create a new bureaucracy, and may not contain complete data because of the existence of many unregulated trucks and barges whose presence is difficult to quantify.

4. Part two of the test necessitates a major ICC bureaucracy constantly monitoring the railroad rates on competitive traffic and computing their rates of return.

5. Railroad-to-railroad competition would not show up in the census, and the railroad, would, therefore, have to resort to time consuming and discretionary ICC proceedings to prove even obvious intramodal competition.

6. Since this is a "mechanical" test with a resort to a "verbal" test, proceedings may be long, complex, and expensive, and would not finally eliminate ICC discretion.

### III. MINIMUM RATE REGULATION

1. A zone of reasonableness would be established and expanded each year for five years. The zone established for the fifth year would remain in effect thereafter. Rate decreases within the zone would be deregulated.

2. Rate decreases outside the zone would continue to be regulated by the ICC.

3. The ICC test would be identical to the Clayton Act test that makes it unlawful "to sell or contract to sell . . . at unreasonably low prices for the purpose of destroying competition or eliminating a competitor."

4. The burden of proof would be on the shipper to prove, by clear and convincing evidence, a violation of this test. The ICC decision would have to be based on the evidence of record in a particular proceeding, and would be subject to tight time limits.

#### Explanation

Protection against predatory or otherwise anticompetitive pricing practices should be continued to prohibit attempts by a railroad to harm another railroad or another mode by unfair prices. There is no reason, however, to govern the railroads by a standard different from that applied to all other (non-transportation) industries. This proposal would require the ICC to enforce a standard identical to that applied elsewhere in the economy and would not allow the ICC to use its previously broad discretion to hold rates artificially high to protect another mode.

## IV. RATE BUREAUS

### Background

Most railroad traffic moves over the lines of more than one carrier. Railroads are now immunized from the antitrust laws when they meet in a rate bureau to establish rates for such movements. However, only some collective ratemaking activities would actually violate the antitrust laws. This distinction is not clearly made in the Railroad Revitalization and Regulatory Reform Act of 1976 (the "4R Act") which reformed rate bureau practices.

The 4R Act prohibited the ICC from granting immunity for agreement or voting on single-line rates (rates for movements conducted wholly on one railroad's lines), but permitted railroads to discuss such rates. The 4R Act limited immunity for discussing and voting on inter-line rates (rates for movements requiring two or more railroads) to those railroads that can "practically participate" in the affected traffic. The 4R Act also required the ICC to find any proposed rate bureau agreement to be in "furtherance of the national transportation policy" before granting immunity. The ICC has not yet approved any agreements under the new standards and has, in fact, turned several down as being insufficiently justified. Further, the ICC announced that future agreements would have to open rate bureau activities to the public. The rate bureaus have challenged these ICC decisions in court. Those cases are still pending.

Three options follow for dealing with rate bureaus in the future.

### OPTION A: Make Some Changes in the Current Rate Bureau Statute and Open Meetings to the Public

1. Leave the current rate bureau provisions in effect except that single-line rates could no longer be discussed or voted on; joint-line rates could be discussed and voted on by carriers that "practically participate" in the rates, a term whose application would be more narrowly defined.

2. Open all rate bureau meetings and activities to the public.

3. Deny antitrust immunity for general or broad territorial rate increases by the entire industry, but permit them for individual firms.

### Pros

1. Single-line rates would have to be set competitively.

2. Open meetings would prevent violations of the joint-line rules.

3. Ratemaking could be conducted quickly and efficiently, assuring the railroads of the ability to respond promptly to changes in demand.

4. Ratemaking would be an efficient and economical administrative process.

5. This proposal would invoke the least opposition from railroads.

6. Open meetings would inhibit railroads from sham discussions of shipper rate reduction requests.

7. A good start toward this system has already been made by the ICC administratively.

### Cons

1. Collective ratemaking or discussions would occur on many rates even though ratemaking would be totally or significantly deregulated.

2. Collectively ratemaking may provide an incentive for carriers to agree on rates higher than would otherwise exist.

### OPTION B: Justice Department Grants Antitrust Immunity

1. The ICC's authority to grant antitrust immunity would be repealed immediately.

2. The Department of Justice ("DOJ") would be empowered to grant antitrust immunity for joint ratemaking activities, if:

- a. immunity is required to allow the railroads to set a particular type of joint rate; and
- b. DOJ determines that the importance of the practice for which immunity is sought outweighs its anti-competitive effects.

3. Across-the-board general rate increases and broad territorial increases would be prohibited on an industry-wide basis, but permitted on an individual railroad basis.

4. All rate bureau and rate bureau committee meetings and activities, including voting, would be open to the public.

5. The bureau may publish tariffs.

[NOTE: Items 3, 4, and 5 would apply in the other options also.]

### Pros

1. Responsibility for granting antitrust immunity would be placed with the Justice Department, which administers the anti-trust laws for all other industries.
2. Antitrust immunity would be granted only as needed to avoid violating the antitrust laws, not, as today, for virtually all joint rates.
3. Railroads would have an incentive to use less anti-competitive methods, where feasible, for setting joint rates.
4. If the Justice Department finds antitrust immunity is not needed to set a particular joint rate, they would effectively issue a "no-action" notice to the railroads, assuring them that the ratemaking method is legal.
5. Rate bureaus would continue to serve as forums for permissible discussions, eliminating the need for a series of separate meetings with attendant delay and cost.

### Cons

1. The Justice Department's known opposition to rate bureaus may result in a perception (or reality) that no immunity would ever actually be granted.
2. The proposal would continue some collusive ratemaking at a time when rate regulation is being totally or substantially phased out.
3. Setting of some joint rates would be slower, more difficult and administratively burdensome.
4. Railroads would find this option the least acceptable, as would shippers who, today, can dictate desired routes and effectively manipulate the rate bureau process.

OPTION C: Justice Department Advisory Memos

1. The ICC's authority to grant antitrust immunity would be repealed immediately.

2. The Justice Department would be required to issue one or a series of advisory or policy statements describing the situations in which joint rates may be set collectively without violating the antitrust laws. In all cases so described joint rates may be set in rate bureaus without need of immunity.

3. No antitrust immunity would be granted for situations in which the antitrust laws would be violated.

Pros

1. Antitrust immunity would be eliminated, forcing rates to be set competitively, and thus offsetting rate deregulation.

2. Railroads would be assured of the legality of those joint ratemaking activities covered by the Justice Department statements.

3. Rate bureaus would continue to exist as convenient administrative forums for setting some joint rates collectively.

Cons

1. Some joint ratemaking activities require antitrust immunity that could not be granted under this proposal. Alternative rate-setting procedures could lead to less efficient rail operations, higher rates, delay in ratesetting and, therefore, delay in response to changes in demand.

2. The railroads would strongly oppose this proposal, as would big shippers who are, today, accustomed to working through rate bureaus.

3. DOJ traditionally is reluctant to issue general advisory opinions.

## V. DISCRIMINATION

Although three options are provided, certain features are common to each. These are listed below.

1. Section 4 of the Act would be immediately repealed. Section 4 contains:

(1) A prohibition against a rate for a shorter distance being higher than a rate for a longer distance in the same direction, regardless of cost or competitive circumstance; and

(2) A requirement that rates lowered to meet water competition cannot be raised if the water competition is eliminated.

2. Section 3(4), prohibiting discrimination between connecting carriers will be retained, although slightly rewritten, to assure that a railroad cannot refuse to cooperate on an equal basis with all feasible connecting carriers, subject only to differences in cost.

### OPTION A: Rewrite the Discrimination Provisions of the Interstate Commerce Act, but Remove Enforcement from the ICC

1. The antidiscrimination provisions would be rewritten to prohibit a railroad from discriminating between shippers, localities, ports, gateways, and types of traffic, unless:

(1) The railroad faced different competitive circumstances in serving the different shippers, localities (etc.); or

(2) The cost to the railroad of providing the services differed, and the rate charged reflected only the difference.

2. The ICC would retain its authority to enforce the anti-discrimination provisions of the Interstate Commerce Act for the first five years following enactment. Thereafter, the provisions would be enforced in the Federal Courts by DOJ or the Federal Trade Commission (seeking enforcement of cease and desist orders) and by private parties (seeking damages).

3. The burden of proof would be on the complainant to show similar competitive conditions, and to prove damage if the discriminatory rate were upheld. The burden of showing cost justification would be placed on the railroad.

Pros

1. The proposal codifies the Supreme Court's interpretation of the current statute, rather than continuing the ad hoc nature of current ICC decisions in discrimination cases.

2. The proposal minimizes frivolous challenges by putting much of the burden of proof on the complainant (shipper).

3. The proposal would permit discrimination based on economic or competitive circumstances, but not personal whim. The proposal would not, therefore, if properly implemented, be a serious inhibition on ratemaking flexibility.

4. The proposal would eliminate the possibility of the ICC using this authority as a permanent substitute for rate regulation.

5. Railroads would favor this over Option C.

Cons

1. This proposal would allow the ICC to substitute discrimination proceedings for rate regulation for the first five years.

2. Accurate discrimination findings require long and expensive administrative or court proceedings.

3. The railroads would object to this proposal as imposing on them standards different from and more stringent than those imposed on other industries.

4. Individual shippers may believe that bringing suit in the courts is more difficult and expensive than ICC litigation.

5. DOJ and FTC may resist this enforcement responsibility as they have resisted enforcing the Robinson-Patman Act.

6. The proposal could further clog the federal courts.

OPTION B: Keep Enforcement at the ICC

1. Rewrite the discrimination laws as proposed in Option A.
2. Allow the provisions to be enforced by the ICC on a permanent basis.

Pros

1. The same as 1, 2 and 3 in Option A.
2. This proposal would have the greatest shipper support.

Cons

1. The same as 2 and 3 in Option A.
2. This proposal would allow the ICC to thwart deregulation permanently by substituting discrimination authority for rate regulation.

OPTION C: The Antitrust Laws

1. All ICC authority over discriminatory rates would be repealed immediately.

2. All rail rates would be made subject to the Robinson-Patman Act (Sections 2 and 3 of the Clayton Act), which makes it a felony to:

...discriminate in price between different purchasers of commodities of like grade and quality ... where the effect of such discrimination may be substantially to lessen competition or tend to create a monopoly in any line of commerce ...

The Robinson-Patman Act may also be enforced by a civil treble damage action brought in any Federal court by an injured party.

Pros

1. This proposal would continue the prohibition against discriminatory pricing, but subject the railroads to the same laws as those imposed on all other (non-transportation) industries.

2. This proposal eliminates the possibility that the ICC could use the discrimination laws as an effective substitute for lost or diminished rate regulation authority.

3. This proposal would encounter the least opposition from the railroads.

Cons

1. The Robinson-Patman Act now covers commodities but not services. Amending it could cause additional political and Congressional jurisdiction problems.

2. The Robinson-Patman Act as interpreted by the courts, permits price differences to meet, but not beat, competition.

3. The Robinson-Patman Act has been interpreted to make the plaintiff's case easy to establish and the defendant's case quite difficult. This interpretation, along with the treble damage feature of the Act, encourages nuisance suits.

4. DOJ has frequently sought repeal of the Act, and enforced it only reluctantly. This option may, therefore, encounter their opposition or be viewed as a sham.

5. This proposal would encounter the greatest opposition from shippers, port interests, etc.

## VI. MERGERS AND ACQUISITIONS OF CONTROL

### Background

Any of the proposals dealing with structural changes will have to include retention or change of the labor protection provisions now applicable to these transactions. The provisions, formerly sections 1a(4) and 5(2)(f) of the Interstate Commerce Act, are now codified at 49 USC §11347. Unless the carrier(s) and union(s) agree otherwise, the ICC must condition approval of an abandonment, consolidation or merger on the employees affected being guaranteed that they "will not be in a worse position related to their employment" during at least the four years following the effective date of the transaction. Among other things, this requires preservation of all existing rights under the collective bargaining agreement (including continuation of pension rights and benefits), continued right to collective bargaining, protection against job degradation, assurance of priority employment for employees terminated or laid off, and paid training or retraining programs. As interpreted by the Commission, this has resulted in labor being guaranteed an income equal to prior salary for a six-year protective period.

### OPTION A: The Antitrust Laws

1. All ICC regulatory authority over mergers and acquisitions of control would be repealed immediately.

2. Mergers would be subject to the antitrust laws that prohibit one corporation from acquiring another "where in any line of commerce in any section of the country, the effect of such acquisition may be substantially to lessen competition or to tend to create a monopoly." (Sec. 7, Clayton Act)

[Note: The Clayton Act has a special railroad provision facilitating end-to-end rail mergers:

Nor shall anything herein ... prevent [a] common carrier from extending any of its lines through the medium of the acquisition of stock or otherwise of any other common carrier where there is no substantial competition between the company extending its lines and the company whose stock ... is so acquired. [Emphasis added]

The Clayton Act also facilitates mergers involving failing companies.]

Pros

1. This proposal would treat rail mergers like all other mergers by eliminating the regulatory prior restraint, and imposing the same substantive standards.
2. End-to-end mergers (that may have pro-competitive effects), and mergers involving failing companies, would be facilitated.
3. Parallel mergers that eliminate healthy competitors would be difficult to consummate.
4. Since ICC-approved mergers are generally challenged in the courts, this proposal would probably shorten the review process.

Cons

1. The Justice Department can be expected to oppose most parallel mergers, and parallel mergers are sometimes desirable to eliminate excess capacity and rationalize the rail system.
2. This option will be strongly opposed by the railroads who prefer the current ICC system over the antitrust laws.

OPTION B: The Rule of Two

1. The ICC would retain authority over mergers.
2. DOT would identify "important" rail-bound markets (origin-destination pairs).
3. The ICC could not approve any merger that would reduce intramodal rail competition below two carriers in any "important" market. (Railroads wishing to merge would be expected to seek trackage rights, market swaps, operating agreements, or other methods to avoid violating the "Rule of 2.")

Pros

1. The proposal would stimulate and retain intramodal competition, mitigating shipper fears of "captivity" in large markets.
2. The proposal would stimulate trackage rights and other efforts to rationalize and restructure the rail system.
3. The proposal would remove most of the ICC's discretion in deciding on mergers, without removing the ICC completely.
4. The railroads would not be enthusiastic about this proposal (since they want to keep the current system), but it would be better received than Option A.

Cons

1. Identifying "important" markets must necessarily be an arbitrary process, subject to great pressure and legal challenge.

2. The "Rule of 2" concept will invoke strong Justice Department opposition to the premise that two carriers constitute enough competition, particularly in "important" markets.

3. The railroads would have an incentive to create sham devices to get a second railroad ostensibly operating in an important market.

4. A railroad that opposes a merger could hold it up by refusing to negotiate trackage and other agreements with the merging railroads.

OPTION C: The New Airline Merger Test

1. ICC authority over rail mergers would continue.

2. The ICC would approve a merger found to be in the "public interest" unless it violated a standard like that in the Airline Deregulation Act; that is, if the merger -

(A) ... would result in a monopoly or conspiracy ... or attempt to monopolize ... or

(B) The effect ... in any region of the U.S. may be substantially to lessen competition, or to tend to create a monopoly, or ... be in restraint of trade, unless the [ICC] finds that the anticompetitive effects ... are outweighed in the public interest by the probable effect of the transaction in meeting significant transportation conveniences and needs of the public ... not [satisfiable] by a reasonably available alternative having materially less anticompetitive effects.

3. The burden of proof in challenging a proposed transaction is on the protestant to prove anticompetitive effects and on the proponent to prove transportation convenience and need.

4. Tight time limits would be placed on ICC actions.

Pros

1. The proposal would be premised on the antitrust laws applicable to other industries, but provide a loophole for overriding transportation circumstances.
2. The proposal has already been accepted by Congress for use in one segment of the transportation industry.
3. The proposal would coincide with the balancing tests generally applied by the courts.

Cons

1. The proposal would leave the ICC with wide discretion.
2. The proposal would not involve consideration of the effects of the transaction market by market.
3. The proposal would inhibit parallel mergers more than Option B, but less than Option A.

## VII. CONSOLIDATIONS, TRackage AGREEMENTS, AND MARKET SWAPS

### Background

Section 401 of the 4R Act allows DOT to grant antitrust immunity to railroads who meet with the Secretary to discuss ways to eliminate duplicative or overlapping operations and facilities, use the most efficient routes, exchange trackage rights, combine track or terminal facilities, or take other steps to rationalize the rail structure. If the railroads reach agreement on one or more of these matters, the agreements must still be submitted to the ICC for approval. Such agreements offer the possibility of great operating efficiencies and economies with less adverse effect on competition than mergers. We propose a new standard for use by the ICC in approving or disapproving 401 agreements.

### Proposal

1. The ICC would retain jurisdiction over 401 agreements.
2. Such agreements would be measured against the merger standard contained in the airline bill, which, as discussed in Section VI above, allows significant transportation benefits to override any anticompetitive effects of the agreement.
3. Strict time limits would be placed on the ICC in weighing 401 agreements.
4. The ICC would be required to accord substantial weight to DOT findings with respect to the merits of any 401 agreement.

### Explanation

This proposal will give the railroads the greatest opportunity to consummate agreements determined by DOT to offer significant transportation benefits, while still requiring the ICC to consider any anticompetitive effects of the agreement. Because of the importance of 401-type agreements to the future operating efficiency and cost-reduction efforts of the railroads, a test allowing transportation benefits to override some anticompetitive effects is fully appropriate.

## VIII. ABANDONMENT

### OPTION A: Abandonment on Notice, Allowing the Shipper to Subsidize or Buy the Line

1. For a three-year transition period, a rail carrier may abandon a line or discontinue service by providing 240 days' notice to the public. The only proviso is that the carrier must accept an offer of subsidy, made during the notice period, that would cover the full costs of operating and maintaining the line, including a rate of return on the line adequate to attract investment capital.

2. Either the railroad or the potential subsidizer may seek binding arbitration (from the ICC or, alternatively, a commercial arbitrator) on whether a subsidy offer meets this test.

3. At the end of five years, a rail carrier may abandon a line or discontinue service by providing notice of 240 days. During the notice period the carrier must offer to sell the line--at net liquidation value--to any financially able person or community who offers to use it to provide rail transportation. The carrier could not be compelled to offer service even if a subsidy were available.

#### Pros

1. This proposal would remove the prior restraint on abandonments, allowing the railroads to devise a rail network that could sustain itself financially.

2. This proposal would require service to be provided only if a shipper or community could meet the true test of need: willingness to subsidize the service or buy the line.

3. This proposal would assure that any subsidy would meet the full costs of operating the line, but would recognize the limited value of the actual property if the line were to be sold.

4. This proposal is the only means of assuring that the ICC does not force railroads to operate the line at a loss.

5. By requiring purchase of the line after the transition period, the provision limits the pressure on the Federal government to subsidize communities and encourages communities to negotiate new operating agreements rather than simply continuing to pay the costs of existing agreements.

6. This option would receive the greatest support from the railroads.

Cons

1. This proposal would place the greatest burden on shippers and communities who wish to assure continued service. It would be strongly opposed by them.

2. This proposal will be strongly opposed by labor.

OPTION B: A Variation of Option A

1. This option is the same as Option A except:

- a. The current system (requiring the railroads to prove "public convenience and necessity" before abandoning a line, and placing a lower level on the subsidy) would be retained, with minor changes, for 3 years before the Option A plan took effect; and
- b. At the end of the transition period in Option A, a railroad could sell the line at net liquidation value, or be required by the ICC to continue to operate the line if a full subsidy is provided.

Pros

1. The delay feature would allow more time for rail management and labor negotiations aimed toward reducing branch-line costs.

2. The delay feature would also allow all affected parties to gain experience under the 1978 branchline abandonment legislation, which provides for a 3-year subsidy.

3. The delay feature would allow shippers and communities to plan ahead for the time when abandonments will be easier to accomplish.

4. The continuing subsidy option eases some of the burden on shippers and communities who could not realistically acquire and direct the operations of the rail line.

5. This option would receive more support from shippers, communities, and labor than would Option A.

Cons

1. The delay requires the railroad to continue to operate lines at a loss, thus exacerbating their financial situations and their need for financial assistance.

2. The delay allows more Federal dollars to be expended in subsidizing the line.

3. The delay feature continues current ICC abandonment procedures that are lengthy and costly, thus reducing the number of needed abandonments.

4. The continuing subsidy option will result in tremendous pressure on Congress to provide Federal subsidy.

5. The proposal would be strongly opposed by the railroads.

OPTION C: Permit Abandonment of Money-Losing Lines Only

1. This proposal would adopt the basic structure of either Option A or Option B, but limit the operation of either proposal to rail lines that are not generating revenues sufficient to cover the full costs of providing the service.

Pros (In addition to those associated with the previous options)

1. This proposal would result in fewer abandonments than the other options, and would, therefore, engender the greatest support of the three options from shippers, communities, and labor.

Cons (In addition to those associated with the previous options)

1. This proposal would require continued operation of lines that, even if profitable, may be redundant or duplicative, thus denying rail management the opportunity to design the most efficient and economical rail system.

2. Pressure for subsidy would continue indefinitely.

## IX. COMMON CARRIER OBLIGATION

### The Proposal

1. The ICC would continue to enforce the railroad obligation to provide service upon reasonable request.

2. For purposes of this section, a request would be found reasonable only if it is premised on payment of the railroad-set rate.

[NOTE: If maximum rate regulation is retained, the railroad rate must be found reasonable by the ICC under the selected standards.]

3. The common carrier obligation would not preclude a carrier from:

- a. Offering different frequencies or qualities or service at different prices;
- b. Offering contract rates (as discussed in section XII below), for the movement of some commodities or under some circumstances, but not for other commodities or under different circumstances; or
- c. Failing to provide prompt service during periods of peak demand because of prior equipment commitments.

4. DOT would be empowered to direct carriage, under specified terms and conditions, to assure safe transportation of hazardous and nuclear waste material.

### Explanation

The common carrier obligation now requires carriers to provide service "upon reasonable request therefor." The proposed provision retains the requirement that carriers not refuse to provide service for personal or other non-market reasons, but allows price and service variations. This is consistent with the thrust of the antidiscrimination options discussed in section V above.

## X. JOINT RATES AND THROUGH ROUTES

### The Proposal

1. ICC authority to compel joint rates (single factor rates agreed on by two or more railroads over both of whose lines a given movement occurs) would be repealed immediately. Railroads would be permitted to set joint rates in accordance with the rate bureau proposal.

2. ICC authority to compel through routes (agreements between railroads to provide connecting service over two or more railroads' lines) would be retained.

### Explanation

The rail system depends on through routes--that cannot always be agreed to by the affected carriers. This proposal would permit the ICC to compel the railroads to establish such routes, thereby assuring continuation of a transcontinental (east-west and north-south) rail network. However, joint rates are not necessary to the establishment of through routes. Under this proposal railroads can either agree to joint rates, or use the sum of the relevant individual railroads' rates. This will leave rate setting to the railroads--in accordance with other ratemaking changes proposed--and eliminate the traditionally long, expensive and acrimonious ICC proceedings to decide each railroad's share of a joint rate.

## XI. SERVICE REGULATION

### A. Background

#### 1. Service regulation includes:

a. Car hire regulations relating to the need of one railroad to compensate another for the time the former's cars are on the latter's lines;

b. Service orders requiring a railroad to provide particular services at a particular time or in a particular manner; and

c. Rules or orders that prescribe a particular quality or type of service for a given shipper, region, or period of time.

#### 2. Definitions

a. Per diem is the payment made by one railroad to another for the use of rail cars.

b. Demurrage payments are payments made by a shipper to the delivering railroad for holding a rail car (for loading or unloading) longer than the time prescribed by standard demurrage rules or specific terms of a particular tariff.

c. Payments to private car owners are made to compensate shippers who own their own rail cars for the use of those cars. Compensation is usually made in the form of a mileage or other use allowance or in the form of a reduced rate when the shipper uses its own cars.

d. Car service orders are orders directing carriers to use their cars in a particular way such as in single car service (as opposed to unit train service), or to serve a particular shipper, geographic area, or commodity for a particular period.

e. Directed service orders require one or more railroads to operate over the lines of another railroad to provide service the owner of the line cannot provide.

f. ICC management orders direct a particular type of investment, or a particular type of business practice that would, absent regulation, be up to rail management.

### B. Proposals on Car Hire

#### 1. Per Diem

a. Per diem payments would be set by agreement of all railroads.

b. If the carriers cannot agree, the charges would be determined by binding arbitration, which could be sought by any interested carrier.

c. Establishment of an industry-wide per diem charge would not prevent individual railroads from making specific per diem arrangements for particular equipment, as long as the arrangements are offered in a non-discriminatory manner.

d. The ICC would have the power to grant antitrust immunity to the railroads to discuss setting standard per diem rates. All discussions, agreements, or voting for which immunity is granted would be opened to the public.

## 2. Demurrage Proposals

a. Standard demurrage payments and "free time" for loading and unloading would be set by agreement of all railroads.

b. Whenever standard demurrage terms cannot be reached in any other manner, demurrage agreements, and the question of who keeps what share of demurrage payments, would be decided by binding arbitration among the carriers.

c. In any particular circumstance, a railroad and shipper could negotiate free time and demurrage provisions different from the standard provisions.

d. The ICC would have the power to grant antitrust immunity to the railroads to discuss setting standard demurrage rates. All discussions, agreements, or voting for which immunity is granted would be opened to the public.

## 3. Payments to Owners of Privately-Owned Cars

The amount a railroad pays a shipper for the use of the shipper's cars, and the form of payment, would be set by negotiation between the shipper and the railroad. The railroad industry would not be allowed to set standard terms for use in such situations, nor could the ICC grant antitrust immunity to the railroads for this purpose.

## C. Explanation

Currently, per diem payments are negotiated by the railroads and adjudicated by the ICC. As a practical matter, the Commission has approved whatever the railroad industry agrees to. Unfortunately, the industry has not, historically, been able to agree on appropriate charges. The ICC, therefore, operates as a de facto arbitrator.

The proposed rule would continue to allow determination of per diem payments by consensus. Unlike the present system, however, individual railroads would be able to set their own rates. Binding arbitration would be available as needed. Antitrust immunity, limited to this function, could be provided by the ICC.

Absent rate regulation, regulation of demurrage charges should also disappear. It will, however, be convenient and helpful in most instances to develop a standard demurrage charge. The standard charge could be superseded whenever the railroad and shipper agreed. Antitrust immunity could be granted by the ICC for this activity also.

Payments made by railroads to shippers for use of shipper-owned cars must be individually negotiated in light of individual circumstances. The railroads would not be permitted to set a standard charge.

#### D. Service Order Proposals

##### 1. Car Service Orders

a. Car service orders could be issued by the Secretary of DOT if the President declared a national emergency.

b. Railroads could, by general agreement, delegate to a representative organization of the industry the authority to establish standard car service procedures and to modify those procedures in the event that particular changes in transportation conditions warrant. The standard procedures need not be adhered to if other provisions are made in particular situations. Antitrust immunity may be granted by the ICC, if needed, to facilitate general agreements.

##### 2. Directed Service Orders

a. Directed service orders could be issued by the Secretary of DOT if the President declared a national emergency.

b. All costs of providing directed service not covered by revenues earned from provision of the service would be covered by the U.S. government.

##### 3. Rail Management Orders

a. Rail management orders may be issued by the Secretary of DOT if the President declared a national emergency.

b. A railroad could seek recompense from the government for any costs incurred in complying with such orders and not otherwise recovered.

#### E. Explanation

Over the years, the ICC has issued numerous service orders in response to particular problems. While those orders may temporarily have helped a particular shipper or group, they often resulted, inadvertently, in substantial harm to other parties. Too often the result has been either not to improve the overall quality of service, or to cause more damage than benefit. For example, car distribution orders often increase empty mileage, and result in reduced car utilization and efficiency.

Directed service orders are designed to assure continued service when carriers normally serving the area cannot continue to provide service (through, for example, bankruptcy). This proposal would allow the government to assure continued service where necessary in an emergency.

Under this proposal, the ability of government to involve itself in management decisionmaking would be eliminated except in times of national emergency. In such instances, the government would be required to pay the costs incurred by the railroads in carrying out those orders, insofar as such costs are not recouped by the provision of the required service.

The proposal calls for the Secretary to issue specific orders to the railroads in response to a Presidential declaration of national emergency. Another option would be for such orders to be issued by the ICC or the Federal Preparedness Agency.

## XII. CONTRACT RATES

### Background

Contract rates are rates negotiated between shipper(s) and carrier(s) that impose specific obligations on the shipper(s) to tender traffic under agreed terms, and on the carrier(s) to provide specific services at agreed rates. The purpose of such rates is to enable a railroad to tailor service to the needs of individual shippers, and to allow both railroads and shippers to minimize uncertainty as to supply, demand, and price. Until recently such rates have been forbidden by the ICC and are now available only under stringent and limiting rules.

### The Proposal

1. Effective immediately, shippers and carriers would be allowed to enter into contracts specifying rates, conditions of service, quantity of traffic, duration, and any other provisions mutually agreeable.

2. Any carrier would be required to negotiate in good faith with any shipper who requests a contract rate. Discrimination (i.e., who must be offered a contract containing the same conditions and the same rate) would be determined in accordance with the discrimination options contained in Section V above.

3. The terms of a contract, if agreed to by the affected parties, would not be subject to ICC approval. Rates and terms agreed to by the parties could not be protested before the ICC, except on the basis of violation of the antidiscrimination laws.

### Explanation

The new ICC policy states that, in principle, the Commission will consider permitting railroads to enter into contract rates, but only subject to the full panoply of ICC regulation, which effectively minimizes the value of such rates. Contractual agreements, arrived at without ICC interference, would permit shippers to remove the uncertainty associated with fluctuating rates by contracting for a specific rate, thereby also assuring themselves of adequate, prompt car supply. Contracting would, thus, be an especially helpful tool for shippers to use in the event of total rate deregulation, and would be an effective device to protect shippers who believed themselves dependent on a single railroad. Contract rates would be beneficial for railroads, as well. Railroads can reduce the uncertainty of demand for rail cars and set charges that better reflect market circumstances if they are assured, under the terms of the contract, of a minimum or fixed amount of traffic, at a set time. Those shippers not negotiating contract rates would continue to use regular rail rates.

### XIII. NOTICE

#### The Proposal

1. Effective immediately upon enactment, a seasonal, regional, or peak-load rate could be proposed to the ICC in a tariff establishing a range of rates (with upper and lower limits). Within that range (if approved by the ICC), rates may be decreased without notice, or increased on one-day notice. Reasonableness of the limited rates would be judged in accordance with the ratemaking standards proposed elsewhere.

2. There would also be a five-year transitional period of ever-decreasing notice periods for all rates. All rates (including peak tariffs as defined above) could be published on notice of 21 days (year one); 14 days (year two) and 7 days (year three). Thereafter, rate increases could take effect after one day's notice and decreases could become effective without notice.

#### Explanation

The ability to change rates with little or no notice is fundamental if railroads are to compete effectively with other unregulated modes, and smooth peak and trough demands for rail service. Since this is especially essential for rates intended to reflect peak or seasonal demand, special provision would be made to allow immediate changes in such rates within pre-agreed limits. This provision would no longer be needed at the end of the transition period.

After the transition period, rate decreases would be permitted without notice so that the railroads can meet or beat a competitor's rate. Increases would require a one-day notice to permit shippers to shop for a better rate.

#### XIV. RATE PUBLICATION

##### The Proposal

1. Railroads would publish rates on commencement of service.
2. A performance standard (e.g., "essentially contemporaneous availability") would be enacted to require the railroads to establish a system assuring shippers of prompt notice of published rates. In addition, continued publication at the ICC would be required.

##### Explanation

There are many advantages to requiring rate publication. First, it is an important shipper service. Second, it facilitates enforcement of discrimination laws. Third, it is essentially pro-competitive in that it allows shippers to choose from a full array of price options.

## XV. INTERMODAL OWNERSHIP

### The Proposal

1. Railroads would be permitted to merge with, acquire (etc.) motor carriers or water carriers.

2. Such mergers or acquisitions would be subject to the same standards as proposed for intra-industry mergers.

3. Railroads would be permitted to establish motor or water carrier subsidiaries or affiliates, but would not be permitted to discriminate in favor of that subsidiary or affiliate.

### Explanation

Currently, intermodal acquisitions and establishment of intermodal firms are generally prohibited. The economy and efficiency of intermodal carriage would be enhanced if railroads could acquire or establish motor or water carrier operations. The same laws governing tendencies to monopolize or restrain trade should be sufficient to prevent such practices in the transportation industry and the discrimination laws would prohibit an intermodal firm from discriminating against other possible intermodal connections.

## XVI. RATES ON GOVERNMENT TRAFFIC

### The Proposal

1. Section 22 of the Interstate Commerce Act would be repealed immediately.

2. The government would be free to negotiate rail rates on the same terms as other shippers.

### Explanation

Section 22 was intended to free the government of the regulatory restraints on rail pricing and to get rail service at lower rates consistent with rail costs. The new ratemaking proposals would allow the government to negotiate on the same basis as other shippers for the best rate/service package.

## XVII. FINANCE MATTERS

### The Proposal

Section 20 of the current Interstate Commerce Act--which includes ICC authority over securities issuances, interlocking directorates, self-dealing, etc.--would be immediately repealed; authority would be placed with the SEC.

### Explanation

Regulatory constraints on rail securities issuances should be the same as those on other industries--since the goals are the same. ICC regulation has not always been consistent with SEC regulation, leading to costly burdens on the railroads, needless confusion for potential investors, two sets of inconsistent accounting requirements, and other unnecessary and expensive duplication of regulation.

## XVIII. PREEMPTION

### The Proposal

A specific preemption provision would be enacted to make clear that a federal exemption from regulation is effective to preempt state action. The provision would read (roughly) as follows:

The power, jurisdiction, and authority to regulate railroads is exclusively reserved for the federal government. The states are hereby preempted from regulating railroad activities that are in any way covered by this Act.

### Explanation

A state statute affecting interstate commerce is today preempted if it conflicts with a valid federal statute. This result follows from the interpretation of the Commerce and Supremacy Clauses of the U. S. Constitution. State action is superseded where the conflict with the federal act is so direct that the two acts cannot be reconciled or consistently stand together. Kelly v. Washington, 302 U.S. 1 (1937); Illinois Natural Gas Co. v. Central Illinois Public Service Co., 314 U.S. 498 (1949). In short, state action will fail if it would interfere unduly with the accomplishment of Congressional objectives or policy. Hill v. Florida, 325 U.S. 538, 542 (1945); California v. Zook, 336 U.S. 725 (1949) rehearing denied 337 U.S. 931.

State regulation of rail rates, mergers, abandonments, service obligations (etc.) would directly conflict with Congress' desire for a deregulated environment, as expressed in these proposals. A conflict exists with state laws whether Congress has taken direct action or affirmatively prohibits an agency from taking action in a particular area. In terms of preemption, it is irrelevant as to which alternative method of drafting Congress chooses. Decisions have made clear that exemption from regulation constitutes a form of preemption. Baltimore Ship & Receiv. Ass'n v. Public Ut'l. Com'n. of Cal., 268 F. Supp. 836 (1967), aff'd, 389 U.S. 583 (1968); Pioneer Airways v. City of Kearney, 199 Neb. 12, 256 N.W. 2d 324 (1977).

Thus, although it is probably not necessary to provide for preemption in the statute, a clear statement of Congressional intent in this regard will put to rest any lingering doubts as to federal deregulatory and preemptive intent. It is well settled that Congressional declarations of activities excluded from state controls are controlling in the determination of intent

to occupy the field. Rice v. Santa Fe Corp., 331 U.S. 218 (1947).  
Since it is impossible to forecast accurately in advance of  
litigation the outlines of the "field" that Congress occupies,  
it is highly preferable to draft a clear statement of intent.

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Tab C

INTERAGENCY TASK FORCE\*  
EXECUTIVE SUMMARY  
TRUCK REGULATORY REFORM OPTIONS

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\*This options paper is the result of a task force consisting of representatives of the Departments of Agriculture, Commerce, Defense, Energy, Justice, Labor, and Treasury, the Council of Economic Advisors, the Council on Wage and Price Stability, Federal Trade Commission, Interstate Commerce Commission, Office of Consumer Affairs, and the Office of Management and Budget.

## TRUCK REGULATORY REFORM OPTIONS EXECUTIVE SUMMARY

### I. The Need for Change

Economic regulation of the trucking industry establishes cartel type rates which can keep prices from reflecting economic conditions; substitutes government regulation for private sector management of an industry with a naturally competitive structure; often wastes fuel and reduces operating efficiency by requiring indirect and circuitous routing and excessive empty backhauls; and poses an artificial barrier to minorities and other small businessmen who would like to offer competitive trucking service.

Economists for many years have claimed their analyses show that shippers throughout the economy are paying inflated rates for trucking service. There is evidence to suggest that these rates could be reduced in many cases. Inflated rates go largely unnoticed by consumers because transportation costs are seldom greater than 5 percent of the cost of a product. Several studies have concluded that excessive rates and operating restrictions that cause inefficiencies, are imposing unnecessary costs of several billion dollars annually on the U.S. public.

The need for regulatory controls on trucking raises many questions. With over 17,000 regulated carriers, and a total of perhaps 150,000 carriers, the trucking industry has a great potential for competition. Intermodal competition in the form of rail, barge and air cargo transport is also prevalent. The purpose of protecting shippers and the public by regulation is now questionable since most actions before the ICC involve only the groups with a direct financial

interest. The common carrier obligation is not being enforced as it should be for small shippers and geographically remote small towns and rural areas.

Perhaps the most obvious evidence of the overwhelming intrusion of the government into the trucking business is the complex and cumbersome nature of the regulatory system itself. There are literally hundreds of thousands of pages of intricately formulated tariffs (rate notices) filed each year. The system also produces endless litigation. Last year almost 8,000 cases were filed requesting motor carrier operating rights alone. For example, an examination of a few pages of a recent trade publication show requests for authority to transport glass containers, not exceeding one gallon capacity, between three small towns in Pennsylvania and one city in New Jersey; authority to transport skeet and trap targets from one point in Indiana to points in five states. Many other examples can be provided.

Existing regulation also causes many carriers to operate less efficiently than they could, which raises their costs and wastes fuel. Empty backhauls, partial loads, and circuitous routes often result. DOT-ICC data show that more than 16% of general purpose ICC-regulated vehicles travel empty. An even larger percentage of exempt vehicles travel empty. For example, under the current system, an exempt agricultural carrier may carry fresh, unprocessed produce to the canning plant but may not transport processed commodities on the return trip without entering into a leasing arrangement with a regulated carrier.

The regulatory maze is particularly burdensome to small businessmen and has worked especially to restrict the opportunities for minorities to participate in the industry. Most of today's operating authority can be traced to the grandfather

provision of the 1935 Act, when minority participation in the industry was quite limited. Restrictive entry has resulted in continued low minority participation. For example, according to available evidence, of the 2,500 interstate household movers fewer than 1% are minority-owned, and not a single minority-owned carrier has broad geographic authority to move household goods.

## 2. Structure of the Industry

Due in large measure to a regulatory structure that was forced to make incremental modifications in order to adapt to a rapidly changing distribution system, the trucking industry has a complicated structure. The principal types of carriers are as follows:

Regulated Common Carriers. These are truckers who offer their services to the general public. In general the regulatory system limits these carriers either by restricting the commodities a trucker may haul or the routes he may travel.

"Regular Route Common Carriers" (Carriers with restricted routes)

- o have broad commodity authority and carry general freight;
- o transport less than truckload (LTL) shipments;
- o require terminal facilities to consolidate and distribute the shipments;
- o are highly unionized; and
- o for the most part do not compete with the railroads;

"Irregular Route Common Carriers" (Common carriers with broad route authority)

- o have limited commodity authority (liquid petroleum, refrigerated goods, automobiles, etc.);
- o transport truckload (TL) shipments;

- o have specialized trucking equipment but limited investments in terminals;
- o are not as highly unionized as LTL carriers; and
- o are highly competitive with railroads and private carriers.

Contract Carriers. These are regulated carriers who generally carry TL shipments but offer their services to a limited number of clients. These carriers are restricted by the ICC, mainly in terms of the number of clients each may serve.

Private Carriers. These are unregulated non-transportation companies who operate their own trucks to carry their own goods. This sector of the industry is growing rapidly, primarily because of problems with the rates or services provided by regulated carriers. Even though these carriers are not directly subject to regulation, they are indirectly regulated and restricted. (For example, in most instances a private carrier may not haul for its corporate subsidiaries.)

Exempt Operators. Transportation of unprocessed agricultural commodities is exempt from ICC regulation. These commodities are primarily hauled by an estimated 100,000 owner-operators. This very competitive segment of the trucking industry has captured much of the Nation's agricultural traffic from the railroads, but is limited in its ability to transport regulated traffic.

### 3. Recent Trends in ICC Regulation

With the appointment of Daniel O'Neal as Chairman, the ICC began to reexamine many of its trucking regulations. As a result:

- The Commission has streamlined some entry procedures and relaxed some criteria for obtaining new operating authority.
- It has rejected a recent rate bureau request for a 6.2% general rate

increase on the grounds that the profits of the trucking industry are inflated and should be reduced to a level comparable to that of all manufacturing industries.

- The Commission has reduced restrictions on private carriers and is reconsidering reform for contract carriers.

A list of recent ICC decisions and proposals, and a response from several Congressmen, is given in an Appendix to the Executive Summary.

These reforms just scratch the surface of the existing complicated maze of economic regulations. Legislation is still needed, if for no other reason than to speed up the current administrative initiatives which, at a minimum, will consume several years in Commission hearings and several years thereafter in court challenges. Legislation also is desirable to foreclose the possibility that a future Commission will undo the work of the present ICC.

Even before proposing legislation, commitment to deregulation and further ICC-initiated reforms could be assured by the appointment of new Commissioners who favor increased competition in the industry. There are currently six vacancies on the Commission.

#### 4. Options

The interagency task force has outlined three basic options:

1. total deregulation, phased in over a prescribed transition period;
2. selective deregulation, emphasizing deregulation of truckload traffic, with substantial reform for less-than-truckload traffic;  
and
3. administrative changes, accompanied by legislation that consolidates the reforms undertaken by the ICC.

These options are explored briefly in this section along with the pros and cons of each option. A more complete discussion is given in Section IV of the main body of the paper. There are, of course, many variations of these basic options.

#### OPTION 1. PHASED TOTAL DEREGULATION

Deregulation would take place over a transition period of, say, five years in order to permit shippers to adjust their freight distribution patterns and service requirements and to offer carriers an opportunity to redeploy their assets. This option does away with the existing system of regulation. It relies exclusively upon the marketplace to ensure that the rates shippers are charged are appropriate and that service is provided where and when required.

##### Features

a. Entry/Exit - Completely eliminate the Commission's authority to prescribe conditions of entry (except safety, financial and insurance requirements) or exit from the industry during the transition period.

b. Rates and Rate Bureaus - Prohibit collective ratemaking. Eliminate antitrust immunity for rate bureaus (repeal the Reed-Bulwinkle Act). Institute a no-suspend pricing zone during the transition period. After five years prohibit the Commission from setting maximum and minimum rates.

c. Mergers. Transfer all responsibilities for both intramodal and intermodal mergers to the Department of Justice and Federal Trade Commission (FTC) for enforcement under the antitrust laws.

Other - Eliminate restrictions on private carriage, equipment leasing and backhaul movements for agricultural cooperatives. Freight forwarders would be deregulated. The ICC's responsibility for regulating motor carrier

stocks and securities would be transferred to the Securities and Exchange Commission.

### Arguments For and Against

#### Pros

- o Comprehensive approach deals most decisively with the need for change and has maximum anti-inflationary and other benefits over the long run.
- o Completely deregulates LTL carriers, where most regulatory distortions occur.
- o Clearly defines the new market environment for carriers and shippers; consequently, minimizes uncertainty over future "rules of the game" and allows all parties to adjust to the new system.
- o Is consistent with the recent reforms in aviation.
- o Would not be piecemeal, and does not rely upon ICC review and interpretation.

#### Cons

- o Unless the industry becomes disenchanted with the ICC because of recent reforms by Chairman O'Neal, this option will get maximum opposition from carriers, labor and most shippers.
- o To the extent that adverse impacts on carriers and small communities do occur, they will be greater.
- o Carriers and some shippers will advance arguments of chaotic competition and the potential for anticompetitive practices absent regulation.
- o It may be difficult to organize general consumer support since

the perceived benefits to the individual consumer may be quite small although the overall national benefits could be quite significant . There will be no apparent consumer benefits from ICC-initiated reforms comparable to the airline experience to bolster the deregulation argument.

## OPTION 2. SUBSTANTIAL DEREGULATION THROUGH SELECTIVE LEGISLATIVE CHANGES

### Features

- a. Entry/Exit - Except for financial, insurance, and safety requirements, all entry and exit restrictions would be removed for TL carriers after a very short transition period. For LTL carriers, relaxed entry standards would be redefined legislatively to promote competition.
- b. Rates and Rate Bureaus - Collective ratemaking would be abolished and rate bureaus would lose their antitrust immunity. For TL carriers, no rate regulation would exist. For LTL carriers a "no-suspend" pricing zone would be instituted.
- c. Other - Other provisions would be the same as in Option 1. The repeal of restrictions on leasing, intercorporate trucking, and backhaul movements would be the same. Freight forwarders would be deregulated. The Department of Justice and FTC would have jurisdiction over mergers and the SEC would regulate securities.

### Arguments For and Against

#### Pros

- o more opportunity for monitoring the impact of deregulation legislation.
- o opposition may not be quite as vocal for this proposal as for

Option 1. This option could be characterized more as reform and not "a destruction of the whole system."

#### Cons

- o substantial political opposition from those affected, especially those who see this approach as only a first step.
- o it relies upon some administrative discretion to implement certain reforms and could be frustrated by a future uncooperative ICC. Because of this the anti-inflationary benefits are less certain.
- o there will be greater uncertainty over a longer period of time than Option 1 and it will be harder for carriers and shippers to plan.

NOTE - A combination of Options 1 and 2 could also be proposed, wherein TL traffic would be completely deregulated first and LTL traffic would be completely deregulated over a longer time period.

### OPTION 3. ADMINISTRATIVE ACTION AND LIMITED LEGISLATIVE CHANGE

#### Features

Legislation would be proposed to consolidate and expand upon the ICC's own reform initiatives. The Administration would continue to express its views through ICC filings and petitions. DOT's right to petition the ICC for rulemaking changes would be defined and increased. Selective legislative reforms would be offered to correct certain specific ICC restrictions. The goals of the I.C. Act would be amended in favor of efficiency and competition, and time limits would be imposed in all proceedings. Reform of rate bureaus could also be proposed, as a minimum; collective ratemaking would be severely restricted.

## Arguments For and Against

### Pros

- o reduces opposition to change, although the remaining opposition is non-trivial.
- o codifies current ICC initiatives and reduces opportunities for court challenges to ICC decisions.
- o provides maximum flexibility to adjust to possible unforeseen developments in the industry.

### Cons

- o depends to maximum extent on ad hoc, case-by-case approach to a fundamental transportation public policy issue. Uncertainty with respect to eventual regulatory structure makes it difficult for carriers and shippers to adjust and plan.
- o depends to a large extent on ICC interpretations that may vary with time.

## 5. Arguments Against Deregulation

After 43 years of regulation, truckers and shippers are understandably uncomfortable at the thought of substantive changes in the system. No matter which option is chosen, the following arguments will be raised in opposition. Evidence to refute them is fragmentary and incomplete in some instances.

1. "Deregulation will create chaos in the trucking industry. Firms will go out of business frequently, and shippers will be unable to depend on service."

RESPONSE: Increased turnover in an unregulated industry may result, but there is little evidence that significant disruptions in service will occur. Our experience with exempt and private carriers, and in minimally regulated intrastate markets, certainly doesn't support such an argument. Trucks are

easily sold and moved from one market to another. Reduced profit margins will place natural limits on entry, as will the need for shippers to trade off improved service quality with price.

2. "Deregulation will erode carriers' certificate values. This would be unfair to those who have worked hard to obtain operating rights, either through the regulatory process or through purchase."

RESPONSE: Certificate value that is derived from an artificial scarcity created by regulatory restrictions will certainly decline under entry deregulation. Their value, by all indications, has decreased substantially with the reforms initiated by the ICC. The value of an efficient, functioning carrier should increase, however, when crippling regulations are removed and artificial limits on growth are eliminated. For reasons of equity, of course, some form of compensation for certificate holders may need to be considered.

3. "Service to small communities will suffer if a common carrier is no longer obligated to serve particular points."

RESPONSE: A number of studies indicate that ICC enforcement of the common carrier obligation is now virtually nonexistent. Truckers who don't want to serve a point simply don't accept that traffic. However, many truckers specialize in small town service, and do so profitably. Others might find small town service attractive if entry restrictions were removed.

4. "Deregulation will encourage the proliferation of marginal, shoestring operators who will skimp on safety expenditures in order to make a profit."

RESPONSE The ICC doesn't regulate safety; DOT does. Economic deregulation won't change safety standards at all. Safety can always be improved, however, and DOT recommends that it be granted additional authority in

this area. A penalty system that acts as a greater deterrent, more reliance on civil penalties and better job protection for drivers who report safety violations would all be valuable safeguards. An effective entry standard that emphasizes safety and financial responsibilities could be put into the legislation.

5. "Deregulation will lead to dominance of the industry by a handful of large, powerful firms."

RESPONSE: A reduction in ICC entry restrictions should reduce industry concentration in many markets. The combination of antitrust enforcement, the large number of firms already in business, and the absence of any significant economies of scale will also serve to reduce industry concentration.

6. "Deregulation will create instability which will in turn create unstable working conditions. Organized labor will suffer particularly as deregulated firms rely more heavily on independent contractors."

RESPONSE: We do expect some efficiency gains, which may slow employment growth in the industry. There may also be some downward pressure on wage settlements. For these reasons, some form of labor protection provision will probably be demanded in the legislation.

7. "We don't need legislation because the ICC is already granting 96.7 percent of the entry applications before it."

RESPONSE: Statistics on the ICC's approval of new applications are misleading. They include applications that were only partially approved, and they don't count applications that were withdrawn before any action could be taken. The ICC has relaxed entry, but it is a long way from removing all entry barriers.

8. "Deregulation will increase highway congestion and the air and noise

pollution due to increased truck traffic."

RESPONSE: The number of trucking firms may indeed increase due to surface transportation deregulation, but that isn't the same thing as an increase in the number of trucks. With less circuitous routing and less empty mileage, a deregulated industry could carry the same amount of freight in fewer trucks and a larger amount of traffic in the number of trucks that exist today.

9. "If truckers can charge whatever they want, some big firms will underprice their services in order to drive small companies out of business -- and then raise their prices after the competition is gone."

RESPONSE: Protection against predatory pricing can be provided easily in the deregulation law, as it was in airline deregulation. If entry is sufficiently liberalized, truckers would have no incentive to cut costs to drive their competitors out because another competitor would always be waiting.

10. "Under deregulation, large shippers will use their market leverage to obtain better prices from carriers than small shippers could get."

RESPONSE: Discriminatory pricing also can be prohibited by law, if necessary. Large shippers already use their bargaining power to obtain better deals from carriers, and often can turn to private carriage. However, rate differences based on differences in transportation costs should be permitted and encouraged.

## RECENT ICC MOTOR CARRIER DECISIONS

There has been some significant movement in recent months at the ICC in modifying Commission policy respecting motor carrier regulation. This trend started largely with the appointment of Dan O'Neal as Chairman in April 1977.

In July 1977 an ICC Staff Task Force submitted a report to the Commission which contained 39 recommendations for easing entry. The Commission is reviewing these recommendations on a case by case basis. These recommendations have served as the focal point for reform in the area of operating rights. The following is a summary of recent notable decisions.

### 1. Protest Standards in Motor Carrier Application Proceedings - Ex Parte No. 55 (Sub No. 26)

On October 27, 1978, the ICC sharply limited the rights of those holding ICC licenses to protest applications by individuals seeking new certificates. These regulations will make it easier for new applicants to obtain interstate operating rights authority. Previously, the applicant was often subjected to lengthy and expensive hearings by carriers holding similar licenses. The Commission frequently ruled that because another carrier already held a license (even though that route authority is dormant), an additional firm's entry was unwarranted. The new protest standards should result in shorter, less expensive proceedings, and an increased likelihood that applications for new authority will be granted. The new rules take effect as of January 1, 1979.

### 2. Eased Entry - Liberty Trucking

On October 6, 1978, in a routine case involving regular-route, general commodities service between Chicago and two Wisconsin towns, the Commission reversed years of decision law and established a new precedent in operating rights cases by putting a heavy burden on existing carriers who protest the granting of new authority (130 M.C.C. 243). The Commission had previously interpreted "public convenience and necessity" to protect existing carriers. Under the Liberty Trucking standard, a carrier protesting a license application must prove that the "new competition is likely to materially jeopardize existing carriers' ability to serve the public." Even if the carrier is so impaired, the ICC may still award a new certificate, "if the benefits of heightened competition and new or improved service may outweigh the potential substantial harm to protestants."

### 3. Expanded Commercial Zones and Terminal Areas - Ex Parte No. MC-37 (Sub-No. 26)

The Commission's decision, issued December 17, 1976, substantially expanded commercial zones and freight forwarder terminal areas as a result of the promulgation of a new population-mileage formula. Commercial zones and terminal areas are zones - usually a municipality plus a described portion of the surrounding territory - within which motor carrier transportation is generally exempt from regulation.

4. Dual Operations - Ex Parte No. 55 (Sub-No. 27)

In this case, decided March 24, 1978, the Commission reversed its past practice and issued a general finding that the holding of both common and contract carrier authority is normally consistent with the public interest. The I.C. Act prohibits a carrier and its affiliates from holding both common carrier certificates and contract carrier permits authorizing transportation over the same route or within the same territory, unless the ICC finds that arrangement to be consistent with the public interest and the national transportation policy. In policy determinations of dual operation, the ICC refused to make these statutory findings if there appeared to be a "mere possibility" of discriminatory practices, and that standard often resulted in finding of objectionable dual operations solely because there was some degree of territorial overlap between the common and contract carriage.

5. Granting Private Carriers Operating Authority as For-Hire Carriers - Toto Purchasing & Supply Co., Inc.

In the 1938 Geraci decision (7 M.C.C. 369 (1938)) the Commission first articulated its long standing policy not to grant a certificate to an applicant who intends to use it primarily as an incident to carriage of its own goods and its own transportation business. On March 24, 1978, the Commission issued its decision in Toto Purchasing and Supply Co., Inc. Common Carrier Application, 128 M.C.C. 873, in which it broke with this long standing policy. In Toto, the Commission determined that motor carrier operating authority can be granted to the aforementioned type of private carrier provided (1) that the standard criteria for carrier applications are satisfied and (2) that the applicant is agreeable to the imposition of conditions requiring it to conduct its for-hire motor carrier activities independent from the other activities and to maintain separate records for each. This decision recognizes the Commission's diminishing concern for shielding shippers from discriminatory practices.

6. Limitation on Rate of Return - The Southern Motor Carrier's Rate Conference Case

In a case involving a freight rate request by the SMCRC, the Commission, using the case as a vehicle to determine standards for future motor carrier cases, disregarded its previous reliance on operating ratios in favor of the use of the rate of return on stockholders' equity. The Commission decided that the allowable rate of return should be no higher than that for all manufacturing industries - currently about 14%. This is substantially below the current composite figures for major motor carrier rate bureaus which are approximately 21% or the anticipated yield for southern carriers which was nearly 24%. The Commission specifically permitted a 3.5% rate increase, rather than the 6.2% requested. The Commission expressed the view that this smaller increase would be consistent with the Administration's anti-inflation guidelines. The permissible rate of return was sharply reduced because of a recognition that regulation insulates the industry from price competition.

# Daily Traffic World

## **O'Neal Is Told Congress, Not ICC, Will Make Future Regulatory Policies**

*Two Key House Public Works Chairmen Warn ICC Chief to Stop 'Adopting and Implementing' Substantial Changes in Trucking Until Congress Decides if it Is Necessary. Briefing Asked.*

The chairmen of the full committee and the subcommittee which will handle trucking deregulation legislation in the House have warned Chairman O'Neal of the Interstate Commerce Commission to stop "adopting and implementing" changes in trucking industry regulation until Congress has had a chance to decide whether "substantial changes" in the industry are necessary.

Other key congressmen also have written to the ICC in recent days criticizing ICC decisions which many say amount to *de facto* economic deregulation of the trucking industry.

The sentiments of Representatives Harold T. (Bizz) Johnson (D-Calif.) and James J. Howard (D-N.J.), the chairman of the House Public Works and Transportation Committee and its surface transportation subcommittee, respectively, were contained in a letter to Mr. O'Neal sent under both signatures on December 7. It is the second time in 10 months that Representative Howard has told Mr. O'Neal that substantive changes in the trucking industry are the business of Congress and not of the ICC acting by itself (T.W., Mar. 6, p. 17).

In their letter of December 7, Representatives Johnson and Howard noted that the Ninety-sixth Congress will convene in a short time and that regulation of the surface transportation industry will be one of the "critical questions" to be examined by Congress. They noted that except for railroads, all surface transportation falls within the purview of their committees.

The two chairmen then went on to say:

"Recently the Interstate Commerce Commission has engaged in a great deal of activity aimed at changing the scope and application of economic regulation in

that industry. Many of the changes significantly alter the way in which the surface transportation industry is to be regulated. Although some of these changes affect policies that we believe should be implemented by the Commission, most do not.

"It is, therefore, our request that the Interstate Commerce Commission stop its program of adopting and implementing new policies that substantially alter the manner in which the surface transportation industry is regulated until this committee has had an opportunity to hold hearings on this subject, and until this committee and the Congress have had an opportunity to decide whether substantial changes in the economic regulation of the industry are necessary.

"Certainly, the Commission and other interested persons will have every opportunity to appear before the committee and to present views on why regulatory changes are necessary. However, the adoption and implementation of far-reaching policies that alter and reverse the scope of economic regulation are clearly matters of congressional policy and must be decided by the Congress.

"We therefore again request that the Commission's efforts instituted to change substantially the economic regulation of the surface transportation industry not be implemented until the Congress has had an opportunity to review them and to decide whether or not the proposed changes are in the public interest as a matter of congressional policy."

Mr. O'Neal has also received at least two other letters from congressmen expressing grave concern over the Commission's recent decision in the Southern Motor Carriers Rate Con-

ference general rate increase wherein the Commission set a 14-per-cent "threshold guideline" rate of return based on stockholders' equity for the trucking industry and rolled back from 6.2 per cent to 3.5 per cent a general rate increase granted the conference last April (T.W. Dec. 4, p. 43).

One of the letters came from Representative Bo Ginn (D-Ga.), chairman of the Public Works and Transportation Committee's subcommittee on investigations and review. Representative Ginn said, that "while the Congress can and may well wish to revise the scope of authority it has afforded the Commission, it certainly has not yet done so." Representative Ginn then told Mr. O'Neal to arrange a briefing of his subcommittee staff by "appropriate members of the Commission staff" within the next two weeks. His letter was written to Mr. O'Neal on December 6.

Representative Stephen L. Neal (D-N.C.), noting that trucking was a major industry in his Congressional District and throughout his state, called the decision a "major blow to the industry" and one that could threaten the financial stability of a number of firms. He said in his December 4 letter the SMCR has indicated that it would ask the Commission to review its decision and asked Mr. O'Neal to grant such a review.

The text of the letter to the ICC chairman from Representatives Ginn follows:

"I want to take this opportunity to bring to your attention some of my concerns about the recent Commission decision in Docket No. H-29772 involving the suspension of the general rate increase sought by the Southern Motor Carrier Rate Conference.

"A number of Members of the House, some of my own constituents, and other people from around the country, have contacted me about this decision. They point out that it represents an unprecedented departure from the traditional method used to evaluate revenue need in motor carrier rate cases. They have likewise noted that the Commission has indicated it regards the decision as a major one which will be used as precedent for other rate cases. Finally, they estimate that as a result of the decision as many as forty per cent of southern motor carrier firms may be forced into bankruptcy, leaving a large portion of the public unserved by necessary truck transportation. This would appear to be at odds with the Commission's own responsibility to oversee the public interest.

"My own particular concerns, Chairman O'Neal, are twofold. First, I have been following the general pattern of ICC regulation in the last few months and have sensed that there may be an inconsistency with the intent of Congress when it created the Commission and empowered it to regulate motor freight transportation. While the Congress can and may well wish to revise the scope of authority it has af-

forded the Commission, it has certainly not yet done so.

"Secondly, as chairman of the Public Works and Transportation subcommittee on investigations and review, I think it is important for my own subcommittee staff to have a full briefing on the technical points and implications of the SMCR case since it does represent a radical departure from previous policy. Consequently, I would like for you to have appropriate members of the Commission staff arrange to meet with the professional staff of the subcommittee within the next two weeks. I ask that you contact the staff director, George Kopecky, or Charles Prisk at 225-3274 to work out these details."

Representative Neal's letter to Mr. O'Neal read:

"On November 27, 1978, the Interstate Commerce Commission ruled that a 6.2-per-cent increase in trucking rates, granted to the Southern Motor Carriers Rate Conference earlier in the year, would have to be rolled back to 3.5 per cent.

"To many, this decision represents a major blow to the industry; one that could seriously threaten the financial stability of a number of trucking firms still struggling to recover from the nationwide strike of 1975. Through the rate hike, the industry had hoped to recoup much of the losses incurred by a recent Teamster pay raise of 10.4 per cent combined with the incessant cost of inflation.

"It has been pointed out that individual companies may request higher rates. However, this is not a viable option for most, as it would tend to place a company at a competitive disadvantage, further hampering recovery.

"Trucking is a major industry in my district and the whole state of North Carolina. It is the "life-blood" of commerce, whose health is of immense importance to the national economy and too important to risk hasty judgment.

"The Southern Motor Carriers Rate Conference has indicated that it will petition the Commission to review its decision. I would urge you to grant such a review and allow the industry to resubmit its case.

"Thank you very much for your consideration."

There was no comment from Mr. O'Neal on the content of the letters. His office said he would be responding to the letters from the congressmen later in the week.

Bruce N. Hatton, ICC congressional relations officer, said December 11 that Chairman O'Neal received the letter from congressmen Howard and Johnson on December 8. He said that the chairman was "looking forward to sharing with and explaining to Congress" the Commission's regulatory reform objectives.

According to Mr. Hatton, Mr. O'Neal emphasized that what the ICC is doing in the area of truck deregulation is within the legal framework of its statute.

Mr. Hatton said that the ICC has a duty to keep Congress "out of the dark" regarding the agency's objectives for deregulation.

Tab D

INTERAGENCY TASK FORCE\*  
TRUCK REGULATION REFORM OPTIONS

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\*This options paper is the result of a task force consisting of representatives of the Departments of Agriculture, Commerce, Defense, Energy, Justice, Labor, and Treasury, the Council of Economic Advisors, Council on Wage and Price Stability, Federal Trade Commission, Interstate Commerce Commission, Office of Consumer Affairs, and the Office of Management and Budget.

## TRUCK REGULATORY REFORM OPTIONS

### I. INTRODUCTION - THE NEED FOR CHANGE

Meaningful change of the system for economic regulation of the trucking industry should be a key point of the Administration's agenda for the 96th Congress to:

- . Fight inflation by reducing motor carrier rates;
- . Reduce the inefficiency and fuel waste of the present system;
- . Reduce unnecessary red tape and bureaucracy; and
- . Reduce barriers to minority participation in the trucking industry.

A number of agencies on the interagency task force have urged that deregulation of the intercity bus passenger industry be included in this options paper. It is not included because the truck options paper has involved a major effort and there has been no full consultative process with the bus industry, and because we believe it so important to tie truck deregulation with that of rails. DOT will be considering bus passenger deregulation, and developing a separate bus options paper, over the next few months.

### INFLATION

Today's truck regulation stifles competition by limiting entry and allowing collective rate setting. Without competition or the threat of competition rates are inflated since carriers have little incentive to hold down cost increases, let alone reduce their rates. Critics of regulation maintain that billions of dollars in waste results.

When motor carrier economic regulation was instituted in 1935, broad authority was provided the Interstate Commerce Commission (ICC) to regulate

entry. The focus in entry proceedings before the ICC has traditionally been to protect the existing carriers. The result is that there are about 40% fewer regulated carriers in the industry today than in 1940, despite the tremendous economic growth experienced in the meantime. The ICC has taken some steps recently to ease entry, as will be discussed later.

The existing system also limits competition by allowing motor carriers to meet among themselves to agree upon rates in rate bureaus.\* These bureaus operate under a special exemption from antitrust laws which would normally outlaw such joint pricing. While the ICC has authority to review the rate bureau decisions, historically this authority has been used to minimize competition.

In addition to the logic of economic analysis there is real world evidence that rates are too high. Much of it comes from comparisons of similar truck freight moving in regulated and unregulated markets. The Federal economic regulatory system does not apply to totally intrastate movements. Certain states, such as New Jersey, have only minimal economic regulation of trucking. A recent DOT study<sup>1</sup> compared unregulated intrastate New Jersey movements with regulated interstate traffic and concluded that rates on the unregulated movements were 10%-15% lower than the regulated movements.

Comparisons of rates in other unregulated sectors — within so-called "commercial zones" around urban areas — show that rates of regulated household movers may be 40%-67% higher than rates of unregulated movers.<sup>2</sup> In the mid-1950's, when movement of some agricultural products became unregulated, Department of Agriculture studies<sup>3</sup> found lower rates and better service resulted. Four foreign countries' experience with deregulation also provides evidence that less regulation provides lower rates. While some analysts believe that

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\*A glossary of technical terms used in this paper is found at Tab E.

rates increased subsequent to the British deregulation of trucking, there is evidence that deregulation did cause some real rates to decrease.<sup>4</sup>

Additional evidence that rates are too high is the inflated value of trucking certificates and operating authority. The total market value of these certificates was estimated by the American Trucking Association<sup>5</sup> to be in the billions of dollars in the early 1970s. This is well beyond any amount that could be attributed to ordinary business "goodwill." Certificates can have such high value only because they reflect the present value of future inflated profits which certificate buyers expect to be able to earn because they can charge more than they could without ICC limitations on entry and antitrust exemptions. It is interesting to note that industry financial experts have indicated that the market value of certificates has dropped dramatically in the last few months. This decline in market values evidently reflects uncertainty associated with fears the system may be deregulated and rates will have to come down as the industry becomes more competitive.

A final piece of evidence comes from the analysis of the impressive profits in the trucking industry. The ICC figures for 1976 indicate that large firms averaged returns on equity of nearly 24 percent.<sup>6</sup> This is extremely high in an industry that does not require large capital investments, where there are no particularly large economic risks, and where lower returns would otherwise be expected. This figure compares with an average of roughly 14% return on equity in manufacturing.

#### INEFFICIENCIES AND WASTED FUEL

Existing regulation causes carriers to operate less efficiently than they could, raising costs and wasting fuel. Moreover, it stifles innovation, both in technology and in price/service options. Operating authority is normally narrowly granted, either by restricting the commodities a trucker can carry

or the routes he may travel. The current system of fragmented authority also leads to excessive interlining between carriers, delays in shipment delivery, and increased industry costs. Empty backhauls, lower load factors, and circuitous routes also result. For example:

1. In one example cited in a study by the Federation of Rocky Mountain States,<sup>7</sup> the highway mileage between Denver and Albuquerque was calculated to be about 400 miles, but the carrier's authority required it to go along a 700-mile route between these two communities. In another instance, a carrier had to go almost 900 miles to make what was usually a 540-mile trip between Denver and Omaha.

2. Because would-be carriers know that entry is tightly restricted, they often write their applications very narrowly to maximize the chance for getting into the market at all. The following are examples of applications taken from a few pages of a recent trade publication:<sup>8</sup> authority to transport glass containers, not exceeding one gallon capacity, between three small towns in Pennsylvania (named) and one city in New Jersey; authority to transport skeet and trap targets from one point in Indiana to points in five states; authority to transport prepared dough in vehicles equipped with mechanical refrigeration from a city in Georgia to named points in several states.

3. The regulatory system imposes inefficiencies on both the regulated and the unregulated. Carriers are allowed to transport unprocessed agricultural items without ICC authority, but they may not carry regulated commodities. An exempt agricultural carrier may carry fresh produce to the canning plant but may not transport canned goods on the return trip as an exempt carrier. He may enter into a separate arrangement with a carrier with authority to carry canned goods from that plant, but there are restrictions on exempt carriers' ability to make such arrangements.

The result of such restrictions is an excessive number of trucks on the highways with empty backhauls, partial loads, or on circuitous routes. DOT-ICC data<sup>9</sup> show that more than 16% of unspecialized ICC-regulated vehicles travel empty. An even larger percentage of exempt vehicles travel empty. These empty trucks and unneeded miles increase the truckers' costs and waste fuel. A Department of Justice study<sup>10</sup> estimates that the circuitry requirements alone waste at least 51 million gallons of fuel per year.

#### UNNEEDED BUREAUCRACY AND RED TAPE

The existing system is needlessly complex and cumbersome. A major issue is why over 2,000 federal bureaucrats are needed to regulate the business practices of what would otherwise be a good example of a competitive industry. There are literally hundreds of thousands of pages of tariffs (rate notices) filed each year, and sometimes individual tariffs go on for pages with intricate formulas and complicated calculations. The system also produces endless red tape. The last annual report of the ICC indicates that almost 8,000 cases were filed for motor carrier operating rights alone. There may be even more applicants this year. In addition, millions of rates are filed with the Commission annually. Even under more expedited Commission action cases can take months and years, and this means that businessmen who should be spending time thinking of ways to improve their operations, instead, have to think of ways of moving through the labyrinth of the current regulatory system.

#### INEQUITIES AND SOCIAL COSTS

The regulatory maze is particularly burdensome to small businessmen. Large businesses may be able to afford experts to wade through the complicated regulations and wait the long months to obtain decisions, but this is not true for the small entrepreneur.

The regulatory system has worked to restrict the opportunities for minorities

to participate in the industry. This was not intentional, but it nevertheless happened. As mentioned earlier, most of today's operating authority can be traced to that authority created by the "grandfather" provision of the 1935 Act. Minority participation was quite limited in the industry at that time, however, and the restrictive entry policy has meant that minority participation in the industry has remained very low. For example, according to available evidence, of the 2,500 interstate household movers, less than 1% are minority-owned and no minority-owned carrier has broad geographic authority to move household goods.<sup>11</sup>

## II. STRUCTURE OF THE INDUSTRY

The trucking industry accounts for over half of total intercity freight revenues. ICC-licensed carriers account for just over 20 percent of the industry's total intercity ton-miles. In 1976, the estimated value of intercity motor freight services (both regulated and non-regulated) was estimated at \$56 billion; regulated carriers had operating revenues of \$26 billion. The trucking industry earns more revenue for services provided than any other industry in the transportation sector. There are approximately 17,000 regulated trucking companies in operation today. The industry employs more than one million people and is highly unionized, principally by the International Brotherhood of Teamsters.

The internal structure of the industry is highly mixed and can be categorized in many ways. One logical way is to divide carriers into those that provide truckload (TL) and less-than-truckload (LTL) traffic. Carriers providing TL and LTL have different operating patterns, costs and organizational structures, and provide very different types of freight service to shippers.

One way of defining truckload traffic is any truck rig that moves under a single bill of lading. In general, TL shipment consist of a point-to-point (shipper-to-consignee) shipment that "fills" a trailer. The concept of "fullness" depends upon the nature of the carrier's operations and the type of traffic carried, as well as the services demanded by the shipper. LTL traffic are those movements that do not fit the truckload (TL) definition. In terms of freight revenues, LTL carriers earn the majority of industry revenues.

## 1. ICC-Licensed Carriers: Less-Than-Truckload (LTL)

LTL motor freight service is almost exclusively provided by regular-route common carriers of general freight. Regular route certificates specify all the points of origin and destination along with the detailed routes over which the carrier must travel. Common carrier service is provided by LTL carriers for a wide variety of packaged goods (general freight). Up to 90 percent of total LTL shipments weigh less than 1,000 pounds. The motor carrier services provided by LTL carriers can require fairly substantial terminal investment and handling operations to consolidate or distribute individual shipments before or after line-haul movements. These carriers essentially provide regularly scheduled service, often interchange traffic with other carriers, and rarely use specialized equipment. This segment of the industry is heavily unionized (both drivers and dock workers); and employees are typically covered by the Teamster Master Freight Agreement. In most cases, the rates charged for these shipments are collectively agreed upon and then proposed to the ICC regional rate bureaus. LTL carriers are not as prone to cyclical downturns or seasonal/peak-period service demands, as are other sectors of the motor carrier industry. Although the requirements for terminals and facilities pose some economic entry barriers, they are far from overwhelming, especially in comparison to other industries, such as the airline industry now being deregulated.

2. ICC Licensed Carriers: Truckload (TL) There are several categories of carriers which provide truckload service. Typically, TL shipments move directly between the shipper and consignee, thereby bypassing the distribution and consolidation operations which characterize LTL shipments. In comparison to the class rate structure of LTL movements, TL rates are more closely related to the carrier's cost of providing a particular service. This is because

TL carriers are constrained by competition from railroads and the threat of private carriage. TL carriers often require specialized equipment (e.g., tank trucks) and are closely limited in terms of the commodities they may transport, but generally have wide latitude as to the routes over which they may operate. The TL category is composed of two broad groupings: specialized common carriers and contract carriers.

a. Specialized Common Carriers The ICC separates specialized common carriers into 16 different commodity categories (e.g., liquid petroleum, refrigerated products, household goods, etc.). Specialized carriers generally have irregular-route operating authority, and handle full truckload shipments of freight. Traffic levels for these carriers have increased rapidly. The typical movement involves almost no consolidation with shipments of other commodities or parties, and the average size of a shipment is usually quite large. Specialized carriers rely heavily on the service of independent truckers (owner-operators), who lease their service and equipment to carriers holding this type of authority.

b. Contract Carriers Approximately 4,000 carriers are classified as contract carriers. The essential distinction between a common carrier and a contract carrier is that contract carriers do not hold themselves out to provide service on demand. They provide dedicated service and often specialized equipment to meet the unique transportation needs of individual shippers. Unlike common carriers, the rates charged for these movements are negotiated between the carrier and the shipper, and ICC has only minimum rate authority. The contractual agreement can be long-term in nature, and is filed with the ICC. Historically, the Commission has limited the ability of a contract carrier to provide dual operations; i.e., both contract and common carriage by the

same operator. The Commission has recently undertaken some reform in this area.

The Commission also places arbitrary restrictions on the number of shippers a contract carrier can serve, which only reduces competition with other types of carriers while unfairly constraining the growth of contract carriers. These restrictions tend to discriminate against small shippers. Since a contract carrier can only serve a limited number of shippers, it has every incentive to enter into contractual arrangements with the largest shippers it can find. The overall effect of this restriction results in inefficient and costly system-wide operations.

### 3. Non-ICC Regulated Carriers

a. Private Carriage A private carrier is a company whose primary business is not transportation (e.g., a supermarket chain), which hauls its own property. Private carriage, which accounts for the largest single component of intercity motor freight traffic, has varied operating practices and service needs. At the present time, private carriers are prevented by the ICC from entering into for-hire operations for their own corporate subsidiaries, and from entering into short-term agreements for leasing equipment to a common carrier. They are also prohibited from employing owner-operators in the transport of their own traffic. These restrictions are particularly unproductive in that they lead to excess capacity, poor fuel utilization, and extra costs. Nevertheless, private trucking has grown rapidly.

DOT studies<sup>12</sup> demonstrate that companies turn to private trucking when they are dissatisfied with existing regulated carriers. This dissatisfaction is especially pronounced when specialized equipment is required or when shippers

desire new or alternative transportation services. The relative size of private trucking operations — and the fact that a recent survey<sup>13</sup> found that a majority of large industrial shippers planned to increase the size of their private trucking operations significantly — indicates substantial problems with the level and structure of rates and services provided by regulated carriers.

b. Exempt Carriers Various exemptions from economic regulation are specified within the Interstate Commerce Act. The single most important exemption involves the movement of unprocessed agricultural commodities. These commodities are transported primarily by the estimated 100,000 or more owner-operators, who provide a highly flexible service to meet rapidly changing demands for agricultural movements. Through relatively high productivity, these truckers achieve costs which, at least under the present regulations governing rail traffic, make them cost-competitive with railroads in many transportation markets. As a result of their flexibility and competitive rates, they have captured a large part of agricultural traffic that once moved primarily by the railroads.

As noted above, however, because they are "exempt" does not mean they operate without restrictions or could not carry freight more efficiently. In addition to statutory impediments, regulations also limit the ability of owner-operators to solicit and participate in transporting regulated traffic. Owner-operators are also prohibited from carrying regulated and nonregulated traffic simultaneously.

### III. ICC REGULATION AND RECENT TRENDS

With the appointment of Chairman O'Neal in April, 1977, the Commission embarked upon a reexamination of many procedural and substantive aspects of its regulation of interstate truck transportation. A task force composed of six members of the Commission's staff was appointed to make recommendations for improving truck entry regulation. The Task Force's report, submitted July 6, 1977, contained 39 recommendations for easing entry control which the Commission has recently been deciding on a case-by-case basis. While these reforms represent an important first step toward liberalizing entry, the Commission could have gone significantly further in dismantling the numerous obstacles to entry and in reforming other areas of its authority, especially pricing flexibility and rate bureau reform.

1. Entry Before a new carrier may enter the industry or before an existing ICC carrier may expand its authority, approval must be obtained from the ICC and a determination made that the applicant is "fit, willing and able" and that the proposed service is required by the "public convenience and necessity". The Commission's three standards pertaining to public convenience and necessity entry were developed in 1936 in the seminal Pan American decision. 1 M. C. C. 190 (1936). In its consideration as to whether an applicant has satisfied the public convenience and necessity standard, the Commission determines whether (1) the applicant has established a public need for the proposed service; (2) the existing carriers can satisfy the demonstrated service need; and (3) the proposed service will cause protestants to suffer competitive harm of such degree as to outweigh the benefits to the general public. These criteria

have remained unchanged to this day despite fundamental structural changes in the economy and the trucking industry.

Historically, the applicant had the burden of proving that the proposed service was required by the public convenience and necessity. On October 6, 1978, in the Liberty Trucking decision, 130 M. C. C. 243, the Commission reversed years of precedent by shifting the burden of proof regarding the third criteria to the existing carriers who protest the granting of new authority. In another recent decision, the Commission issued final rules which sharply limit the carriers permitted to intervene automatically in operating rights cases to those who not only hold a certificate similar to that being sought, but who have in fact performed the service in the recent past. These restrictions, which place a burden of proof on protesting carriers, should make it easier for new applicants to obtain operating authority by reducing previously lengthy and expensive hearings. These rules represent some reform toward liberalizing entry, but do not eliminate many impediments to entry.

On November 30, the ICC proposed a rulemaking proceeding which, if adopted, would represent the most significant change in the Commission's traditional "protectionist" attitude. Under the proposed policy, an applicant would merely have to demonstrate that the service being proposed would "serve a useful public purpose, responsive to a public demand or need." New common carrier authority would be granted commensurate with the demonstrated need unless the existing carriers could demonstrate that a new carrier would impair their operations contrary to the public interest. In essence, this proposal shifts the burden of proof for showing the potential disruptive effects on existing carriers to those same carriers, thus eliminating the need for an applicant

to prove that the service it proposes cannot be performed by existing carriers. In addition, the proposed policy would loosen requirements for contract carriers. Opponents would have to establish that granting new contract authority would so endanger their operations that they would not be able to provide adequate service within the scope of their authorities. If adopted, and if the Commission does not place a heavy burden on applicants to demonstrate a public need for the proposed service, the proposed rules would ease entry significantly. These rules would still allow the potential for fit and financially responsible carriers to be denied entry into the industry even though they proved a need for their service, however.

2. Ratemaking Trucking rate reform involves primarily three major issues: (1) collective ratemaking; (2) the structure of rates; and (3) rate flexibility. These issues must be addressed if true reform is to be achieved.

The ICC has wide discretion to determine maximum and minimum rates for common carriers. The Interstate Commerce Act also gives the ICC authority to approve collective ratemaking agreements. These agreements are conducted in rate bureaus: private associations of common carriers who discuss and determine rates for individual shippers. All motor carrier rate bureau members (whether they carry the traffic or not) may discuss and vote not only on joint and through rates (where two or more carriers are involved in one shipment) but also on single line rates where only one member is involved. In addition, these rates are based on the average cost of a sample of the larger carriers not the lower costs incurred by the more efficient carriers.

Rate bureaus were granted antitrust immunity in 1948 with the passage of the Carriers' Rate Bureau Act (more commonly known as the Reed-Bulwinkle

Act). In essence, this Act allows potential competitors to agree upon rates and file them with the ICC. The anticompetitive effect of these organizations on rates charged is largely responsible for the shift toward private carriage and excess industry earnings. The ICC has the authority to review rates but generally has accepted rate bureau proposals. In those few cases where the Commission has suspended rates, it has attempted to set rates so as to maintain the existing rate structure. One recent decision, however, indicates that the Commission is questioning the current system of ratemaking. On November 27, 1978, by overturning a general rate increase proposed by a major rate bureau, the Commission overhauled the criteria that motor carriers must meet to justify future rate increases. Moreover, the Commission determined that the profits of the motor carrier industry were already inflated. The ICC further decided that the rate of return for motor carriers should be no higher than that for all manufacturing industries (approximately 14 percent), which is substantially below the current composite return for the major motor carrier rate bureaus.<sup>14</sup>

Inadequate pricing flexibility also currently exists. Rates based upon the level of service provided for an individual shipper, not rates based on the average costs of a group of carriers as currently practiced through collective ratemaking, are highly desirable. Flexible and innovative ratemaking would yield significant benefits to both shippers and carriers. Shippers would be able to select those rate/service features which most fully reflect their shipping requirements. A carrier relying upon flexible pricing could implement different levels of freight service. Through flexible pricing a carrier could charge rates that reflected these service differentials. For example, scandalous over-booking

in summer months by household goods carriers results, in part, from ICC regulations that do not permit peak load pricing. Since carriers are unable to balance demand through price incentives in off-peak months, they overbook for five frantic months of the year, with a resulting deterioration in service.

3. Mergers Motor freight common carriers have sought end-to-end mergers as a means of balancing traffic flows, decreasing circuitry, increasing equipment utilization, and improving service to shippers. More expedited traffic movements and fewer joint movements of traffic between carriers often lead to service improvements and cost savings for both shippers and carriers. Under existing law, motor carriers are only permitted to merge when the Commission determines that the merger is consistent with the public interest. Carriers with combined revenues under \$300,000 do not have to seek ICC approval for merger.

Regulatory restrictions on entry, especially for established carriers seeking to broaden their operating authority into new geographic and commodity markets, provide trucking companies with incentives to merge. Carriers interested in expanding their authority have often merged with other carriers holding the desired authority, rather than pursue the lengthy, costly, and sometimes futile process of seeking additional authority through Commission procedure and review. Under liberalized entry, a carrier's incentive for intra-industry mergers as a means of rationalizing its own route network would be reduced dramatically.

In its policy statement of November 30, 1978, the Commission expressed concern that its current merger policy may lead to the reduction of effective competition and service, especially in short-haul markets and small communities.

Frequently, a long-haul carrier will purchase the authority of a short-haul carrier and use that new authority as a means of extending its long haul service into another market. The Commission has announced that if a new service is intended by the merger, the proper vehicle is the filing of an application for new authority. Under the proposed rules, the Commission will authorize an acquisition of operating authority only if the acquiring carrier establishes that it will continue to perform service similar in scope to that performed under the operating authority being acquired.

Intermodal mergers between railroads and motor carrier are presently restricted by Commission policy. Intermodal ownership and operations would increase the coordination between the modes and achieve cost economies for the participating carriers and increased service options and benefits for shippers. By increasing the attractiveness of multimodal service, the different modes could specialize in those transportation functions they perform most economically (e.g., rail carrier linehaul movements and motor carrier pickup and delivery). Rail ownership of trucking companies should be encouraged as a means of achieving more appropriate and profitable transportation service on low-density branchlines. Forced maintenance of rail service on such routes is a serious drain on the rail industry's currently poor earnings. Further, decreasing costs and improving the service for intermodal movements would bring about a more appropriate intermodal division of traffic based upon lower shipment costs.

### CONCLUSION

Although the ICC's proposals do not eliminate all the problems created by the motor freight carrier regulatory scheme, these proposals represent

a step towards regulatory reform. Further reforms could be expected if new commissioners were appointed who supported the Administration's economic policy favoring deregulation. There are currently five Commissioners plus one acting until a replacement is named. Thus effectively there are six vacancies on the Commission. In addition, two Commissioners' terms will expire at the end of 1979 and two more at the end of 1980.

However, even if the Commission were to propose more substantial reform, a major legislative thrust would still be required to achieve the objective of significant lasting reform.

Without legislation, the ICC's apparent forward movement could be hindered by several developments. First, the proposed ICC reform initiatives will take a very long period to achieve. The individual dockets designed to effectuate reform on each aspect of the motor carrier industry could take several years. Second, even after the Commission does act, it is likely that any significant administrative reform will be tied up in litigation, perhaps for several years, with an uncertain outcome. The American Trucking Association and other affected parties will contest any significant Administrative reforms in the courts.

Finally, many of the ICC- proposed reforms, even if subsequently adopted, will not be cemented into the law without legislation. Future Commissions could undo the work of a reform Commission. A somewhat similar situation was faced with the air deregulation bill. With the support of this Administration, the CAB instituted far-reaching changes to deregulate the air carriers. The question was raised at that time whether legislative change was still needed. The unanimous response by the Administration and the CAB was to continue

to seek legislative change. Chairman Kahn himself testified that without legislative change, the CAB faced long internal proceedings and monumental lawsuits. In order to achieve lasting regulatory reform for motor carriers, as well, some form of legislation is necessary.