

EXECUTIVE OFFICE OF THE PRESIDENT
OFFICE OF TELECOMMUNICATIONS POLICY
WASHINGTON, D.C. 20504

deregulation

Date: November 5, 1970

Subject: Deregulation of Radio

To: Mr. Whitehead

We keep talking about doing away with federal regulation of programming when cable comes in. Maybe the way to start is to deregulate AM and FM as an "experiment."

Program:

1. Starting in 197x, there will be no further regulation of AM and FM radio stations in any market which has at least four such stations plus at least one TV station and one daily newspaper.
2. Deregulation means no licensing, no fairness doctrine and no other regulation except (a) that which is required by law (e. g., equal time) and (b) technical standards to prevent interference.
3. Present stations would be vested in their present owners at existing powers and frequencies. New assignments within existing allocations to highest bidders.

This should be a very popular idea with the broadcasters (until they begin to think about it), and the FCC should like it, since they don't really regulate radio anyhow, and this would save them a lot of paperwork. Indeed, the only obvious source of opposition is the bureaucracy.

Bruce
Bruce M. Owen

After we get some of our pressing agenda squared away, let's explore this -- but we need more options & probably a very clever rationale for why our better regulation would be in the public interest. I basically like the idea.


EXECUTIVE OFFICE OF THE PRESIDENT
COUNCIL OF ECONOMIC ADVISERS
WASHINGTON, D.C. 20506

August 6, 1970

MEMORANDUM FOR TRANSPORTATION SUBCOMMITTEE

Subject: Working Group Report

Attached is the report of the working group to the Transportation Subcommittee. While it considers the benefits to railroads from deregulation, the impact on union wage settlements is not treated. Theoretically, regulation, especially the type imposed by the ICC on trucking, could be expected to generate higher wages. However, there is no reason to believe that the rate of increase in wages should be higher than elsewhere. Nor is there any empirical evidence that wages or wage rates in regulated industries exceed those in markets equally unionized and with equal skill levels. Since the case for deregulation is so strong in any case, and the wage level/regulation issue so cloudy the working group felt that it would be better to leave that issue out of the report. However, the working group would recommend that a committee of DOT, Labor, and CEA be formed to consider the effect of regulation on unionization and wage levels generally.


Thomas G. Moore

IMPROVING THE PERFORMANCE OF THE TRANSPORTATION INDUSTRIES

This paper briefly describes the advantages to moving towards a more competitive market allocated system of transportation. It presents a selection of major options available and indicates the advantages and disadvantages of each. This paper does not, however, consider political strategy, though it is the opinion of the working group that not only will the program, whichever it may be, have to be sold to the various transportation industries but shippers and the public must be thoroughly educated for the program to have a success.

I.

Cost of Regulation

Regulation has led in general to higher rates for transportation, though there are products and particular routes which are being subsidized by other areas. Overall though rates are higher than they would be were the industry unregulated; this is especially true in trucking.

Higher rates for transportation have not led to higher profits for most firms but have been absorbed through higher costs and inefficiencies. A 1944 study found that 70 percent of the regular route common carriers did not have full authority to serve intermediate points on or near their specified routes. Some had no such authority.

Irregular route carriers were generally confined to radial activity with pickup and delivery limited to one or more specified points within their territory. Such carriers have to pass up business at points between their authorized terminals. Regular route carriers were required to follow specified highways with the result that they often had to use circuitous routes. One-third of the interstate truckers had return haul limitations and almost one-tenth had no return authority at all. While this is a rather old study there is no reason to believe that conditions are any better today. In fact, comparisons between regulated and unregulated trucking indicate considerably higher costs for the former.

Regulation by holding rates above competitive levels has encouraged excess capacity. With fixed rates, traffic will flow to the carrier with the most capacity; this minimizes waiting time for shippers. Thus each firm competes by providing more capacity than the traffic warrants. The result is considerable economic waste; even the motor carriers don't benefit since the profits are competed away.

Regulation has led railroads to emphasize bureaucratic procedures. Innovation has been stifled; experimentation held up or prevented. Regulation has forced railroads to operate uneconomic services on particular lines. The cross-subsidization between freight

transportation and passenger transportation is too well known to need elaboration. Thus railway costs have been inflated by regulation.

The economy has also suffered from the rate structure which has often resulted in a higher cost mode, carrying traffic that could be more efficiently carried elsewhere. Higher rates on scrap materials than on new has discouraged recycling and have added to the solid waste problem as well as led to a faster use of raw materials. Higher rates for fabricated materials over unfabricated have encouraged manufacturers to locate close to their markets, often in major metropolitan areas, rather than near their raw material supplies. This has aggravated population concentration and pollution.

Cost to Shippers

A casual estimate of the enhancement of the common carrier freight bill may be made on the basis of the sample of the deregulation of carriers of chickens and frozen foods by judicial decisions in the 1950s. Fresh-dressed poultry movements were deregulated in 1953 and frozen poultry movements in 1956. The Department of Agriculture attempted a before- and after-study of 144 poultry processors and 67 truckers, comparing 1952 and 1955 experience with 1956-57 experience. The Department found that rates had fallen by 33 percent for fresh and 36 percent for frozen. The Department, studying the general deregulation of frozen food movements when they were found to be subject to the agricultural exemption in 1956, found that rates had fallen by amounts from 11 to 29 percent by 1957, averaging 19 percent. If

anything, this is an understatement because the Department also found an improvement in quality of the service with respect to willingness to handle small shipments, or to provide service to multiple destinations.

The courts' finding that these movements were exempt was presumably random with respect to the level of rates being charged. That is, there is no reason to believe that these commodities were in some sense atypical. Thus, we are probably justified in presuming that individual common-carrier trucking rates, if deregulated, would fall by about 20 percent. The behavior of the railroads in the "umbrella ratemaking" cases is roughly consistent with this. At least in a large number of instances, mainly on barge-competitive traffic, the railroads manifested a willingness to cut rates by similar amounts.

This leads one to a tentative conclusion that regulation raises the common-carrier freight bill by some 20 percent, which would put the cost between \$4 and \$5 billion per year. Unfortunately, such an estimate would have two biases. The decartelization of a part of a cartelized industry will result in an inflow of resources such that the price will fall more than if the entire industry were decartelized. Since the cartel will presumably have generated excess capacity in the industry, the price may fall to a lower level than would have prevailed under

competition, as, for example, gas prices go to a level probably below competitive during "gas wars."

Second, it is by no means clear that all rates are artificially elevated. Some, such as bulk agricultural commodities and some products of mines, may be below the levels which railroads would charge in absence of political pressure for depression of rates. George Hilton reported in his book, The Transportation Act of 1958, that railroads are thought to fail to cover "out of pocket" costs on some 23 percent of traffic. There is no likelihood that rates would fall on such traffic by 20 percent.

Such biases are probably no greater than 50 percent. This leads to a casual estimate of the lower bound of \$2 billion. Thus regulation probably elevates the common-carrier freight bill by \$2 to \$5 billion a year.

Cost to the Economy

The cost to the economy of regulation is probably considerably less than this at any one point in time. Some part of these higher rates have simply gone to enrich firms with entrenched positions and possibly into higher wages for workers. This means that while shippers are worse off by \$2 to \$5 billion, some individuals in the transportation industry have been made better off. But in addition there is real waste that benefits no one.

No one has ever attempted a rigorous estimate of the cost to the economy of the regulation of transportation. There are, however, some casual estimates of the cost of regulation. Notably, Ann F. Friedlaender in a recent Brookings study, The Dilemma of Freight Transport Regulation, attempts an estimate of the loss from the misallocation of freight among modes stemming from the survival of discrimination in tariffs. Accepting the cost estimates of Meyer, Peck, Stenason and Zwick in The Economics of Competition in the Transportation Industries, she argues that the survival of discriminatory rate structures has diverted a substantial amount of traffic moving over 200 miles to trucks which would move at lower cost by rail in a competitive organization of the industry. She speculates that this logic may also imply that some freight which could move more cheaply by barge now moves by rail. She estimates the loss from such misallocations -- explicitly casually -- at \$500 million a year to the economy as a whole.

Her conclusions concerning the nature of the misallocation seems to be inconsistent with observed experience. That is, in the "umbrella ratemaking" cases before 1958 and under Section 15a(3) of 1958, in which the railroads secured somewhat more freedom in efforts to reattract traffic through rate-cutting, they mainly endeavored to reattract cargo from barges, not trucks. Professor Friedlaender has no explicit treatment of relative damage experience of carriers: railroads have considerably

higher damage rates than trucks. This reduces the ability to re-attract freight from trucks. With more extensive use of containerization and development of slack-free rail vehicles, such as the Santa Fe is currently endeavoring to develop, such reattraction may well be possible. On the other hand, a study done for DOT indicates that even taking account of damages, virtually all traffic hauled more than 200 miles should go by rail. This indirectly confirms Mrs. Friedlaender's estimate.

The 29 discussants at a conference at Brookings on the manuscript before its publication showed virtual unanimity -- apart from certain industry representatives -- that the \$500 million estimate was too low, the total welfare loss from the existence of regulation was surely much higher than this. The idleness of resources, direct losses on perpetuation of uneconomic services, impediments of disinvestment, expenditure of resources on satisfying routine requirements, inhibitions on experimentation and similar costs must run the total far higher.

Relation of Railroads to Regulation

Reduced regulation of the railroads could improve their financial situation considerably. Railroad regulation is characterized by the establishment of an accustomed pattern of procedures and effects, and this accustomed pattern has a well defined economic impact. The pattern will first be identified and characterized, and the economic impacts will be assessed.

The Accustomed Pattern

Railroad regulation is comprehensive in covering the areas of rates (maximum, minimum, and precise), entry and exit, merger, finance, and administration and reporting. Over the years since 1887 the emphasis has shifted from concern with maximum rates, discrimination, and rates of return to concern with the welfare of the industry and its competitors, and sometimes to procedure (both within the industry cartel itself and before the ICC) for its own sake.

Railroad regulation is characterized by two features; a rigid pattern and contradictory effects.

Procedures have become institutionalized and applied with less flexibility than competing modes of transportation. In the rate area, for example, the possibility of protest from shippers and rival carriers

is so great, and the potential of administrative cost in dealing with these protests is so frustrating, that major economic adjustments in rates have been made under special procedures, themselves time consuming and rigid. Railroads will not raise rates selectively on individual commodities, no matter how low and unremunerative they may be or how great their need for revenue. The procedural difficulties under ICC regulation are too great. The railroads have sought instead to raise rates across the board and to meet special competitive situations by holding down selected rates. As a result of many such rate increases with many thousands of adjustments in holding rates down, the tariffs have become essentially unintelligible. This has tended to favor established shippers who take pains to look after their special rates. Many holddowns are imposed by the Commission and may be politically popular rates; agricultural products for example. On the other hand, new shippers may be discouraged by the formidable machinery of rate adjustments and may think automatically of other modes of transportation.

The Commission imposes no such procedures on other carriers. Trucking rates are seldom investigated, and trucking rates have been increased from year to year with only nominal attention to regulatory standards. Usually an indication that the average operating ratio of

a particular segment of the industry is deteriorating is sufficient to allow the rates to be increased with little procedural difficulty.

Procedural rigidity extends from rates to rail line abandonments, to merger, to common ownership, and many rulemaking activities associated with rail management and administration, such as financial reporting, cost standards, statistics, tariff filing, and the like. Rigid standards are applied to railroads, loose ones to nonrail carriers. Truck lines, for instance, file very summary financial statements, and practically no statistical information.

Procedures also have contradictory effects. Some rates will be kept at a high level to protect competition or merely to "protect revenues." Others will be kept low to favor certain traffics. Service obligations will be imposed for light branch lines, poorly paying traffic such as small shipments and passenger trains. Aggressive marketing for new traffic will be discouraged by the setting of rates too high to beat the competition. Piggyback, for example, was held back for about 20 years on account of unfavorable rate decisions and is still bound by fairly rigid regulations dealing with the various "plans" relating to the status of the various carriers and shippers involved. In another area, rail mergers have been scrutinized with exaggerated intensity, while year in and year out, trucking mergers are approved by the hundreds as a matter of almost routine.

These accustomed patterns have set the pace and rhythm of railroad management outlook. They have provided an incentive for complying with and anticipating procedural standards rather than improvement of the business. The Penn Central merger, for example, undoubtedly minimized the economies which management expected to derive from the merger, so that protest would be minimized and the merger could be "gotten through" the Commission. Rate cases, as noted above, also are tailored to regulatory expectations; the railroad manager will justify his proposal as one most likely to be approved by the ICC not the one most likely to increase his market or improve his service capacity.

Economic Effects of Regulation

Transportation regulation has been founded on the idea of average cost pricing with the concomitant principle of aggregate financial analysis emphasizing the total costs and revenues and the total return. Railroads have traditionally been subject to this kind of economics, stemming first from their early days when such average cost pricing was used by the industry under the protection of its high threshold costs. Regulation was superimposed on this existing practice so that an umbrella was provided for many things, including favorite public services, managerial carelessness, and the pressure of big shippers.

Both unreasonably low and unreasonably high rates flourish under this regime usually labeled as "value of service" pricing. Losses on low rates become a cost which is a part of the average cost base for assignment to high rates. The traditional assignment of the passenger losses to the freight rate base is in point, although the practice has been much wider. In any event, a group of low paying clients developed with vested interests, all of them requiring investment in facilities beyond that of a normal market demand. These were subsidized by a group of high paying clients whose reaction was to seek transportation elsewhere. Again competitive forms of transportation achieved a vested interest in high rail rates and have struggled through the political system to maintain their advantage.

The effect of value of service pricing, having its foundation in average cost pricing and aggregative accounting, leads to management efforts to spread out the gains and losses over more extensive aggregates. Merger, for example, is justified in part as a means of minimizing the costs of special public service obligations and spreading the costs over larger aggregate revenues. Letting a weak road be taken over by a strong one would permit the strong one to charge more when it has a strong market position to cover the losses of the weak line. This principle was even sanctified in regulatory law in the 1920s when rich and poor roads were by official policy to be combined to provide systems of even earning capacity.

Real efficiency gains have never been a major objective of rail merger, and for this reason merger applicants have not gone to any great pains to outline new operating philosophies to attain efficiencies of operation deriving from more intensive use of facilities or the advantages of scale. By the same token, merger applicants have not sought greatly improved service policies or extended markets through genuine promotion of new services made possible by merger.

Because of management's search for a spreading of the load over a greater aggregate revenue, merger studies have been superficial, and the greatest procedural energy has gone into meeting the expectations of various groups with specific interests in the railroad; labor, localities, shippers, and government agencies.

The most basic economic effect of the average cost-aggregate accounting syndrome has been a dampening of the entrepreneurial incentive in the rail industry. It is not an industry where risks are taken and markets developed, or where savings are attained as the economic base of a service concept. It is an industry financed with borrowed capital based on a claim on aggregative assets. These claims or "fixed charges" are another cost to be averaged out. Some rail managers list fixed charges as their most important responsibility. Since there is no real risk capital in the business, there is no entrepreneurial incentive to promote growth or to provide management

rewards for performance achievement. Accounting systems and financial practices are geared to the borrowed fund concept, and stewardship rather than performance responsibility is the order of the day.

In this sense, railroads are behind the other major regulated industries in the utility area, where there is an effort to identify market and service opportunities and to price for these in relation to marginal costs. No doubt these factors reflect another syndrome of accustomed regulatory patterns rather than regulatory enlightenment. The high technology utility and communications industries, doubtless, had to promote their service and utilize their plants so that their practices became enshrined in an accustomed pattern. In fact, the utility accustomed patterns may have encouraged capital intensity due to the need to have a large rate base to maximize revenues and return.

In the railroad industry, there has not been the same incentive to improve the capital structure of the business. It is one of the least progressive in terms of technological innovation. The stewardship of existing assets owned by banks has not provided any incentive for increased earning power from innovation.

Estimates of Freight Diversion Due to Deregulation

On the basis of the Meyer study, the Friedlaender works, and a DOT sponsored study by the Charles River Associates (CRA), estimates have been made on the amount of freight that could be diverted to railroads from trucks. To estimate the effect of deregulation, cost data from each mode was compared, given the assumption that in each case, freight will move via the low-cost mode in a deregulated situation. Implicit in this estimation procedure is the assumption that relative costs of the two modes would be unaffected by deregulation. As indicated above, deregulation can be expected to reduce costs of trucking by eliminating most empty back hauling, excess capacity, etc. Deregulation of railroads would also permit abandonment of uneconomic services, a new emphasis on cost reduction, promotion, and competition. These estimates then are based on the assumption that relative levels of marginal costs remain unaffected by deregulation. Since the impact of regulation for both trucks and rails appears to have been mainly to inflate overhead costs and to affect only slightly marginal costs for a particular traffic, the assumption seems warranted.

All three studies give relatively comparable estimates of the line haul and terminal costs of shipping by rail and by truck. Figures from Meyer's book are given in attached Tables I and II.

Since truck service is preferred to that provided by rail, these studies attempt to quantify this service differential. The low-cost

mode is thus determined by adding the service differential to the basic handling and line-haul costs of rail transport, and comparing the total to the costs of providing truck transport.

The Charles River Associates' study, following Meyer, attempts to quantify three specific service differentials. The first differential results from the greater size of shipment necessary for carload lots in rail rather than truck transit. The second results from the greater time required by rail transit. The third differential aggregates all other service qualities, especially differences in incidence of damage claims.

Estimating the importance of this third differential in service is particularly difficult and was not attempted by Meyer or Friedlaender. While the CRA estimates are extremely crude, they are used here.

Using these costs estimates, the CRA study predicts that 26.3 percent of traffic presently hauled by truck would go by rail given marginal cost pricing, even considering all three service differentials. In other words, virtually all traffic hauled more than 200 miles should go by rail. If the damage and reliability differential could be eliminated, rails could claim 66 percent of the traffic now being hauled by truck. Friedlaender's figures, which do not include an adjustment factor for damage and reliability, imply that 64 percent of the traffic now hauled by truck would go by rail.

Thus, the 64 percent figure is comparable to the 66 percent figure from the DOT study. The two studies' conclusions are very close to each other, which is to be expected, since they differ only in a minor fashion due to slightly different cost data.

The effect of a diversion of about 26 percent from truck to rail would be to increase rail ton miles about 15 percent. This would increase revenue even more since most of the traffic attracted would be high value. If it moved at the average cost to rails of 1.16 cents per ton mile for 400 miles, it would add about \$1.3 billion to rail revenues for a 24 percent increase in revenues.

Water Transport

Examination of possible diversion between water transport and rails was not made, since cost data are limited. Moreover, total revenue of regulated water carriers is only about 3 percent of the revenue of railroads. Even though regulated barge lines carry only part of the total waterborne traffic, the potential dollar diversion to roads cannot be large. However, barge lines fear that railroads could attract significant traffic and while the dollar amount may be small by railroad standards they may be large for water carriers.

Monopoly, Discrimination, and the Railroads

If railroads were completely deregulated, the pattern of rates would change considerably. Even if all rates were forced by competition to be set equal to marginal cost, some rates would rise and many would fall. This means that existing shipping patterns would change and some shippers, some cities, some ports, and some areas would gain while others would be made worse off.

Competition, however, is not equally strong for all products and all areas. For long haul, bulk commodities such as grain, coal, and lumber, railroads have a distinct advantage. This advantage is, of course, limited. At high enough rates, these products can move by truck or possibly by pipeline. Inter-area competition exists; oranges from California compete with those from Florida. Yet the railroads have considerable leeway for a large number of products when they are being shipped a long way.

Absent regulation, the railroads would attempt to maintain high rates to shippers with few good alternatives while reducing rates in the more competitive areas. This means that some railroads in some situations might charge more for a short haul which does not face competition than for a long haul. This practice, however, will be restrained by the fact that trucks are more competitive on short hauls.

Railroads may also discriminate among shippers if they differ on their need for rail transportation. Since most shippers of the same commodity at the same place will have the same competitive options open, discrimination among such shippers should be rare. But since large orders are often more profitable than small, large shippers may get lower rates, at least sometimes, than their smaller competitors. However, it is probably true that most large shippers who would under deregulation benefit by the lower rates, now receive special deals that give them an edge on smaller firms.

It is impossible to predict whether discrimination will increase or not under deregulation. Undoubtedly it will change. Much discrimination among products will disappear; small shippers who cannot afford private trucking would be able to secure trucking service comparable to bigger firms. On the other hand, discrimination among ports and cities may increase (since it already exists, it may not increase but just change).

The issue of discrimination is primarily one of equity. Competition in non-transportation sectors will be virtually unaffected. Some economic waste results from any economic discrimination but it is quite clear that the cost of this waste in today's highly competitive transportation world is several orders of magnitude less than the loss from the existing regulation.

Nevertheless, there is an equity problem. Moreover, fears of discrimination lie behind much of the opposition to deregulation and may have to be placated in order to secure legislation. Even if control over maximum rates is retained, fears of discrimination and predatory pricing will be widespread. Therefore, it may be desirable to consider an antidiscrimination statute coupled with any railroad deregulation program.

The scope of such an antidiscrimination statute should be considered further. Almost any such statute will reduce competition somewhat but this may be a necessary price to pay. Utopia is never achievable. Nevertheless, care should be taken to prevent the anti-competitive effects of the Robinson-Patman Act.

II.

Experience with Deregulation

The trucking industry has all the attributes of a highly competitive industry. There are no substantial economies of scale or barriers to entry. The number of firms in the market is potentially large. Absent government restrictions on entry, the industry would approximate the competitive ideal.

Consequently, we can confidently expect the industry to operate like a highly competitive one. This means that service will be good and prices equal to marginal cost in the short run and over a period of time equal to average cost including a normal profit. Thus while prices will fluctuate somewhat depending on the season and on market conditions, there is no reason to expect wildly fluctuating rates or price discrimination. In a competitive market, price discrimination is impossible since competition will insure that all are provided with low cost service.

Actual experience with deregulation and with unregulated trucking confirm the theoretical expectations.

Useful reports are available on two major examples of unregulated trucking: trucking of agricultural commodities in the United States, and all intercity trucking in Australia. (A portion of the trucking industry in Great Britain has been deregulated, but we have as yet no written report on the results of the change.)

Reported case studies of shifts from regulated to unregulated regimes include shifts involving some agricultural commodities in the United States, and deregulation of trucking in Australia in the 1950s. Again, the recent shift in Britain has not yet been reported on.

Studies of trucking unregulated for a substantial period of time (10 years or more) indicate the following. There is generally a good availability of trucking. The industry attracts sufficient capital to meet demands: it grows with the growth of the general economy. Rates are generally stable. They reflect supply and demand factors, as do prices in other competitive industries, but they do not show excessive fluctuation. The average size of firm is smaller than in regulated trucking, but the field is populated by a number of stable companies. All available indications are that the service is satisfactory to shippers. Indeed, judging from repeated farm sector resistance to attempts to regulate domestic agricultural commodity trucking, unregulated trucking appears, on the whole, to be greatly preferred over regulated trucking by those who have it available to them.

Shifts from regulated to unregulated transportation provide a means of directly comparing regulation with open competition in the same transportation market. In the United States, fresh-dressed and frozen poultry, and fresh fruits and vegetables, were declared exempt

from regulation by the Supreme Court in the 1950s, after about two decades of regulation. The Congress reimposed regulation upon frozen fruits and vegetables. The Department of Agriculture made reasonably thorough studies of the effects of deregulation as to these commodities and the effects of reregulating frozen fruits and vegetables.

The most striking effect of deregulating rates and entry was to bring the rate level down, and keep it down. Rates for poultry fell, on the average, about 33 percent. Rates for fresh fruits and vegetables fell, on the average, about 19 percent. The rates stayed at the lower level.

While rates were lower, the quality of service apparently did not deteriorate. Agriculture's shipper survey covered a number of different aspects of service. As might be expected, shippers had comments and complaints in numerous service categories under both the regulated and unregulated regimes. But the overall pattern of responses indicated no greater total volume of complaints under the deregulated regime than under the regulated regime. The responses did show some differences in the nature of the service offered in the two regimes. The pattern of responses indicated a somewhat greater availability of trucking in the unregulated regime, particularly with respect to out-of-the-way points and distant markets. Also, shippers frequently reported faster service.

On the other hand, the pattern of responses reflected a somewhat greater need to pay attention to the financial responsibility of carriers, and to devote more time and attention to negotiating rates and otherwise supervising carrier performance.

Shippers characterized service as reliable somewhat more frequently with respect to regulated than unregulated carriers. On the other hand, they reported difficulty in getting trucks, less truckload service, service to distant points, and multiple stopoff service more often under regulation than in a free trucking market.

The Australian experience with deregulation was roughly as follows. Trucking in Australia had been held back by state restrictions and high federal taxes. Taxes were lowered, the state restrictions lifted, and a highway construction program instituted, in one fell swoop. The following transition period has been described as briefly turbulent. However, according to available reports, the market settled down to very satisfactory operation. Rates have been stable. The trucking industry has shown a good deal of adaptability and flexibility. A group of stable, substantial-sized firms have emerged, doing a general common carrier business. There is regular and reliable transport for small shipments. There is a good deal of entrepreneurship by individual owner-operators. Larger firms get a substantial portion of their capacity from owner-operators. The owner-operators, and the smaller firms,

move freely between different portions of the country as seasonal requirements for transport change.

One of the most notable effects reported is a major improvement in rail services consequent to increased truck competition. Before trucking became a substantial factor in Australia, the railroads there had followed the course of rail carriers in this country. They had built up an elaborate and discriminatory rate structure, with high rates on high valued goods, lower rates on low valued goods, and a major subsidy of agriculture. They were not noted for spectacular efficiency. Reportedly, as trucking became freer, increased in quantity, and offered competitive rates, the rail system responded with major improvements in the quality of its services, and substantial changes in its rate structure.

The shift to less regulation in England is more recent. The shift was less than total. Short-haul shipments and shipments of smaller size were deregulated. However, large volume shipments and long distance shipments were not. This is apparently an attempt to protect the nationalized railroad industry to a degree, while permitting a free market in trucking in those areas where it is clearly and inarguably superior to rail transport. We have no thorough report on the effects of this scheme at this time.

III.

Major Options

The following options are available to improve the ability of the rails to compete for traffic and to reduce regulation over trucking. Each of these options stands by itself. However, more than one might be chosen. In particular, any option under Section C -- deregulation of trucking -- can be chosen with any of the options dealing with railroads.

Under each section the options are arranged in order of less and less regulation. As a general rule the less regulation, the more competitive pressure on rates, the more efficient the system will be, the greater the change, and the more opposition from major truckers. A more competitive and efficient transportation system would also have significant environmental benefits in that factories will tend to get located closer to raw material sources, scrap rates will move towards virgin material rates, and since substantial freight will be diverted from trucks, congestion and air pollution should be reduced.

The advantages and disadvantages are set forth in terms of additional advantages and disadvantages over the previous option which for option 1 means over the status quo. In other words, the advantages of any option are those listed plus all those listed under earlier options.

A. Railroad Options

1. Department of Transportation Proposal. Department of Transportation has proposed a bill to permit railroads to reduce rates in competitive situations to "avoidable" costs.

Advantages

- This proposal would improve the ability of the railroads to attract business from trucks and barge lines.
- It is a simple modification of current regulatory practices.
- It would receive the wide support of the railroad interests in the country and probably the support of most shippers.

Disadvantages

- It would be opposed by motor carriers and barge lines.
- Presumably these rate reductions would be done in the context of rate-bureaus and the Interstate Commerce Commission efforts to cartelize the industry. Competition would not have full sway and rates would not be as low as they would be in a non-regulated setting.
- This proposal does not free the railroads to change rates quickly where they need to do so.
- It does not achieve a fundamental reform of transportation regulation.
- It does nothing for truck lines or barge companies (though it could be coupled with other options).

2. Remove all control over minimum rates. This means the railroads could cut the rates as far as they saw fit. The rate-making process would have to be made subject to the antitrust laws (repeal of the Reed-Bulwinkle Act is required). This raises two questions:

(1) Would the antitrust laws provide sufficient protection to other modes from predatory pricing? (2) Can all controls over minimum prices be removed and still effectively keep control over maximum rates and over abandonment? Since entry would be relatively easy among other modes of transportation without regulation, it seems unlikely that predatory pricing would be tried or could be effective. This it would appear that market conditions plus the antitrust laws make the answer to the first question affirmative.

The answer to the second question would seem to be no. If regulators are required by law or by equity to let railroads increase rates if their rate of return falls below a certain level (becomes negative perhaps?), then they have to consider all rates or abandon control. A rate below cost in one area would reduce earnings and perhaps justify a higher rate elsewhere. Minimum rate control may also be necessary to insure that a railroad earns enough to support an uneconomic service, if controls over abandonment of such service are to be effective. This would be especially true where a railroad is required to provide uneconomic services in competition with roads not subject to this constraint.

Advantages

- Would provide the maximum competitive pressure on rates.
- Would eliminate the regulatory activity designed to protect competing modes.
- Would put the emphasis on protecting shippers from monopoly.

Disadvantages

- Probably is inconsistent with maintenance of maximum rate control.
- Is also inconsistent with maintenance of controls over abandonment.
- Would be strongly opposed by motor carriers and water carriers.
- Water carriers would fear predatory pricing.
- The railroads would probably oppose; they would in any case prefer option (1).
- Many shippers fearing they would be disadvantaged competitively would oppose.

3. Repeal all regulation over maximum rates except where required to curb monopoly power and all control over minimum rates.

This approach could be modeled after Section 336 of the Canadian Railways Act which permits a shipper to apply to the Canadian Transport Commission to apply for the regulatory prescription of either the

range of possible reasonable rates or the exact rate for rail transportation where "there is no alternative, effective, and competitive service by a common carrier other than a rail carrier." The shipper granted such a rate is required to use it. In all other respects, maximum rates would be free from regulation and subject to the antitrust laws.

Advantages

- Would limit the monopoly power of railroads where it exists.
- Would reduce shippers fears compared to total deregulation.
- Some rates that are below cost would rise.

Disadvantages

- Would raise judgmental problems on the availability of other methods of transportation.
- Shippers that now get rates below cost would oppose.

4. Remove all rail regulation. This would mean repeal of all of the Interstate Commerce Act dealing with railroads. This would leave the railroads in a position to compete like any other company in the non-regulated sector. Presumably roads would be subject to the antitrust laws.

Advantages

- This would remove the "dead hand" of regulation.
- It would encourage rate experimentation.

- It would encourage innovation.
- It would generate all the advantages of a private, unregulated market.
- We would probably secure the somewhat weak support of some railroads. (The railroads would prefer this option to option 2 or 3.) Most of the lines would oppose elimination of the antitrust exemption and so oppose complete deregulation.

Disadvantages

- It is likely to lead to somewhat higher rates for commodities in which the railroads have a definite advantage and little competition. Such higher rates would affect primarily western agricultural and mining interests which are notably politically strong.
- It would generate the opposition of many small shippers who would fear, probably with little foundation, that big shippers would get special deals not available to them. (It is probably true that big shippers would get special deals but they do so now; small shippers therefore would probably be made no worse off, and possibly better off than under the current situation.)

- Motor carriers and barge lines would vigorously oppose this change but probably not any more so than they would the DOT proposal above.

B. Deregulate Barge Lines

Most barge traffic is not subject to regulation. In fact, no more than 20 percent consists of regulated non-bulk commodities. If railroads are permitted more freedom to compete with barge lines, it seems only fair to remove regulation of barges. The purpose of barge regulation is, in fact, to restrict their competition with railroads. There is no possibility of a monopoly in barge transportation and hence no economic reason for this regulation.

Advantage

- The advantage of this would be to permit a more efficient barge transportation system and more efficient competition with rails.

Disadvantage

- The proposal to remove barges from regulation would probably be opposed by railroads unless part of a package and by some barge line interests.

C. Deregulation of Trucking

General Considerations. The rate and entry control scheme is elaborate. The intercity trucking industry has a large number of firms -- over 1,200 with revenues of over \$200,000, and over 11,000 smaller firms. It operates under approximately 90,000 ICC certificates. All certificates are limited in one or more respects -- as to routes, points to be served within a given area, type of service offered, equipment which may be used, etc. Over 75 percent of the Commission's cases involve motor carrier operating rights.

Also, carriers file tariffs with the ICC. These are subject to the elaborate body of rate authority and precedent built up over 83 years of ICC history, and 35 years of motor carrier regulation.

A number of considerations must be integrated in any program of deregulation. They include: (1) the rate at which both shippers and carriers can adjust to changes; (2) the assurances shippers will need in order to be agreeable to the program; (3) the administrative requirements of various methods of decontrol; (4) fair provision for the investment in operating rights incurred under the current licensing regime; and (5) maintenance of safety protections.

The end result sought for the trucking industry could be a total disassembly of existing rate and entry controls, or a partial modification or liberalization of them. There would seem to be no reason

to withdraw safety controls. If entry and rate controls were dropped, specific financial responsibility requirements might or might not be imposed.

Motor Carrier Options

1. Remove commodity restrictions in motor carrier certificates except as necessary for safety.

Advantages

- Would reduce economic waste by permitting carriers greater flexibility in their cargoes.
- Would generate the support of truckers with restricted certificates.
- Would generate shipper support.

Disadvantages

- Would continue cartel pricing.
 - Geographic restrictions and hence inefficiency would remain.
 - Large motor carriers with general certificates would oppose.
2. Remove control over rates.

Advantages

- Would mean greater flexibility in rates and probably lower rates.
- Coupled with option (1) above would go far towards organizing industry on a competitive basis.

Disadvantages

- Would still not achieve a competitive solution.
- Would encourage mergers to eliminate competition.
- Would be opposed by most motor carriers and by the railroads.

3. Total decontrol

The arguments for total decontrol of rates and entry are as follows. First, the industry's economic characteristics are such that the industry should be able to perform best without entry or rate controls. Second, experience has shown that unregulated trucking has in fact performed well.

Advantages

- The result would be a highly competitive industry with low costs and prices related to costs.
- It would eliminate inefficiencies in trucking.
- Would result in the greatest gain for the public.

Disadvantages

- Unless railroads were also decontrolled at least for minimum rates, it would probably divert additional traffic to trucks even though at least some of the additional traffic would move on the higher cost mode.
- Would be opposed vigorously by most motor carriers, by the railroads, and by barge lines.

- Shippers would have to be educated to support this.
- Would result in capital losses for many truckers who have invested in certificates on the basis of their monopoly value.

Mechanics of Decontrol

If total decontrol of trucking is chosen -- from the economic point of view the preferred option -- it would be preferable to move by predetermined steps. Such a policy would permit the industry to adjust gradually and to avoid excessive price fluctuations.

If predetermined objectives were set, at least three considerations counsel phased decontrol. The sheer quantity of restrictions now extant suggest that substantial changes would occur. A deliberate pace could mitigate carrier-raised fears of chaos in an important service area. Both carriers and shippers might find it easier to adjust operations to changed conditions if given a little time to do so.

The decontrol statute could outline steps, and be self-executing, or it could give various degrees of discretion to an administrative body (such as DOT or ICC) in effectuating decontrol. However, if the goal were certain deregulation in a limited time period (say three years), the amount of discretion which could be given an agency is limited. The major steps, at least, and time limits for them, would need to be spelled out in the statute.

Although rate and entry decontrol could be phased simultaneously, there are advantages to deregulating rates first. Deregulation would put some downward pressure on the rates, making new entry less inviting, and thus lessening the likelihood of a rush into the industry when entry bars were lifted. The likelihood of an influx temporarily creating overcapacity could also be lessened by opening up restrictions on carriers within the industry before the barriers to new entry were lifted. This would permit firms in the industry to realign their operations and exploit most of the opportunities opened up by deregulation.

The demonstrated feasibility of unregulated trucking, the size of the industry, the complexity of the control scheme, the substantial resistance to deregulation in trucking, the hostility of the ICC to the deregulation objective, and the limitations on the sustained attention which shippers, the general public, and Congress could give the matter, all counsel a predetermined plan of general scope set out in legislation.

Such a statutory scheme might spell out rate decontrol first, general rule decontrol of licensing next, and free entry into the business last. License restrictions could be lifted by classes -- e.g., commodity restrictions first; geographic restrictions next. The overall process might be scheduled to take place within a period which will not allow too much time for stubborn carrier resistance to bog down

the initiatives after the shipper, consumer, and other interested groups have turned their attention elsewhere -- e. g., three years after the time the first step toward deregulation takes effect.

IV.

Sweeteners

As indicated above, deregulation is likely to engender the opposition of the trucking industry, the barge lines, and at least some railroads. While it is probably not possible to placate motor carriers completely some steps might be taken to reduce the opposition of carriers.

A. Truck Size and Weight

As a trade-off for deregulation, it would be proposed that the trucking industry's desire for increases in the allowable size and weight limits on trucks be supported on the theory that (1) without this support, such legislation cannot pass, and (2) increased sizes and weights are required to enable the truckers to compete with the liberated railroads. Other things being equal, the second point is probably valid. As to the first, the truckers would have to first be persuaded that this is, in fact, true and then decide whether the game is worth the candle. Moreover, there are other trade-offs on this matter, i. e., increased safety requirements and highway user taxes.

B. Rail Abandonments

A more liberal policy with respect to railroad abandonments would have great appeal to the railroads. However, neither this "sweetener" nor others, e. g., grants or loans to the railroads, etc., that might be proposed would be needed for most deregulation proposals (since the railroads gain the most) except those which attack the fundamental basis of rail rate-making such as the repeal of Reed-Bulwinkle, the section that legalizes rate conferences. At this point, it would be somewhat premature to list possible nonregulatory programs for aiding the railroads since these are still under study by DOT. These could be easily factored into whatever regulatory program might be developed. Since most of these programs could be justified on their own merits, the combining of these "sweeteners" with a program of regulatory reform should be carefully evaluated.

C. Easing the Burden of Transition on Truckers

There seems little reason to feel tender about requiring trucking companies to face fully competitive markets, provided the changes were made in stages, upon a reasonable timetable. But there may be some reason to make allowances for investments made in operating rights. Frequently, companies have bought operating rights from other carriers because the ICC entry controls prevented de novo entry into

markets. In many cases, companies' higher than average rates of return have already compensated them for operating rights charges. To the extent this has not happened, a free market, with new entrants unencumbered by operating rights costs, could wipe out unamortized investments of this sort. If an allowance were thought needed, the companies could be allowed to write unamortized franchise payments off against taxes in three or four years. On the other hand, this would cause a loss to the Treasury. It might also be attacked by some groups making the public foot the carriers' bill for adjustments to a regime which should have been in effect all along.

D. Free Entry by Railways into Trucking

Railroads have long wanted the right to enter trucking on their own. Authorizing them to do so would not only help gain their support for a deregulation package but might improve transportation efficiency. The combination of rail/truck may lead to significant economies. There is no need to fear that railroads could eliminate trucking competition given the ease of entry. Consequently this proposal has merit in itself while it also helps gain railroad support.

TABLE I

LONG-RUN MARGINAL COSTS OF FULL CARLOAD RAIL FREIGHT
 BY DISTANCE SHIPPED -- 20 TON SHIPMENT BY BOXCAR
 (Cents Per Ton Mile)

<u>Distance (Miles)</u>	<u>Rail Terminal Cost</u>	<u>Rail Line-Haul Cost</u>	<u>Pickup and Delivery</u>	<u>Total Rail Cost</u>	<u>Service Differen- tial -- Time in Transit¹</u>	<u>Service Differen- tial -- Size of Shipment²</u>	<u>Service Differen- Other Service Factors³</u>	<u>Total of Rail Cost Plus Service Differen- tials</u>
50	3.16	0.33	3.40	6.89	1.31	0.13	4.49	12.82
100	1.58	0.33	1.70	3.61	0.73	0.06	2.25	6.65
200	0.79	0.33	0.85	1.97	0.42	0.03	1.12	3.51
400	0.40	0.33	0.43	1.16	0.27	0.02	0.56	2.01
600	0.26	0.33	0.28	0.87	0.23	0.01	0.37	1.48
800	0.19	0.33	0.21	0.73	0.19	0.01	0.28	1.21

TABLE II

TRUCK, RAIL COST COMPARISONS
(Cents Per Ton Mile)

(1) Distance Shipped (Miles)	(2) Rail Marginal Costs Plus All Service Dif- ferentials	(3) Rail Marginal Cost Plus Ser- vice Differ- entials Due to Size of Ship- ment and Time In Transit	(4) Rail Marginal Cost Plus Ser- vice Differ- ential Due to Size of Ship- ment	(5) Total Mar- ginal Costs of Trucking (Truckload Shipments)
50	12.82	8.33	7.02	8.80
100	6.65	4.40	3.67	6.00
200	3.51	2.39	2.00	4.80
400	2.01	1.45	1.18	3.85
600	1.48	1.11	0.88	3.27
800	1.21	0.93	0.74	3.24

Deregulation

May 1, 1970

DEREGULATION: Critical Elements of an Administration Effort

1. Creation of an administration consensus on regulatory policy.

The agreement should cover the need for deregulation, the areas to be deregulated, and the extent to which deregulation should proceed. Regulatory commission chairmen, as well as major agency heads, have vital contributions to the formulation of regulatory policy initiatives.

2. Production of substantive administration proposals.

Both legislative and administrative actions should be considered in developing administration initiatives.

3. An educational program directed toward Congress, the press, and the public.

Past attempts to deregulate have not clearly aired the inadequacies of present regulatory policy. The efficacies of administration proposals should be widely publicized and fears of uncompensated loss of equities should be laid to rest.

Deregulation: Procedural Options

I. Presidential Commission

- Adv. 1) provides substantive proposals
 2) contributes to educational program
 3) can be adopted later if other options fail
- Disadv. 1) recommendations administratively uncontrollable
 2) precludes action for at least 1 year
 3) Congress (Baker) is proposing a Commission on Transportation
 Regulatory Agencies

II. Subcommittee of Cabinet Committee on Economic Policy

- Adv. 1) can be constituted so as to address policy question, or to
 produce administration initiatives, or both
 2) if properly publicized, could provide significant education
 3) could provide administration consensus on some other option
 (including DOT paper and Ash report)
 4) would provide for continuing awareness of the issue within
 the administration
 5) would provide opportunity to extend deregulation to other
 areas
- Disadv. 1) would require careful co-ordination to ensure that subcommittee
 work is consistent with the broader transportation policy
 formulation now underway in DOT.

III. DOT Initiative (Policy Paper)

- Adv. 1) contributes to educational activity
 2) produces some concrete proposals
 3) could be used in conjunction with option II

- Disadv. 1) action would be delayed until fall at the earliest
- 2) limits deregulation effort to transportation unless used as kick-off for larger effort
- 3) both Congress and the regulatoryies are wary of DOT intrusion
- 4) since deregulation is part of economic as well as transportation policy, other members of the administration have contributions to policy formation

IV. Inter-agency Task Force

- Adv. 1) would produce substantive proposals
- 2) has been used successfully in the past to solve problems concerning more than one agency
- 3) could produce proposals fairly quickly

- Disadv. 1) a staff-level operation would not necessarily secure policy-level consensus
- 2) a task force is likely to foreclose options which may appear politically infeasible to staff level

DRAFT 5/1/70

CTWhitehead

Deregulation

Deregulation Strategy Objectives

1. Creation of an administration agreement on deregulation strategy, the areas to be deregulated, and the extent of deregulation. Parties to the agreement should include major agency heads and, to the extent feasible, the regulatory commissions.
2. Development of substantive administration initiatives to deregulate, including both legislative and administrative actions.
3. An educational program to reach Congress, the transportation industry, the press and the public on both policy and proposals.

Deregulation Tactical Options

I. Presidential or Congressional Blue-Ribbon Commission

- Adv. 1) makes public substantive proposals that the Administration is not necessarily committed to
- 2) contributes to educational program
- 3) Congress is proposing a Commission on Transportation Regulatory Agencies

- Disadv. 1) recommendations administratively hard to control
- 2) precludes major action for at least one year
- 3) will ultimately have to go to options II or IV anyway.

II. Subcommittee of Cabinet Committee on Economic Policy

- Adv. 1) can be constituted so as to address legislative proposals, administrative initiatives, or both
- 2) if properly publicized, could provide some education
- 3) could provide vehicle for administration planning on other options (including DOT paper and Ash report) and is the most effective way to effect cooperative participation of the regulatories
- 4) would provide for continuing awareness of the issue within the Administration
- 5) would provide framework to extend deregulation to other areas

- Disadv. 1) would require careful coordination to ensure that subcommittee work is consistent with the broader transportation policy formulation now underway in DOT.
- 2) there is a serious possibility that most, if not all, regulatory agency heads are pro-regulation.

III. Wait for DOT Policy Paper

Adv. 1) assures that any regulatory initiatives would be consistent with the broader transportation policy.

2) could be used in conjunction with options I, II or IV.

Disad. 1) action would be delayed until 1971 or later

2) some Administration machinery will be needed in any event to plan deregulation strategy in more detail.

3) both Congress and the regulatories are wary of DOT intrusion

4) since deregulation is part of economic as well as transportation policy, other members of the Administration should contribute to policy formation.

IV. Inter-agency Task Force

Adv. 1) gets staff work and some inter-agency agreement done before principals are involved.

Disadv. 1) a staff-level operation would not secure policy-level agreement.

2) a task force is likely to foreclose options which may appear politically infeasible to staff level.

~~W/K~~
T.W.
Regulation

CABINET COMMITTEE ON ECONOMIC POLICY

AGENDA FOR
SUBCOMMITTEE ON TRANSPORTATION REGULATION

9:00 a.m. - May 19, 1970
Room 415, Executive Office Building

1. Consideration of the Objectives of the Transportation Regulation Subcommittee (see attached paper).
2. Consideration of the Work Program and timetable.
3. Staffing of the Subcommittee and funding if any outside help is needed.

THE OBJECTIVES OF THE SUBCOMMITTEE ON TRANSPORTATION REGULATION

The objective of the Subcommittee is to consider the degrees of economic regulation of domestic transportation needed and the degree of competition that can be and should be introduced in transportation. Specifically the Subcommittee should consider what regulation if any is necessary in:

- (1) Railroads
- (2) Motor carriers
- (3) Water carriers
- (4) Pipelines
- (5) Airlines
- (6) Air cargo
- (7) Freight forwarding
- (8) Bus lines

In particular it is expected to consider the necessity and desirability of rate fixing by rate bureaus, minimum rate regulation, entry control, route control, maximum rate control, and the need for joint through rates. The Ash Commission's recommendations as well should also be considered.

To this end the Subcommittee should evaluate the competitive potential of each of the modes, examining whatever evidence that might exist on the likely performance of the mode in a free market. The Subcommittee should also consider the possibility of predatory pricing and the extent to which antitrust action could be depended on to prevent such action. It will also be important to evaluate the extent of cross subsidization and the allocative and equity effects of its abolition. In this connection, the Subcommittee should estimate the regional and locational impact of a free market. In those markets where intra-modal competition is insufficient to prevent monopoly competition, the potentiality of intermodal competition has to be examined, as well as the effectiveness of existing regulation. The objective is to produce a report or reports on all forms of domestic transportation similar to the one prepared by the Department of Justice on Motor Carriers. Our report would make recommendations on legislative and executive action in time for inclusion in the President's program for 1971.

WORK PROGRAM

(1) The first step to be taken could be the preparation of a report on the appropriate mix of regulation and competition in domestic transportation. This report would address itself to the issues raised above in the section on Objectives. This report could be drafted by a small staff under the direction of CEA with inputs from other agencies.

(2) A report on the political problems of changing and reducing regulation could be prepared by a small group under the direction of DOT. It should include a strategy for achieving our goals, including ways to educate shippers, carriers, travelers, and the consumer on a free market. Various political approaches should be considered, possibly including programs that might be tied to reduced regulation.

(3) The steps that could be taken administratively and those steps that need legislation would have to be identified. This effort may have to wait until after the main conclusions of the report in paragraph (1) are clear.

(4) The public part of the work needs planning. Should hearings or informal discussions be held? At what stage should the regulatory agencies be included in the deliberations? This

part of the work should be considered by the whole Subcommittee.

STAFFING

The task of this Subcommittee is huge but its importance to an efficient economy cannot be overstated. Most of the preliminary work must be done within the Government, although an adequate job may involve an effort commensurate with that launched for the Cabinet Committee on Oil Imports. Consequently, it may be necessary at this stage to consider bringing in a man to direct this study full time. Such a man could be hired by the CEA if funds were available or made available for the summer and fall.

Deregulation

May 4, 1970

MEMORANDUM FOR

Secretary John A. Volpe
Chairman Paul McCracken
Director Robert Mayo
Mr. Henry Cashen
Mr. Clay T. Whitehead


The purpose of our meeting on May 5 is to bring together those in the Administration who are concerned with transportation regulatory policy to discuss how the Administration can best proceed in bringing about less restrictive regulation. This is an important enough topic in itself, of course, but, seen as a part of a broader effort to make Federal regulatory policy more responsive to the public interest, it takes on special importance and goes beyond the transportation field alone.

I have attached a short options paper for discussion on Tuesday. Also attached are:

1. Past attempts at deregulation
2. Bills currently before Congress

Peter Flanigan
Assistant to the President

Attachments

cc: Mr. Whitehead 
Central Files

CTWhitehead:ed

Regulatory Policy Tactical Options

I. Presidential or Congressional Blue-Ribbon Commission

- Adv. 1) makes public substantive proposals that the Administration is not necessarily committed to.
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Disadv. 1) a staff-level operation would not secure policy-level agreement.

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II. Previous Attempts at DeRegulation

Through the years attempts at easing regulation, expanding exemptions, or deregulating substantially have been sporadic and without major success. In rails, for example, the 1920 Act had provided for a master plan of consolidation of existing lines into a practicable network, a major step toward more complete regulatory control. This long-pending requirement was finally allowed to lapse, with the Commission left with power to consider consolidations on an ad hoc basis. But this was largely due, not to the opponents of regulation, but to the failure of ICC to develop the plan.

A minor success was achieved on minimum rate regulation in 1958, when the Commission was required to consider the needs of intermodal competition.

In trucking, farming exemptions were broadened in 1940 to include federations as well as single farm cooperative associations, but this exemption was significantly hedged about in 1968. Again, judicial broadening of the most significant agricultural exemption was curbed in 1958.

The only major attempt at significant deregulation occurred following the President's Transportation Message in 1962. This was legislation to remove minimum rate regulatory authority from ICC, FMC and CAB in bulk commodities, agricultural and fishery products, and passenger transport. In effect, these areas would be returned from rate regulation to the forces of competition. As part of this the Reed-Bulwinkle antitrust exemption for carrier rate-bureau activities would be repealed as to these commodities, except for setting joint rates for through routes, and the applicability of the antitrust laws reinstated. Full-dress hearings were held in House and Senate in 1962, but problems arose and action was postponed. In 1963 a similar Administration bill was introduced and further hearings held. Finally in 1964 the House Committee patched together a bill going far beyond Administration proposals, including complete deregulation of agricultural carriage by all modes and repeal of the commodities clause, which the Administration was forced to oppose. Ultimately, all this legislation was allowed to die.

The railroads had in part sponsored the Administration legislation and originally strongly supported it. They saw this rate deregulation step as a chance at more effective intermodal competition against truck and water carriers in bulk and agricultural products. But they were not equally keen for intra-modal competition, and on this rock the legislation ultimately foundered.

The rails put forward amendments to weaken antitrust coverage. They wished to narrow the number of antitrust provisions which would apply; to retain the existing exemption for all rate-bureau activities other than predatory price cutting; and, even there, to require proof of specific intent to drive out competition. This general position received some support from Commerce, and Defense expressed fears about the legislation stemming from its concern over the effect on its special Government carrier rates under Section 22 of the Act.

Truck and water carriers were highly suspicious throughout that the legislation was a railroad device to permit predatory pricing to drive them out of business. Shippers, in turn, were not active supporters. The economic power of the largest shippers had already enabled them to make advantageous transport arrangements under regulation which were not available to small shippers. Other shippers, vocal about rate problems and deficiencies in service under regulation, were still uneasy that the unknown of deregulation might be worse. Basic concern was with stability in rates and fears that competitors might obtain a transport cost advantage.

As for potential lowering in the general level of rates, shippers seemed complaisant about the status quo, influenced perhaps by belief that the higher transport costs under regulation can be passed on to consumers. Finally, among the affected industries and in Congress, many feared that the alternative of the antitrust laws and antitrust enforcement would not suffice, without major buildup in manpower and money, to swiftly curb the predatory rate practices which it was feared would follow deregulation.

The consumer revolution had not yet been born in 1962, and the consumer's voice was hardly heard on this legislation.

In retrospect, major problems with the 1962 proposal were:

- (1) There was insufficient preparation and education of the public and interested groups on the adverse price and other effects of regulation on them. Shippers, consumer groups and other interested parties were not asked for opinion, and were not thoroughly informed about the rationale or the effects of the proposal before it was put to Congress.

(2) Consumer groups must be informed of the part transport costs play in the price of everything they buy. They must also be advised how regulatory controls contribute to a higher level of prices to them than under an unregulated economy.

(3) There should be better clarification of the shipper's real interest. Almost all shippers seemed to count it desirable to have some clear notion as to the relationship between the transportation costs to them and the transportation costs of their competitors. Small shippers, in particular, are concerned about being put at a disadvantage by transportation rate discounts not justified by cost differentials. Frequently shippers may feel that as long as transport charges are uniform as among competing enterprises, they have relatively little interest in the overall size of the charges.

(4) Quite apart from the rate question, shippers must be made aware of how regulation in general tends to promote rigidities and inefficiencies in transport service and fails to promote adequate technological development in transport.

(5) Communities and industries with major investments were fearful that changes in transport rates would obsolete these investments. Ports in particular were concerned about maintaining administered transport rate relationships so they could have a way of protecting their interests.

(6) The barge lines, and others, were afraid that there would be no effective control of predatory pricing by the railroads. Barge lines feel vulnerable because their commodity list is small compared to the railroads, and their overall economic resources are also small when compared with the railroads. There was doubt that Justice Department activity would fully fill the gap once rate control was withdrawn.

(7) Reliance of carriers on the Reed-Bulwinkle Act provided a further stumbling block to obtaining effective intra-modal competition. The essential incompatibility of exempted rate-bureau activities with deregulated, competitive transport industries was not made entirely clear.

Introduced Bills to Study Transportation Regulation

A summary of S 2355 - An advisory commission to study freight rates

1. Thirteen members appointed by the President, as follows:
 - a. 1 from agricultural industry
 - b. 1 from industry generally
 - c. 4 from transportation industry: one each from parts I, II, and III of ICC Act (railroad, trucks, and domestic water carriers respectively) and one from the air carriers (FA Act)
 - d. 2 from the public generally
 - e. 4 from the Federal Government: one each from DOT, Agriculture, ICC, and CAB
 - f. 1 to serve as chairman
2. Duties of the Commission -- make a full and complete study to determine:
 - a. the factors that contribute to the fixing of freight charges
 - b. the reasons for any differences in such charges because of location or commodity
 - c. whether or not all involved government bodies are properly carrying out the national transportation policy
 - d. whether the national transportation policy is adequate in view of modern conditions.
3. Report due to President and Congress no later than two years.

Senate hearings on this bill were held March 17 - 19, 1970.

DOT, in its testimony, recommended postponement of action on this bill pending DOT's upcoming national transportation policy evaluation report. However, if Congress felt a study should be initiated now, DOT suggested that it do the study, not a Commission.

A summary of S 3760 - A Commission on Transportation Regulatory Agencies
(Introduced 5/27/70)

1. Nine members, as follows:
 - a. 3 appointed by the President
 - b. 3 appointed by the President of the Senate
 - c. 3 appointed by the Speaker of the House

2. The Commission shall study the organization, structure, and purposes of the regulation of transportation by the ICC, FMC, and CAB and shall determine and report upon the feasibility and desirability of a merger of these three agencies.
3. The Commission shall consider the need for:
 - a. developing, coordinating, and preserving a national transportation system
 - b. providing fair and impartial regulation of all modes of transportation
 - c. promoting safe, adequate, economical, and efficient transportation
 - d. fostering sound economic conditions in transportation
 - e. encouraging the establishment and maintenance of reasonable charges for transportation services without unjust discriminations, undue preferences, or unfair competitive practices
4. Report due to President and Congress no later than one year.

Bureau of the Budget
ROUTE SLIP

TO _____

C.T. WhiteheadTake necessary action ☐Approval or signature ☐Comment ☐Prepare reply ☐Discuss with me ☐For your information ☐See remarks below ☐FROM E. HallyDATE May 1, 1970

REMARKS

This version is cleaned up to the extent that objectionable (nonpolitical) adus + discards have been removed. Language is prob. not suitable.

E. Hally

Deregulation
May 1, 1970

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 5) would provide opportunity to extend deregulation to other
 areas
- top 2* { Disadv. 1) would require careful co-ordination to ensure that subcommittee
 work is consistent with the broader transportation policy
 formulation now underway in DOT.

III. DOT Initiative (Policy Paper)

- Adv. 1) contributes to educational activity
 2) produces some concrete proposals
 3) could be used in conjunction with option II

- Disadv. 1) action would be delayed until fall at the earliest
- 2) limits deregulation effort to transportation unless used as kick-off for larger effort
- 3) both Congress and the regulatories are wary of DOT intrusion
- 4) since deregulation is part of economic as well as transportation policy, other members of the administration have contributions to policy formation

IV. Inter-agency Task Force

- Adv. 1) would produce substantive proposals
- 2) has been used successfully in the past to solve problems concerning more than one agency
- 3) could produce proposals fairly quickly
- Disadv. 1) a staff-level operation would not necessarily secure policy-level consensus
- 2) a task force is likely to foreclose options which may appear politically infeasible to staff level

Delegation

May 1, 1970

To: Henry Cashon

From: Tom Whitehead

You may or may not be aware that the Schriever Commission has decided to look into the transportation area as one of the first items on their agenda. If you are not already on top of what they have in mind, it might be useful to find out before our Tuesday meeting with Flanigan, Volpe, et al.

I have attached an options paper for Pete to send out to the attendees of the Tuesday meeting. If you have any comments before Monday noon or so, I can incorporate them.

Attachment

cc: Mr. Whitehead
Central Files

CTWhitehead:ed

Deregulation Strategy Objectives

1. Creation of an administration agreement on deregulation strategy, the areas to be deregulated, and the extent of deregulation. Parties to the agreement should include major agency heads and, to the extent feasible, the regulatory commissions.
2. Development of substantive administration initiatives to deregulate, including both legislative and administrative actions.
3. An educational program to reach Congress, the transportation industry, the press and the public on both policy and proposals.

Deregulation Tactical Options

I. Presidential or Congressional Blue-Ribbon Commission

Adv. 1) makes public substantive proposals that the Administration is not necessarily committed to

2) contributes to educational program

3) Congress is proposing a Commission on Transportation Regulatory Agencies

Disadv. 1) recommendations administratively hard to control

2) precludes major action for at least one year

3) will ultimately have to go to options II or IV anyway.

II. Subcommittee of Cabinet Committee on Economic Policy

Adv. 1) can be constituted so as to address legislative proposals, administrative initiatives, or both

2) if properly publicized, could provide some education

3) could provide vehicle for administration planning on other options (including DOT paper and Ash report) and is the most effective way to effect cooperative participation of the regulatory agencies

4) would provide for continuing awareness of the issue within the Administration

5) would provide framework to extend deregulation to other areas

Disadv. 1) would require careful coordination to ensure that subcommittee work is consistent with the broader transportation policy formulation now underway in DOT.

2) there is a serious possibility that most, if not all, regulatory agency heads are pro-regulation.

III. Wait for DOT Policy Paper

Adv. 1) assures that any regulatory initiatives would be consistent with the broader transportation policy.

2) could be used in conjunction with options I, II or IV.

Disad. 1) action would be delayed until 1971 or later

2) some Administration machinery will be needed in any event to plan deregulation strategy in more detail.

3) both Congress and the regulatories are wary of DOT intrusion

4) since deregulation is part of economic as well as transportation policy, other members of the Administration should contribute to policy formation.

IV. Inter-agency Task Force

Adv. 1) gets staff work and some inter-agency agreement done before principals are involved.

Disadv. 1) a staff-level operation would not secure policy-level agreement.

2) a task force is likely to foreclose options which may appear politically infeasible to staff level.