THE TRANSPORTATION PROBLEM

THE ADJUSTMENT OF RATES BETWEEN COMPETING FORMS OF TRANSPORTATION

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Contrary to ideas rather widely entertained by those who have not studied the history of the Interstate Commerce Commission, the transportation abuses which it was created to abate were the product more of competition than of monopoly, although both were contributing factors. Between them, with competition as the main moving force, they had produced all manner of discriminations in rates which were found on every hand and were thought by many to be unjust. The competition was chiefly between railroads, but even in those days water transportation was an important competitive force and was responsible for the more flagrant instances of charging more for short than for long hauls over the same route which were particularly obnoxious to public opinion.

It is significant that in the second year of its existence the Commission recommended "that the carriers engaged independently in interstate traffic on the rivers, lakes, and other navigable waters of the country be put in respect to the making, publishing, and maintaining rates upon the same footing with interstate carriers by rail." In the same report the Commission dwelt upon the damage done to both the railroads and the public by unreasonably low competitive rates, and five years later, in 1893, after mentioning the many railroad receiverships, it recommended that it be given authority to fix minimum as well as maximum rates. It thus appears that even then the thought had gained ground that regulation directed against unduly low rates, and designed to curb competition in this respect, might well be required in the public interest to protect the carriers against themselves.

The power to prescribe for the railroads minimum in addition to maximum rates was, however, not given to the Commission until 1920, when it was conferred in a statute, the Transportation Act of 1920, whose predominant object was to foster and promote good financial health for the railroads. This endeavor to promote carrier welfare through legislation has since persisted. The five most important transportation statutes of recent years (the Emergency Railroad Transportation Act, 1933, the Intercoastal Shipping Act, 1933, the Motor Carrier Act, 1935, the Merchant Marine Act, 1936, and the Civil Aeronautics Act, 1938) were all acts whose primary purpose was, in one way or another, to improve carrier financial conditions; and the same motive dominates the transportation legislation which Congress now has under consideration. The shipper and

traveler have not been the direct objects of concern in the more recent regulatory acts. The immediate objects of concern have rather been the carriers, with the thought, of course, that their welfare is in the long run essential to the public welfare. Those who are wont to inveigh against public regulation as a force that hampers and hurts the carriers may well give heed to the fact that the carriers themselves have been leading proponents of the more important federal regulatory statutes from 1920 to date.

The reason for this lies in the fear, generated by plenty of practical experience, of the effects of unrestrained competition, a fear which has continually grown more acute as competition in transportation has increased in prevalence and intensity. The outstanding transportation fact of the past two decades, as everybody knows, has been the tremendous growth of such competition. The traffic which is not open to some kind of competition in transportation is now so rare as to be negligible, and one very important fact is that much of this competition, so far as all forms of transportation except the railroads are concerned, can be furnished by the shipper or the traveler with his own facilities.

I sometimes wonder whether it might not be wiser to let nature have her way with this competition and work out results on Darwinian principles. Apart from the carnage and disaster for many which this process would involve, however, such a struggle for existence would not be maintained by intelligent human beings in the absence of compulsion. Left to themselves, sooner or later they would begin to trade and combine. The alternatives to an attempt to abate the abuses of competition by public regulation are, therefore, either to compel competition to be maintained in full force and vigor until only the fittest survive, or to permit the carriers to work out a state of peace in their own way through an admixture of throat cutting, trading, and combination. Neither of these alternatives appeals to me as likely to produce satisfactory results, and therefore I see nothing to do except to continue and improve, if possible, the policy of regulating competition in transportation to which the country is now quite definitely committed.

With respect to this matter, I speak with the limitations of one who has the job to do and cannot properly indulge his own theories without hearing and considering what all interested parties have to say. The Commission now has a number of important cases pending in which the rates of competing forms of transportation are under consideration. They present issues which, in my judgment, are as difficult as any that the Commission has ever had to determine, and there is such a clash of views as to how they should be determined that the controversy is likely to spread to the Supreme Court, to Congress, and to public opinion. I am inclined to believe that sound and satisfactory policies will be developed only

gradually through the decision of successive cases and experience with the practical results, much as the common law was developed. For these reasons I shall not undertake in this paper to give answers to the problems but only to indicate what some of them are.

The competition between different modes of transportation is, of course, affected very materially by the extent to which public aid or subsidy is given, directly or indirectly, to each. Very complicated questions of fact and of public policy are presented by this matter, but they have not been committed to the Commission for determination or consideration, and we must take the situation as it exists in this respect regardless of what it should be. The chief questions by which the Commission is confronted in the adjustment of the rates of competing forms of transportation are whether and how and to what extent it should exercise its authority to prescribe minimum reasonable rates.

What is a minimum reasonable rate? This is a question which the Supreme Court may have to answer. There are widely different views. At one extreme, there are those who say that it is a rate which covers with some margin what is termed the "out-of-pocket expense" of hauling the traffic, by which is meant the expense which is added when the traffic is carried and which is saved when it is not carried. Others say that the measure is what I call the full allocated cost of service, including a fair return on the value of the property used in the service. This covers, not only any expense for which the traffic in question is solely responsible, but also its proportional share of the expense incurred in common for that and other traffic and of the profit essential to the financial welfare of the carrier. At the other extreme, many take the view that no particular formula can be used in determining a minimum reasonable rate. Many things are pertinent and there are flexible limits of judgment, dependent on the circumstances, just as there are in the determination of maximum reasonable rates. Congress, according to this view, must have given the Commission this power for the purpose of preventing destructive competition, of promoting the use of each mode of transportation in the service for which it is economically best fitted and discouraging its use under reverse circumstances, and of stabilizing and improving the financial conditions generally prevailing in the transportation industry. This being so, it is argued, the power should be used in each particular situation in whatever way will best accomplish that purpose.

In the past, cost of service lurked in the background in the fixing of railroad rates, but the railroads used only rule-of-thumb methods in determining such cost and were chiefly interested in it from the standpoint of results in the aggregate. In fixing rates on a particular kind of traffic, they were more interested in what it would bear. More euphemistically, this has come to be known as giving consideration to the value of the service. The

highest rates in relation to the cost of service were, I think, and speaking broadly, the carload rates on commodities capable of fairly heavy loading and of relatively high value. The present widespread competition from other modes of transportation, both public and private, has brought cost of service into the foreground and given it a much greater degree of importance. In adjusting rates between competing forms of transportation, specific knowledge of respective costs of service, so far as it is attainable, seems essential.

I say "seems" in this connection, because there is a school of thought to the effect that when carriers of different types compete, each can contribute something in the way of service that the other cannot supply, so that all ought to be available for public use. Therefore, it is urged, competitive rates ought to be adjusted to a basis which will be profitable to the carriers concerned, of whatever type, and which will permit them all to share in the traffic. In such an adjustment, those who hold this view would give lesser attention to respective costs of service, but in determining the general level of the rates would give heed to the value of the service, and they would also establish what are termed "differentials" in the rates, i.e., fix rates somewhat higher or lower for one type of carrier than for another, wherever necessary to bring about what they regard as a fair distribution of the traffic.

However, the Commission is concentrating attention on the subject of cost finding, and has recruited a small staff of experts for this purpose. It is hardly necessary to say that the subject is full of opportunities for controversy, particularly as to railroad costs, because of the large extent to which costs are incurred in common for the hauling of many different types of traffic. To distribute such items of expense, allocation formulas must be used the accuracy of which is not capable of complete demonstration, and which often appear somewhat arbitrary. So-called "out-of-pocket expense," which also enters into the picture, as I have already indicated, has been found to be a shifting and elusive quantity, dependent on the volume of traffic under consideration.

That the questions which arise out of the desire of carriers to take on competitive traffic, if need be, at rates which yield only a bare margin over what they deem to be the out-of-pocket expense require close and thorough study is, I think, already very evident. From time immemorial the railroads have justified low competitive rates on this theory that the traffic so gained adds comparatively little to the expense which would otherwise be incurred. Trucks and ships find plenty of opportunities for applying the same theory, particularly in securing return loads when traffic preponderates in one direction. No doubt it is a fairly sound theory, if confined to a comparatively small fraction of the traffic carried. The difficulty is that out-of-pocket expense tends to increase disproportionately as this

fraction increases in size, and this tendency becomes a positive danger when competition is so generally pervasive as it is at the present time. It is relevant to call attention to the fact that prevailing railroad passenger fares and less-than-carload freight rates in general, as well as many carload rates which they charge in competition with water carriers, can only be justified by the added-traffic, out-of-pocket expense theory.

It is also evident that in adjusting the rates of competing types of for-hire carriers under modern conditions, consideration must always be given to the ability which the shipper frequently has to provide his own private transportation, by ship, truck, or pipe line, if he finds this to his financial advantage. This is a factor which tends to make cost of service much more nearly a measure of what the traffic will bear than once was true. There is some alleviation from the standpoint of the for-hire carriers, however, in the fact that the shipper seldom has a good load factor; that is to say, the traffic which he can handle himself is apt to be mostly in one direction; and he often shrinks from the investment and the creation of an organization required to carry on what is for him a new line of activity. This is especially true of motor carriage. Ordinarily he prefers, unless the cost disadvantage is quite substantial, to utilize the services of the for-hire carriers.

A further danger that we must be on guard against in fixing minimum rates is the establishment of an artificial and rigid method of rate making which will impair the incentive which free competition gives the carriers to increase the efficiency and economy of their operations. When it is borne in mind that the amount of transportation to be performed is not a fixed and static quantity, but one capable of expansion as facilities with lower costs are made available, it is not difficult to realize the danger to the development of the country if this incentive to improvement is removed or impaired. However, this is as yet no more than a remote prospective danger, for certainly the incentive is now very great and improvements in transportation are being made at an unprecedented pace.

In the period from 1920 to 1935, the Commission's transportation jurisdiction, except for a limited authority over pipe lines, was confined to railroads and allied carriers, and the power to fix minimum rates was used very sparingly. The railroads rarely sought its use. There were important cases, however, where it was used, largely on the Commission's own initiative, to protect the rate structure against threatened rate wars; and in the exercise of its discretion to grant or withhold relief from the prohibition against charging more for a short than for a long haul over the same route, the Commission undertook to prevent certain competitive railroad rates from going below a "reasonably compensatory" level.

Since the passage of the Motor Carrier Act, 1935, however, the power to prescribe minimum rates has been invoked much more frequently. Interest-

ingly enough, the motor carriers have often sought its use to curb what they deemed to be demoralizing and destructive competition in their own ranks, and both railroads and motor carriers have increasingly prayed for its use against each other. In the past year or so the competition between these two forms of carriers has grown in intensity and virulence, and in a considerable number of instances the Commission has felt impelled to arrest the vicious circle of reductions through its suspension powers pending a thorough investigation.

To date the Commission has had no jurisdiction over the port-to-port rates of water carriers and only power to prescribe maximum rates for joint rail-and-water hauls. The legislation which has now reached the conference committee stage in the present Congress, however, proposes to extend the jurisdiction of the Commission, so that it will cover water carriers in much the same way as railroads and motor carriers. Obviously, if this is done, our problems will not be simplified. On the other hand, the opportunities to bring about a better co-ordination in the use of these three modes of transportation, to the advantage of the public as well as of the carriers, ought to be increased.

In so short a paper as this, it is of course impossible to give more than a cursory indication of the problems which are involved in the attempt, by public regulation, to adjust the rates of competing forms of transportation. Enough has been said, however, to suggest that the lot of regulatory bodies, like that of which I am a member, which have this task to do is, like that of the policeman, not a happy one. I often wish that it could be my good fortune to have in hand the regulation of a prosperous monopoly. It must, I feel sure, be an infinitely easier task than the regulation of a multitude of violently competing and more or less impecunious carriers. The latter work requires, if it is to be done at all satisfactorily, an extraordinary amount of patience, care, and wisdom. The stock of those qualities which we possess is strictly limited, and if the economists of the country can help us with their own mental powers and stores of acquired knowledge, we shall be very grateful indeed.