

REGULATORY REFORM AND THE TRUCKING INDUSTRY:
AN EVALUATION OF THE MOTOR CARRIER ACT OF 1980*

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* Views expressed in this paper are those of the author. They do not necessarily represent the position of the Commissioners or staff of the Federal Trade Commission.

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I. INTRODUCTION

The Motor Carrier Rate-making Study Commission ("MCRSC") is required by Congress to investigate collective ratemaking and determine whether antitrust immunity for the collective determination of trucking rates should continue. The special antitrust exemption for collective ratemaking is however only one aspect of the regulatory framework within which the trucking industry operates. Industry structure, conduct and performance are also affected by entry controls, rate regulation and general economic conditions. To properly assess the impact of eliminating antitrust immunity requires that the MCRSC also understand how changes in these other variables affect the trucking industry.

The purpose of this paper is to evaluate the impact of both changes in the Motor Carrier Act of 1980 ("MCA") and the current economic recession, and thereby provide the MCRSC with the broader perspective needed to make findings and recommendations with respect to antitrust immunity for collective ratemaking. 1/ Section II briefly reviews alternative public interest and special interest rationales for motor carrier regulation while Section III explains how the post-MCA period of increased competition can be used to test these alternative explanations. Those features of the MCA that serve to promote competition are discussed in Section IV along with the ICC's initial pro-

1/ Specifically this paper attempts to address issues comprising Task IV of "Outline of Investigation and Study", Motor Carrier Rate-making Study Commission (September 29, 1981).

competitive interpretation of the new legislation. Section V then reviews available evidence on entry, rates, financial condition, concentration and service to small communities in the post-MCA environment, comparing actual changes with the predicted effects of reform according to the alternative rationales. Section VI focuses on ICC implementation of the MCA and other developments in recent months, and the case for further regulatory reform is made. The paper's overall conclusions are presented in Section VII.

II. Alternative Rationales for Motor Carrier Regulation

A number of explanations have been offered for motor carrier regulation but these generally fall into two basic categories: the "public interest" rationale and the "special interest" rationale. According to the public interest rationale, an unregulated trucking industry would fail to make efficient use of society's scarce resources or would create inequities for certain segments of society. Regulation is needed, as the argument goes, to correct for "market failure". The special interest rationale, by contrast, attributes regulation to the successful lobbying efforts of the industry, efforts intended to insulate trucking firms from the forces of competition.

Proponents of the public interest rationale allege that competition in trucking is not feasible because it would lead to natural monopoly, it would be destructive or predatory, and/or it would undermine the common carrier system. The natural monopoly argument for regulation for example assumes that the production of motor freight service is subject to unlimited scale economies which would give larger firms, with their lower unit costs, a competitive advantage over smaller firms. The larger firms could drive smaller competitors from the industry by charging lower prices, and in so doing increase their market shares. Alternatively one would expect the industry to become more concentrated through mergers as firms seek to exploit the economies of larger scale. Eventually one firm would dominate the market and proceed to exploit its monopoly position. That

position would be protected from erosion by scale economies, a natural barrier to entry. The conventional wisdom is that regulation is needed (1) to ensure that the economies of large scale production are realized (the monopoly franchise) while (2) preventing monopolistic exploitation (maximum rate regulation, rate of return regulation, etc.).

Market failure in trucking is alleged by some to take the form of destructive competition, rather than natural monopoly. Economists might characterize competition as destructive if "rate wars" result in chronic losses for all participants and there is a deterioration of service to the public as carriers cut corners in an attempt to reduce costs. This argument assumes that trucking has the following characteristics: (1) a high ratio of fixed costs to total costs--otherwise carriers would simply shut down bringing the downward spiral of rates to a halt, (2) large sunk costs--otherwise disinvestment would occur (exit from the industry or downsizing of existing carriers) relieving the downward pressure on rates, and (3) long term decline in demand causing excess capacity to be a chronic problem. Together these characteristics make it difficult for a new equilibrium to be achieved following an outbreak of price competition. Entry restrictions, capacity control and minimum rate regulation are viewed as the appropriate remedies for the destructive competition problem.

Still others see a need for trucking regulation to prevent carriers from achieving or maintaining a monopoly position

through predatory practices. It is argued for example that a predator can engage in below-cost pricing until even equally efficient competitors are driven from the market, and then raise rates again to exploit the monopoly position attained. The predation argument assumes that the predator is the dominant firm with significant market power--otherwise it does not pose a credible threat to competitors nor will it have greater staying power in the event of below-cost pricing. There must also be barriers to entry and re-entry so that the predator has the opportunity to raise rates to the point that excess profits will be generated and thereby more than offset the losses incurred in selling below cost. Rate regulation has been suggested as the appropriate method of dealing with predatory pricing although the antitrust laws would also apply here.

A final allegation of market failure for the trucking industry is the argument that competition will fail to produce a common carrier system whereby carriers hold themselves out to serve the general public and shippers are treated equally, whether they be along major traffic corridors or located in small communities in isolated areas. It is argued that restrictions on entry and high rates are needed to generate the excess profits on dense traffic lanes that will be used by regulated carriers to cross-subsidize service on less dense and presumably unprofitable routes. Some believe that without regulation shippers in small rural communities would lose service or at least be required to pay sharply higher rates.

Whether an unregulated trucking industry would misallocate society's scarce resources or fail to achieve other social objectives is essentially an empirical question. Those who have examined the evidence, and found the market failure arguments lacking, offer an alternative rationale for motor carrier regulation. They argue that regulation serves the industry's interests, not the public's, by suppressing competition. According to this view regulation has converted an otherwise competitive trucking industry into a government-enforced cartel. 1/ If this view is correct, deregulation should lead to lower rates as independent ratemaking and additional competitors squeeze out excess profits and force carriers both large and small to reduce costs if they are to remain viable. Rates would become more responsive to changing market conditions and over time would track costs more closely as competition undermines discriminatory rate structures. Price-service options would also match more closely what shippers demand at competitive prices.

1/ For an elaboration of this view see Statement of Denis A. Breen, Bureau of Economics, Federal Trade Commission, Submitted to the Motor Carrier Ratemaking Study Commission (November 18, 1981), pp. 4-25.

III. The Motor Carrier Act as an Experiment in Deregulation

The Motor Carrier Act of 1980 represents the first significant reform of trucking regulation since the industry became regulated in 1935. The new law was designed to ease entry and increase price competition and for that reason provides an opportunity to compare the predicted effects of deregulation, which vary according to the rationale for regulation being considered, with actual results. The observed changes in industry structure, conduct and performance will tend to support one of the explanations while being inconsistent with the others. In this way many of the rationales offered can be discarded as not useful in understanding why the trucking industry is regulated.

Before examining the effects of regulatory reform several caveats should be made. The post-MCA experience does not represent an ideal controlled experiment in deregulation. First, the industry was not in fact totally deregulated by the MCA. It is legitimate to ask whether changes have been significant enough to have a measurable impact, and whether pro-competitive statutory provisions are in practice nullified either by other provisions that preserve regulation or by restrictive ICC implementation. Second, the new law has only been in effect one-and-a-half years. Have significant changes already occurred and if so have they been adequately studied? Third, regulatory reform has occurred simultaneously with economic recession. Is it possible to isolate the effects of the MCA from those of the recession?

In response to the questions raised above it can be said that sufficient data is available to indicate that regulatory reform has produced some significant changes in the trucking industry. These changes enable one to make a first cut at eliminating less useful rationales for trucking regulation. In addition it is possible, at least in a qualitative if not quantitative sense, to separate the effects of regulatory reform from those of the recession. Of course where the experiment in deregulation appears cloudy, any conclusions can only be of a tentative nature.

IV. Major Pro-Competitive Features of the Motor Carrier Act

A. National Transportation Policy

Congress provided the ICC with an additional set of national transportation policy goals to serve as guidelines for motor carrier regulation. These include meeting the needs of shippers and receivers, promoting the efficient use of the industry's resources, providing fair returns to owners and fair wages and working conditions for employees, and maintaining service to small communities. The means by which the ICC is to achieve these goals is through greater reliance on competition and efficiency. 1/ In addition, specific statutory restrictions on entry and rate competition have been relaxed in the manner described below.

B. Motor Carrier Entry Policy

The MCA preserves the fitness standard used to evaluate applicants for operating authority. An applicant must continue to prove that he is fit, willing and able to perform the proposed service. What has been modified is the public convenience and necessity test. Previously, to prove the proposed service was required by the public convenience and necessity, an applicant needed to demonstrate that (1) the service will serve a useful public purpose responsive to a public need, (2) existing service is inadequate and (3) the proposed service will not harm existing carriers. 2/ Any interested party could protest

1/ See Section 5 of the MCA.

2/ Pan-American Bus Lines Operation, 1 M.C.C. 190, 203 (1936).

an application and the burden of proof was always on the applicant.

Now the Commission is directed to issue a certificate if it finds, based on evidence submitted by the applicant, that the proposed service will serve a useful public purpose responsive to a public demand or need unless it finds, based on evidence submitted by protestants, certification would be inconsistent with the public convenience and necessity. ^{1/} The applicant's burden of proof has been reduced to demonstrating a public need for the proposed service. The Commission will consider whether the service would promote any of the national transportation policy goals. The effect that the service would have on existing carriers may also be considered but that by itself would not be grounds for rejecting the application. Protestants will now bear the burden of proving that the service would be inconsistent with public convenience and necessity. Those seeking to file protests must also be able to demonstrate that they have competing authority, are fit, willing and able to provide the service, and have solicited the traffic or actually provided service of the type in question.

The statutory changes reduce the prospective entrant's burden of proving public convenience and necessity while at

^{1/} The public convenience and necessity test has been dropped entirely for: (1) small shipment specialists, (2) carriers serving the U.S. government (with exceptions), (3) carriers serving communities where rail service has been abandoned or where authorized motor carriers have not been providing service, and (4) owner/operators hauling food and other edible products and agricultural fertilizers.

the same time competitors will find it more difficult to use the regulatory process to block entry. As regulatory barriers to entry are relaxed, those incumbent carriers that were earning excessive profits will be subject to increasing competitive pressure.

Following passage of the MCA, the ICC issued a policy statement to guide carriers in requesting operating authority. 1/ Consistent with the promotion of competition and efficiency, the Commission asked carriers to apply for "broad, unencumbered authority." The Commission indicated its preference for the use of a limited number of generic commodity descriptions in certificate applications. In terms of geographic scope, irregular-route applications are expected to be at least countywide and provide for service in both directions. Regular-route carriers are expected to apply for two-way authority with service to all intermediate points, and to those off-route points desired. The ICC made clear its intention not to allow operating restrictions except in highly unusual circumstances.

The Commission reasoned that broad, unencumbered authority enables carriers to make more efficient use of their equipment, to offer a more complete service to shippers, and to respond to new service demands without having to return to the ICC repeatedly with requests for additional authority. Broad grants also make it more likely that shippers and communities of all types

1/ Ex Parte No. 55 (Sub-No. 43A), Acceptable Forms of Requests For Operating Authority (Motor Carriers and Brokers of Property), Federal Register (December 31, 1980), pp. 86798-86810.

will be served. Finally, broad grants mean that carrier operating authorities will tend to overlap more than in the past in terms of geographic or commodity scope. This overlap increases the number of potential as well as actual entrants and thereby puts additional competitive pressure on incumbent carriers.

C. Removal of Certain Restrictions on Motor Carrier Operation

Congress found that many of the restrictions created by the terms and conditions previously attached to certificates serve little or no public purpose. The Commission was given 180 days to eliminate gateway restrictions and circuitous route requirements and to establish procedures to promote an expeditious consideration of applications seeking to reasonably broaden commodity authority, to eliminate excessively narrow geographic authority, to add intermediate points and back-haul authority, etc. Congress intended that restriction removal would promote operating efficiencies and fuel conservation.

In Ex Parte No. MC-142, Elimination of Gateway Restrictions and Circuitous Route Limitations ^{1/} the ICC issued rules which allow carriers that have authority to provide through service to perform that service over any available route. Carriers are not required to notify the Commission of the use of alternate routes. The Commission in a related rulemaking, ^{2/} established procedures to be followed by carriers in filing restriction

^{1/} Federal Register (December 31, 1980), pp. 86741-86747.

^{2/} Ex Parte No. MC-142 (Sub-No. 1), Removal of Restrictions from Authorities of Motor Carriers of Property, Federal Register (December 31, 1980), pp. 86747-86761.

removal applications. Guidelines were issued to assist applicants in determining what restrictions the Commission considers, under normal circumstances to be "excessively narrow, wasteful of fuel, inefficient or contrary to the public interest."

These include (1) commodity classes of three digits or greater in the Standard Transportation Commodity Code, (2) authority to serve a geographic area less extensive than a county, (3) restrictions against intermediate point service on a regular-route operation and (4) certificates authorizing service in one direction only.

Congress intended that the elimination of certificate restrictions would increase carrier operating efficiency by raising load factors, reducing empty back-hauls and creating more direct routes. More efficient operations will in turn improve the competitive position of those carriers previously restricted. Competition, both potential and actual, will also increase to the extent that restriction removal results in broader operating authority.

D. Zone of Rate Freedom

The MCA offers carriers the opportunity to participate in a zone of rate freedom whereby they can raise or lower rates by as much as 10 percent over rates previously in effect, without threat of suspension or investigation by the ICC on grounds that the rates are unreasonable. The zone was created to stimulate rate competition and provide for greater rate flexibility and this was to be accomplished by restricting the Commission's

authority to review rate changes initiated by individual carriers. The MCA also explains how the zone can be widened, within prescribed limits, by the ICC, through rulemaking proceedings.

In August 1980, the Commission issued procedural rules that "will require carriers to furnish sufficient information to allow identification and analysis of rates, charges, and provisions filed under the zone of rate freedom." ^{1/} One rule requires that a participating carrier state that its rates were not discussed with any other carriers. This rule exists because there is no antitrust immunity for rates implemented through the zone.

E. Rate Bureaus

Historically collective ratemaking agreements that had ICC approval were exempt from application of the antitrust laws. The ICC can continue to approve collective ratemaking agreements under the MCA, but only if they are not inconsistent with the new set of national transportation policy goals. In any event:

- (a) beginning in 1981, only those carrier members with authority to handle the traffic in question may vote on a rate proposal;
- (b) beginning in 1984, no agreement may provide for discussion or voting on individual, single-line rates.

In other words, it will become illegal for single-line carriers competing on a given route to agree upon the rate to be charged.

^{1/} Docket No. 37416, Identification of Rates Filed Under Zone of Rate Freedom by Motor Common Carriers of Property and Freight Forwarders, Federal Register (August 6, 1980), pp. 52161-52163.

Other provisions of the MCA prohibit certain rate bureau practices which serve to discourage independent pricing by individual carriers. A rate bureau may not protest tariff changes proposed by any individual member or non-member carrier. Rate bureau employees are not allowed to docket or act upon rate proposals of individual members. Nor may rate bureaus in any way interfere with independent action proposals.

Congress sought to bring collective rate making out from behind closed doors and thereby insure that shipper interests are better represented. Rate bureau meetings must be open to the public and bureaus must divulge, upon request, who proposed rate changes and how members voted on the rate proposals.

The ICC undertook a rulemaking to implement the rate bureau provisions of the MCA and establish new rules to govern the activities of motor carrier rate bureaus. 1/ One of these is that member carriers taking independent action (IA) shall have the absolute right to decide whether or when rate bureaus will docket these actions. Historically when a carrier directed its rate bureau to publish an IA, the bureau entered the proposal in its files and gave notice of the proposal to other members. The bureau did not immediately file the proposal with the ICC; rather it gave other members time to decide whether they too wanted to have the rate proposal published for their accounts. With advance notice, competitors could match a rate cut even before

1/ Ex Parte No. 297 (Sub-No. 5), Motor Carrier Rate Bureaus--
Implementation of P.L. 96-296, Federal Register (December 31,
1980), pp. 86736-86737.

it went into effect, giving the initiator no lead time to enjoy a competitive advantage. The new rule gives carriers the option of instructing the rate bureau to file the IA without advance docketing, or in the words of the Commission, the independent actor "will have the ability to gain a competitive advantage if it so desires." 1/

In sum, the rate bureau provisions of the MCA and the subsequent ICC rulemaking restrict rate bureau practices and provide incentives for individual carriers to set rates independently. The result should be increased rate competition in the regulated trucking industry.

1/ Ex Parte No. 297 (Sub-No. 5), decision served December 30, 1981, p. 11.

V. Effects of Regulatory Reform: A Review of Available Evidence

A. The Motor Carrier Act and Economic Recession

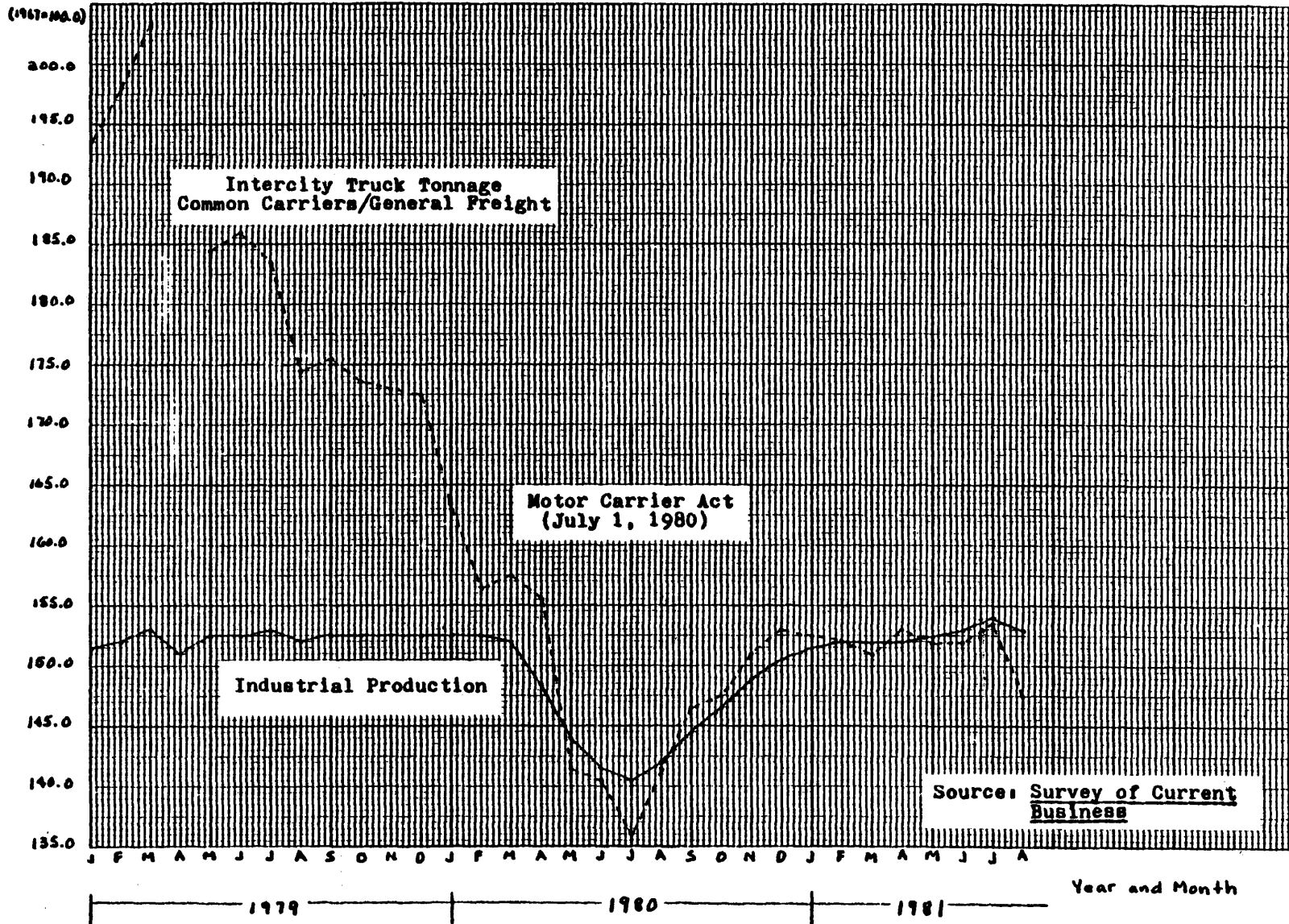
The changes observed in industry structure, conduct and performance in the post-MCA period cannot be attributed solely to regulatory reform. Obviously the state of the economy also has an impact on the trucking industry. Freight carried, for example, varies directly with the level of industrial production. The chart on the next page shows that industrial production moved along sluggishly in 1979 and then declined during the first half of 1980. After a modest rebound, industrial production leveled off in 1981 at about the 1979 level. Intercity truck tonnage declined throughout most of 1979 and during the first half of 1980 before rebounding somewhat. The annual index for freight carried in 1981 may be somewhat higher than that for 1980 but will still be significantly below the 1979 level.

The MCA was signed into law on July 1, 1980 coinciding with the cyclical low point for intercity truck tonnage. The implementation of the MCA has occurred during a period, generally speaking, when the economy continues to be sluggish and the regulated trucking industry remains in a slump. Allowance must be made for these economic conditions when evaluating the impact of regulatory reform.

As a recession reduces the derived demand for trucking service, and thus freight carried, one would expect to observe excess capacity and downward pressure on motor carrier rates.

INDUSTRIAL PRODUCTION AND INTERCITY TRUCK TONNAGE (1979-1981)

Freight and
Production Index
(1967=100.0)



There is evidence indicating that general rate increases were smaller than average during the recession years of 1970 and 1975 suggesting that economic decline constrains pricing behavior in trucking. 1/ There is no evidence though that independent action rate reductions tend to become widespread during recessions.

1/ Interstate Commerce Commission, Office of Policy and Analysis, The Effects of Recession on the Motor Carrier Industry (June 1981), p. 44.

The economic characteristics of trucking are such that operations can be contracted in line with reductions in demand. Specifically, trucking firms have flexibility in adjusting the size of the work force, vehicle purchases can be postponed (a significant proportion of tractors wear out each year), and purchases of transportation services from subcontractors can be reduced. 1/ These adjustments will result in cost savings and a reduction in excess capacity, which in turn will ameliorate recession-induced declines in profitability.

While profitability in trucking is less volatile than the amount of freight carried, any decline for the industry during a recession may lead to failure for what are otherwise marginal firms. Reduced profitability is also likely to cause trucking firms to postpone plans for expansion and to act as a disincentive to enter the business.

The effects of recession will be taken into account as we proceed to examine the impact of regulatory reform on the trucking industry. The evidence reviewed in the following subsections is taken from a variety of public documents and published reports that in one way or another assess the effects of increased competition. The pace of regulatory reform was accelerated in 1979 under Chairman O'Neal, in 1980 under Chairman Gaskins and during the first six months of 1981 under Acting Chairman Alexis. Thus, a review of the evidence for this period of increased

1/ Ibid., pp. 55-63.

competition, which includes twelve months under the MCA, should provide the strongest test of the alternative rationales for regulation. ICC implementation of the MCA since June 1981 i.e., under Chairman Taylor, will be discussed in Section VI.

B. New Entrants and Expansion by Existing Carriers

The ICC, first under Chairman Gaskins and then under acting Chairman Alexis, moved rapidly to implement the pro-competitive provisions of the MCA. In so doing they accelerated the process of removing regulatory barriers to entry, a process that was being undertaken administratively even before the MCA became law in July of 1980. 1/ The number of applications for operating authority increased from 6,746 in fiscal 1976, a pre-regulatory reform year, to 22,735 in fiscal 1980. For the twelve month period following enactment of the MCA, the number was 29,311. The percentage of applications approved by the Commission in whole or in part also rose; from 69.8 percent in fiscal 1976 to 97.4 percent in fiscal 1980 and 95.4 percent for the twelve months beginning July 1980. While most grants have taken the form of extensions for 17,000-18,000 previously certificated carriers, new entry has also occurred despite the recession. Grants to new entrants numbered 2,452 for the July 1980-June 1981 period, up from 1,423 in fiscal 1980 and 468 in fiscal 1976. 2/ New entrants seem

1/ See for example the manner in which the public convenience and necessity test was modified by the ICC in Ex Parte No. MC-121, Policy Statement on Motor Carrier Regulation (October 17, 1979).

2/ Data on applications for fiscal 1976 and 1980 are from Interstate Commerce Commission, Office of Policy and Analysis, (Continued)

to concentrate, at least initially, on truckload business (either general or special commodities) where capital requirements and administrative skills are less. 1/ With the approval of more de novo applications and certificate extensions, shippers are being solicited by an increasing number of competitors.

A further indication of relaxed entry standards is expansion in the scope of certificates sought and granted. Certificates granted in 1981 are less likely to contain operating restrictions and narrow geographic and commodity descriptions. This is apparent when 1981 certificates are compared to 1980 certificates and even more apparent when compared to certificates granted in 1976. 2/ This trend is consistent with the policy established in Ex Parte No. 55 (Sub-No. 43A) that applicants are to seek broad, unencumbered authority. Perhaps the most dramatic change was the willingness of the ICC to grant nationwide, general commodity authority, these grants occurring at the rate of about one per week beginning in January 1981. 3/ Broad certificates are

(Footnote Continued)

The Effect of Regulatory Reform: Structure, Conduct and Performance (June 1981), pp. 43-49 and for July 1980-June 1981 are from statement of Reese H. Taylor, Jr., Chairman, Interstate Commerce Commission, Before the Joint Economic Committee on the Motor Carrier Act of 1980 (November 17, 1981), Appendix IV.

1/ Interstate Commerce Commission, The New Region One Motor Carrier (June 1981), pp. 2-5.

2/ The Effect of Regulatory Reform, op. cit., pp. 49-52.

3/ "Trucking: Current Analysis", Standard & Poor's Industry Surveys (September 10, 1981), p. T-130.

more likely to overlap and this increases the number of potential competitors for a particular type of traffic.

Despite a sluggish economy, carriers are expanding operations into newly acquired territories. Equipment is being reassigned and terminals are being added to carrier networks. Between 1977 and 1980 the number of terminals operated by the 25 largest carriers increased 18 percent. 1/ During the first twelve months following the MCA, Consolidated Freightways added 42 terminals while Yellow Freight added 100 even though recession-level traffic might be inadequate to cover the higher fixed costs. 2/ Carriers seem to be positioning themselves for competition in a less regulated environment even if this means adding to capacity during a recession.

C. Restriction Removal

The ICC's Restriction Removal Board received about 2,700 applications between January 2 and June 2, 1981, and all applications were approved as published in the Federal Register. 3/ Carriers sought broader commodity and territorial authority as well as the authority to serve intermediate points and provide two-way service. These applications are consistent with the

1/ Ibid.

2/ "What Deregulation Has Done to the Truckers", Business Week (November 9, 1981), p. 70.

3/ See Statement of Marcus Alexis, Acting Chairman, Interstate Commerce Commission, Before the Subcommittee on Surface Transportation of the House Committee on Public Works and Transportation, on the Motor Carrier Act of 1980 (June 10, 1981), p. 25.

guidelines established in Ex Parte No. MC-142 (Sub-No. 1) in Dec 1980, the purpose of which was to improve carrier operating efficiency and increase competition. Presumably carriers are also using more direct routes as allowed by Ex Parte No. MC-142, but the absence of any requirement to notify the ICC of their use makes it difficult to obtain data on this aspect of restriction removal.

D. Rate Levels and Rate Structure

Regulatory reform and recession have combined to create downward pressure on collectively set rates. Increased discounting by individual carriers has occurred, not through the zone of rate freedom, but as independent actions and independently filed tariffs. Data from annual reports for the ten major rate bureaus indicate that the number of IA's in 1980 exceeded that for any year back to 1975 when IA's were first reported. 1/ ICC investigations of the Middle Atlantic Conference and the Central States Motor Freight Bureau reveal that almost all IA's are rate reductions and that a significant number of carriers have taken advantage of the Ex Parte No. 297 (Sub-No. 5) changes, instructing the rate bureaus to file IA's without giving advance notice to competitors. Furthermore, while independent action in the past typically involved just truckload commodity rates, a significant number of the initiatives now affect LTL class rates. 2/

1/ The Effect of Regulatory Reform, op. cit., pp. 76-78.

2/ Ibid., pp. 80-81.

A variety of rate discounts have appeared since the MCA was passed. Some represent across-the-board percentage reductions such as Overnite's 10 percent cut in LTL rates, 15 percent if shippers deliver the freight to an Overnite loading dock. 1/ Other carriers have been more selective, cutting rates when cost savings can be identified or as competition requires. A number of carriers are offering multiple tender rates--discounts when separate shipments are tendered for pickup at the same time with the size of the discount depending on the aggregate weight tendered. Yellow's multiple tender discounts range from 3-20 percent, Commercial-Lovelace's from 5-15 percent, and McLean's from 5-10 percent. 2/ Roadway Express has offered promotional discounts to build up business in its new marketing territory, the Northwest. Roadway's discount program includes substantial reductions on eastbound shipments from the Northwest in an effort to utilize back-haul capacity more fully. 3/ Aside from these discount programs, carriers are cutting rates for individual shippers to win, or retain business. Numerous carriers filed tariffs at the ICC with discounts for specifically named shippers. 4/

1/ "Report on Recent Rate Action Initiated by Overnite Transportation Company" in Interstate Commerce Commission, Office of Policy and Analysis, Motor Carrier Monitoring Program: Initial Notes from Carrier Contacts and Sources (June 1981).

2/ Standard & Poor's Industry Surveys, op. cit., p. T-129, and Motor Carrier Monitoring Program, "Third Report" (September 1, 1980), p. 8 and "Staff Report No. VI" (May 1981), p. 11.

3/ "Uphill Climb", Barron's (October 12, 1981).

4/ Standard & Poor's Industry Surveys, op. cit., p. T-130.

At the June oversight hearings, Acting Chairman Alexis characterized rate discounting as "healthy pricing behavior" and because of this the Commission had avoided suspension and investigation of the rate reductions. 1/

Some carriers have decided to reduce rates indirectly i.e., by improving the quality of service offered at current rates. The best example is Transcon's guaranteed delivery with penalties ranging up to 20 percent for delayed service. 2/ With some carriers improving service while others are cutting rates, shippers will have a greater variety of price-service options from which to choose.

Rate discounting in the post-MCA environment may be due to the weak economy but there are indications that regulatory reform itself has had an impact. In contrasting the current slump with the 1974-75 recession, industry observers note that shippers are being offered special discount programs, that discounting on LTL traffic is greater, and that even the largest carriers are cutting rates. All this despite the fact that LTL tonnage has fallen by less during the current recession. 3/

Rate discounting reduces freight bills but it is difficult to detect this in an economy where nominal trucking rates continue

1/ Statement of Marcus Alexis, op. cit., p. 29.

2/ Standard & Poor's Industry Surveys, op. cit., p. T-130.

3/ See "Truck Deregulation Has Cut Rising Costs, Improved Service in a Year, Shippers Say", Wall Street Journal (June 30, 1981); "Trucking & Transport Leasing Industry," The Value Line Investment Survey (October 9, 1981), p. 290; and Standard & Poor's Industry Surveys, p. T-129.

to rise because of persistent inflation. LTL rates continue to rise faster than TL rates because of recent rate restructuring and intense competition on TL traffic. In one report, the ICC's Office of Policy and Analysis compares TL general rate increases with those for 1-500 lb. LTL shipments during the period April 1980-April 1981. Increases on TL rates ranged from 6.7-14.0 percent while rates on the smallest LTL shipments rose 12.0-24.8 percent, exceeding the Producer Price Index rise of 11.4 percent. 1/ Another survey indicates that for the period January-August 1981, rate bureaus received rate increases totaling 10 percent on average. Requests for TL rate increases were held to less than 4 percent indicating that the rate increases for the most part involved LTL traffic. 2/ Neither of these surveys takes into account rate discounting. The Wall Street Journal reports that rates increased about 17 percent during the first twelve months following enactment of the MCA but that discounting has reduced this to about 12 percent, approximately the general rate of inflation during that period. 3/ Overall the evidence suggests that regulatory reform has served to restrain rate increases in the trucking industry.

1/ The Effect of Regulatory Reform, op. cit., pp. 81-82.

2/ Standard & Poor's Industry Surveys, op. cit., p. T-133.

3/ "Truck Deregulation Has Cut Rising Costs", op. cit.

E. Financial Condition of the Industry

Increased competition in the post-MCA environment and a weak economy have reduced profitability for the regulated trucking industry. The after-tax return on equity, including intangibles, for all class I and II general freight carriers declined from 16.2 percent in 1978 to 11.9 percent in 1979. 1/ In 1980 the return on equity was actually negative as carriers reported an extraordinary charge to income to account for the loss in value of operating certificates. 2/ No doubt even without this write-off, return on equity would have been less in 1980 when compared to 1979. This is suggested by ICC data on the 100 largest motor carriers of property. The return on equity, before extraordinary charges, for these carriers (excluding UPS) fell from 13.8 percent in 1979 to 11.8 percent in 1980. 3/ Financial performance is expected to be slightly better for 1981. The President of the American Trucking Associations reports that the volume of freight hauled increased about 1.5 percent over the 1980 level and that earnings as a percent of revenue increased somewhat, although this latter figure includes a substantial tax deduction

1/ TRINC's Bluebook of the Trucking Industry (Washington, D.C.: TRINC Transportation Consultants, 1980 and 1979 editions), summary tables.

2/ Net income after taxes was a deficit of \$76,967,000 in 1980 on shareholders' equity of \$3,280,439,000. See TRINC's Bluebook (1981 edition), summary table.

3/ Interstate Commerce Commission, Bureau of Accounts, Large Class I Motor Carriers of Property Selected Earnings Data (1979 and 1980).

for the lost value of operating certificates. 1/ Value Line estimates earnings to net worth for its composite of trucking firms to be 14.0 percent in 1981, up from 12.3 percent in 1980. 2/

Regulatory reform and the recession may have had an uneven impact on the financial condition of carriers of different sizes but little data is available to test this proposition. American Trucking Associations data comparing 1980 with 1979 for Class I vs. Class II carriers indicate that Class I carriers experienced a smaller decline in before-tax income but also a smaller increase in revenue and a larger decline in tonnage, creating a rather mixed picture. 3/ Furthermore, the elimination of financial reporting requirements for the thousands of Class III carriers means that little systematic information is available on the smallest regulated carriers.

A prolonged recession would be expected to eliminate firms that, even with a strong economy, would be considered only marginal, and increased competition due to regulatory reform would be expected to eliminate relatively inefficient firms. It is generally recognized by the Commission, the industry and the financial community that a shake out is underway but there is no

1/ "Despite Economic, Regulatory Uncertainty, Optimism for '82," Transport Topics (December 14, 1981).

2/ The Value Line Investment Survey, op. cit., p. 279.

3/ Reported in Statement of Marcus Alexis, op. cit., pp. 15-16.

evidence of widespread business failure as some have alleged. 1/ The International Brotherhood of Teamsters claims that between August 1980 and June 1981, 416 unionized carriers went out of business 2/ but it is not clear that this figure represents the failure rate of ICC regulated carriers.

Actually it is somewhat surprising that the shake out has not been more substantial if excess capacity plagues the industry to the extent alleged by some analysts. 3/ The problem of recession-induced excess capacity can be solved by the downsizing of carriers in the industry and/or by the exit of some firms. The indication is that many carriers are not reducing their scale of operations; in fact they seem to be adding terminals to their route networks as they plan for the future, even if this means sacrificing short-term profitability. If lower rates in a more competitive environment stimulate demand for the ICC regulated carriers, some of what is now viewed as excess capacity may be needed to handle the increased traffic. In the meantime, pressure is being placed on relatively inefficient carriers to reduce capacity but some observers are suggesting that the inevitable

1/ One observer claims that there "has been a paroxysm of Chapter 11 Bankruptcies filed in the industry" but provides no support for this assertion. See Statement of Grant M. Davis Before the House Surface Transportation Subcommittee: Oversight Hearings on the Motor Carrier Act of 1980 (June 10, 1981), p. 5.

2/ Statement of the International Brotherhood of Teamsters, Chauffeurs, Warehousemen and Helpers of America Before the House Committee on Public Works and Transportation (June 11, 1981), p. 4.

3/ Standard & Poor's Industry Surveys, op. cit., p. T-130.

shakeout has been delayed by certain changes in pension funding laws that create a substantial penalty for closing down losing operations or going out of business. 1/

The Multi-Employer Pension Plan Amendments Act of 1980 established liabilities for many ICC regulated motor carriers when they withdraw from a Multi-Employer Pension Fund, as would be the case when a carrier goes out of business or closes an unprofitable terminal. Complete or partial withdrawal results in notices being sent from the affected pension plans demanding that the carrier pay its share of the plan's total unfunded vested benefit obligations. The 1980 amendments make each individual carrier liable and they eliminated the previous ceiling of 30 percent of an employer's net worth. Since union-managed pension funds have promised members benefits substantially in excess of what can be supported by current employer contributions, withdrawal liabilities can consume as much as 100 percent of a carrier's assets. Transport Motor Express for example incurred a withdrawal liability of over \$8 million when it closed down and dismissed its employees. At the time Transport's net worth was only \$3.6 million. 2/ The new law seems to encourage failing firms to stay in business longer than they otherwise would, and thereby may be partly responsible for excess capacity in the industry.

1/ See for example "Uphill Climb", op. cit., and "What Deregulation Has Done to the Truckers", op. cit.

2/ Reported in "Constitutionality of Multi-Employer Act Tested in Courts", Transport Topics (December 14, 1981).

It is difficult to isolate the effects of regulatory reform, from those of recession, on the financial condition of the industry because one would expect lower accounting rates of return and the exit of marginal firms in either case. Fortunately, there is another measure of profitability--the value of operating certificates--that does isolate the impact of regulatory reform.

Operating certificates have market value when competition in trucking is restricted. Historically the regulation of entry and rates, together with antitrust immunity for collective ratemaking served to generate monopoly profits for trucking firms and those profits were capitalized into the market values of carrier certificates. 1/ With free bidding, the price paid when one carrier acquires the operating rights of another, tends to equal the present value of the future stream of monopoly profits which the acquiring firm expects to receive from operating in an environment where competition is suppressed. 2/

1/ See Thomas Gale Moore, "The Beneficiaries of Trucking Regulation", Journal of Law and Economics (October 1978), pp. 327-343 and James R. Frew, "The Existence of Monopoly Profits in the Motor Carrier Industry", Journal of Law and Economics (October 1981), pp. 289-315.

2/ The value (V) of a given certificate can be expressed as follows:

$$V = \sum \frac{R_1}{(1+r)^1} + \frac{R_2}{(1+r)^2} + \dots + \frac{R_n}{(1+r)^n}$$

where R = expected monopoly profit for a particular period

r = interest rate obtainable on other investments of comparable risk

n = number of time periods over which monopoly profits are expected

Certificates may decline in value during periods of economic recession, but will not lose value entirely because the price paid for a certificate reflects expectations about the entire future stream of profits, not just what happens during an economic slump. By contrast, removing the restrictions on competition should drive certificate values to zero since monopoly profits would no longer be expected.

Certificate values have in fact been on the decline in recent years as the result of regulatory reforms--particularly relaxation of regulatory barriers to entry--initiated by the ICC. 1/ With the passage of the MCA and the pro-competitive interpretation given by the ICC during the first year following enactment, certificates lost virtually all of their market value. The following statement by the Chairman of Consolidated Freightways summarizes industry reaction to the changed circumstances:

The Motor Carrier Act of 1980 is believed by management virtually to have eliminated the ongoing market value of our operating rights. 2/

The Financial Accounting Standards Board (FASB), by October 1980, had concluded that the value of interstate operating rights had been "permanently and substantially impaired" and that this loss should

1/ The decline in certificate values is noted in Interstate Commerce Commission, Office of Policy and Analysis, The Value of Motor Carrier Operating Rights (October 1979), p. 118 and 1980 Financial Analysis of the Motor Carrier Industry, prepared for the American Trucking Associations, p. 11.

2/ Quoted in "Truck Industry May Lose \$800 Million in Federal Operating Rights," Traffic World (October 27, 1981).

be reflected in the carriers' financial statements. 1/ The FASB issued a policy statement in December directing carriers to write off the carrying value of their certificates as an extraordinary charge against income. As of July 1980 these rights were on the carriers' balance sheets at \$785 million. 2/

During the third quarter carriers began announcing the amounts they would write off; this included Consolidated Freightway's \$33.9 million, Yellow Freight's \$30.9 million, Roadway's \$29.7 million, and Ryder's \$24.9 million. In total the 100 largest carriers wrote off \$431.5 million during the third and fourth quarters of 1980. 3/ The writeoff of certificate values is a clear indication that regulatory reform has increased competition in the trucking industry.

F. Concentration Levels

There is no evidence indicating that the passage of the MCA has moved the truckload sector in the direction of dominance by a few large carriers. Firms can enter the TL business with little initial investment and be viable competitors. With the MCA's relaxation of regulatory barriers there has been an influx of small scale TL competitors and non-union owner operators, in particular, have

1/ Financial Accounting Standards Board, Accounting for Intangible Assets of Motor Carriers (October 24, 1980), p. 10.

2/ Reported in Standard & Poor's Investment Surveys, op. cit., p. T-147.

3/ Interstate Commerce Commission, Bureau of Accounts, Large Class I Motor Carriers of Property Selected Earnings Data for Twelve Months Ended December 31, 1980, pp. 13-15.

been able to undercut the rates of large established common carriers on front-haul traffic. Many large common carriers are experiencing declining market shares on TL freight, 1/ which suggests that the effect of the MCA may have been to reduce concentration in this sector.

Regulatory reform may also have altered the size distribution of firms in the less-than-truckload sector but again evidence is lacking that large carriers are growing at the expense of smaller competitors. Large carriers do seem to be expanding but this is being accomplished by entering each other's marketing territories, not via horizontal mergers. The observed method of expansion tends to reduce concentration on particular routes as shippers have more carriers from which to choose. 2/ This method of expansion may lead to an industry with fewer firms but the evidence to date does not support this proposition. Some small carriers are being forced to leave the industry but an even larger number

1/ See The Value Line Investment Survey, op. cit., pp. 280, 284, 290, 296, and 299.

2/ This argument could be tested if the Continuing Traffic Study data for the post-MCA period were made available for study. Concentration ratios could be calculated and compared to those for a pre-regulatory reform period. Four-firm concentration ratios for 1976, for example, were surprisingly high for an industry with over 16,000 firms. Focusing on major LTL traffic corridors it was determined that the 4-firm ratio ranged from 60-65 percent for all city pairs. For routes in the west and southwest the ratio was about 80 percent on average but for a significant proportion of routes it was over 90 percent. [See Testimony of Senator Edward M. Kennedy before the Senate Committee on Commerce, Science and Transportation on the Trucking Competition and Safety Act of 1979 (June 26, 1979)]. It is unlikely that the concentration ratios have remained this high in the post-MCA environment.

seem to be entering. Nor is there any evidence that large carriers are systematically underpricing smaller competitors or consistently earning higher profits. According to one report the largest carriers, in fact resisted involvement in the post-MCA, rate discounting episodes. 1/ Finally, carrier expansion is to be expected given the manner in which regulation has historically restricted the scope of operations, but there is no evidence that a carrier must provide nationwide trucking service to be operating at an efficient scale.

G. Service to Small Rural Communities

Section 28 of the MCA directs the ICC to study the impact of regulatory reform on motor carrier service to small rural communities. An interim report has been released based on the results of a survey in which shippers were asked to compare service during the first six months following passage of the MCA with pre-MCA experience. 2/ The ICC found that service availability for the most part was unchanged. Where service had changed more shippers said it had improved. In addition, while some shippers reported losing service from one or more carriers, more reported that new carriers were offering service. Service quality--on-time performance, freight loss, and claims settlement--was also unchanged for the most part. Here too where it had changed, more shippers reported it had

1/ Standard & Poor's Investment Surveys, op. cit., p. T-129.

2/ See Interstate Commerce Commission, Office of Policy and Analysis, Interim Report: Small Community Service Study (June 1981).

improved. The ICC also checked its complaint file but found nothing to indicate that small communities were being abandoned.

The American Trucking Associations criticized the interim report because it did not explain what has happened to rates on service to small communities. 1/ It could be that while small communities have not been abandoned, the shippers are paying sharply higher rates as the alleged cross-subsidy is eliminated. Those making this argument however have offered no empirical support. The scant evidence that is available suggests that small communities are probably not paying more for service. 2/ That certainly seems to be the case in Florida where intrastate trucking was totally deregulated at the same time the federal MCA was signed into law. ICC staff examined unregulated intrastate tariffs and reached the following conclusions:

Our review of tariffs in Florida....suggests that carriers still voluntarily list small community points, and have not taken actions to shed this service or substantially increase small community rates. 3/

1/ "Critique of the ICC Report--Interim Report: Small Community Service Study", Appendix F to Letter of Nelson J. Cooney, General Counsel, American Trucking Associations to the Honorable Glenn M. Anderson, Chairman, House Subcommittee on Surface Transportation (July 9, 1981).

2/ See for example, Statement of Henry Eschwege, Director, Community and Economic Development Division, General Accounting Office Before the Committee on Commerce, Science, and Transportation, U.S. Senate, 97th Cong., 1st sess. on Oversight of the Motor Carrier Reform Act of 1980 (June 18, 1981).

3/ Interstate Commerce Commission, Office of Policy and Analysis, Initial Carrier and Shipper Responses to Intrastate Trucking Deregulation in Florida (June 1981), p. 11.

In fact they found that many of the small community rates sampled had declined.

H. Conclusions

Regulatory reform has produced enough change in the structure, conduct and performance of trucking that at least a preliminary empirical basis now exists for evaluating the alternative rationales for regulation offered at the outset of this paper. The first conclusion is that changes observed in the post-MCA environment cannot be explained by recession alone; regulatory reform has also had a significant impact on the trucking industry. New entry and carrier expansion into new marketing territories has been observed despite a sluggish economy. Rate discounting has been more widespread during the current recession despite less of a drop in LTL tonnage. Consistent with both increased competition and recession there has been a decline in profitability and exit by some marginal firms but we also know that certificates have lost their value which is consistent with only the increased competition hypothesis.

Adherents to the natural monopoly rationale for regulation predict that more competition will result in increased concentration as (1) mergers between competitors occur or (2) larger carriers underprice smaller firms and drive them from the market. Eventually rates are raised to monopoly levels. In fact horizontal mergers among major competitors are not occurring nor is there any evidence of large carriers systematically underpricing smaller competitors. Large carriers are growing by entering one another's territory which tends to decrease concentration on individual routes.

Some firms are exiting, but not just small carriers. At the same time new entry is occurring and not necessarily on a large scale. All of these findings cast doubt on the scale economies assumption underlying the natural monopoly argument for regulation.

The predicted result of unregulated competition according to the predatory pricing rationale for regulation is that dominant carriers will engage in below-cost pricing to eliminate their competitors and then raise rates to monopoly levels. It is true that carriers are cutting rates; in some cases selectively and other cases across-the-board, but even the selective rate discounts generally do not exceed 20 percent. This, according to several studies, is approximately the amount by which regulated trucking rates would need to fall to reach cost-based competitive levels. ^{1/} There would seem to be nothing predatory here, just healthy price competition.

Predatory pricing does not appear to be a rational strategy in the post-MCA environment where the only significant barrier to entry and expansion--regulation--has been relaxed. The threat of entry would ensure that a would-be predator would never have the opportunity to raise rates to monopoly levels to recoup earlier losses from below-cost pricing. The most publicized allegation of predatory pricing is that against Roadway Express

^{1/} These studies are reviewed in Congressional Budget Office, "Inflation Impact Statement on Trucking" (March 26, 1980).

for cutting rates on shipments to and from the Northwest. 1/ A 10 percent discount was offered on LTL and "any quantity" rates to points in Idaho, Oregon, Utah and Washington. Eastbound discounts of 34 percent were offered on multiple shipments weighing an aggregate of 5,000 lbs. or more and 50 percent on single shipments weighing at least 5,000 lbs. Do these discounts represent below-cost selling for the purpose of eliminating equally efficient competitors in the Northwest? It is highly unlikely that Roadway Express has the staying power needed to drive Consolidated Freightways, P-I-E, Garrett, Transcon, T.I.M.E.-DC and a host of others from the area, nor it is clear how Roadway could prevent re-entry or new entry if it sought to raise rates to monopoly levels. A more plausible explanation is that Roadway, a new entrant in the Northwest, was offering promotional discounts to gain a foothold in its new marketing territory and that the substantial discounts on eastbound shipments reflect cost considerations, such as the low cost of hauling freight in what is recognized as the back-haul direction. Part of the eastbound discounts may also be intended to compensate for an apparent competitive disadvantage Roadway has with respect to transit time on those shipments. 2/

1/ See, for example, the dissenting opinion of Chairman Taylor concerning the Roadway discount tariff in which he calls for suspension of the proposed rate cuts. Reported in "Rate Discount Battle Between Roadway, PIE Held Up by Court Action," Traffic World (September 21, 1981).

2/ Transit time differences are discussed in Inland Empire Freight Traffic Assoc., "Transportation Digest" (September 29, 1981), p. 3.

Finally, several carriers were able to match even the "34/50" discounts. Thus what some would label as predatory seems to be the type of healthy price competition that the MCA was intended to promote.

A third rationale for regulation--destructive competition--implies that unregulated competition would degenerate into rate wars, widespread losses and a deterioration of service. Large sunk costs would create a barrier to disinvestment i.e., excess capacity, which would make rate wars and losses a chronic problem for the industry. Increased price competition has occurred as a result of regulatory reform and recession but it would be incorrect to characterize this as a downward spiral of rates, the typical rate war scenario. Increased competition has also reduced profitability but there is no evidence of widespread losses or deterioration of service to the shipping public. The extent of excess capacity is more difficult to assess. Some have suggested that the shakeout of marginal carriers is being delayed, making a downward adjustment in capacity more difficult to achieve. If there has been a barrier to disinvestment it is not to be found in the inherent characteristics of trucking for all these imply rapid capacity reduction to restore equilibrium. One must look for non-market barriers such as, perhaps, the liabilities imposed by multi-employer pension funds. Aside from this one possible constraint on adjustment, there has been nothing in the post-MCA experience to indicate that a new equilibrium could not be quickly restored following an outbreak of price competition.

Consider also the common carrier rationale for regulation which predicts that unregulated competition will lead to the cessation of service to small communities or at least sharply higher rates. What has actually been observed is that service availability and quality are pretty much the same as before. Furthermore, evidence is lacking that rates on small community service are sharply higher. These findings are consistent with several studies indicating that even pre-MCA common carriers were not forced to provide service to groups of shippers at rates that fail to cover costs. 1/

Overall there is little in the post-MCA experience to support a market failure rationale for regulation. Competition appears to be feasible in trucking, if given a chance, and findings on new entry, downward pressure on rates and costs, and the squeezing out of inefficiently employed resources indicate the nature of benefits to be realized by removing restrictions on competition.

1/ Some of these studies are summarized in Statement of Denis A. Breen, op. cit., pp. 28-31.

VI. The Case for Further Reform

The MCA has eased entry and stimulated price competition in the trucking industry but the full benefits of unrestricted competition have yet to be realized. The need for further reform is vividly illustrated by the turn of events in recent months. Applicants for operating authority are suddenly finding it more difficult to obtain broad certificates, and a legislative proposal to raise the fitness standard for entry has been developed at the ICC. The ICC is also scaling back some previously granted certificates that are considered to have been too broadly written. As for rates, tariffs are now more closely monitored and competitive rate discounting is being viewed by the ICC as discriminatory and predatory. Finally, there has been one successful court challenge by the trucking industry to the ICC pro-competition interpretation of the MCA, and several other challenges are pending. One researcher has testified that these recent restrictions on competition are making operating certificates valuable once again. 1/

Chairman Taylor has taken a good deal of blame in the press for the ICC's policy reversal but his behavior is symptomatic of a more basic problem: the MCA did not deregulate the trucking industry. The new legislation represents a political compromise between traditional regulation and free market competition. As such, certain provisions designed to promote competition are

1/ See Testimony of Thomas Gale Moore Before the Joint Economic Committee, on Trucking Regulation (November 17, 1981), p. 10.

inconsistent with the tradition of regulation preserved in other sections. The MCA also offers regulation-minded Commissioners, such as Chairman Taylor, enough latitude to attempt re-regulation. Alternatively it leaves a deregulation-minded Commission open to court challenges by the industry. As the four examples discussed below indicate, the gradual, piecemeal approach to trucking reform continues to impose costs on society without generating identifiable benefits.

First, the MCA continues to require the ICC to consider the fitness of an applicant in determining whether operating authority is to be granted. Historically, the ICC has carefully considered each applicant's financial situation and business experience, whether the applicant is likely to abide by the ICC rules and statutory provisions, and whether the applicant has the equipment needed to provide service, as proposed, and can do so safely. Obviously a vigorously enforced fitness standard can create a barrier to entry of a type that does not exist in unregulated markets.

In the early post-MCA environment, deregulation-minded commissioners approved a large number of new licenses which were quite broadly written in terms of commodity and geographic scope. This behavior was consistent with the pro-competitive provisions of the MCA, but it could only be accomplished by downplaying the traditional fitness standard. The American Trucking Associations took the ICC to court claiming the Commission's manner of implementing the MCA exceeded its statutory authority. On October 1, 1981 the

U.S. Court of Appeals for the Fifth Circuit, New Orleans agreed that procedures adopted by the ICC for removal of operating restrictions from existing certificates, and for applications for new authority, led to the issuance of broad certificates without proper consideration being given to whether the carrier was fit, willing and able to provide the service authorized. 1/ The court referred to several cases where the applicant had neither the right type of trucks nor enough of them to provide the extensive service authorized. Apparently the court did not consider that the carrier could add equipment and move into a new territory as business conditions warranted without having to return repeatedly to the ICC to obtain a certificate for each new route or commodity. The Court remanded to permit the ICC to enact rules that do not exceed the statutory bounds, but gave no indication what the ICC should do about the thousands of broad certificates presumably granted illegally under Gaskins and Alexis.

Chairman Taylor claims that he has no intention of turning the fitness standard into a regulatory barrier to entry. In testimony before the Joint Economic Committee, he presented statistics showing that the percentage of certificate applications granted in whole or in part during his first months at the Commission was as high as that under Gaskins and Alexis, and that this was the

1/ See American Trucking Associations, Inc., et al., versus Interstate Commerce Commission and the United States of America, In the United States Court of Appeals for the Fifth Circuit, No. 81-4026 (October 1, 1981).

case even for nationwide, general commodity applications and new entrants. 1/ But this comparison glosses over a basic shift in policy in which, as Marcus Alexis has noted, "quantities may be similar but the quality of grants has deteriorated." 2/ Under Taylor fewer applications are granted in whole as applicants are being ruled unfit to provide broad-based service. 3/ Furthermore, many of the grants counted as nationwide authority were not in fact authority to haul general commodities between any two points in the U.S. 4/

Chairman Taylor's quest for a "meaningful" fitness test has recently taken the form of a legislative proposal. He has drafted legislation to make fitness a more explicit requirement for entry and thereby provide an effective constraint on deregulation-minded Commissioners. 5/ The adverse court ruling, together with individual ICC entry decisions and legislative proposals to raise the fitness standard are creating an obstacle to regulatory reform.

1/ See Appendix IV of Statement of Reese H. Taylor, Jr. Chairman, Interstate Commerce Commission, Before the Joint Economic Committee, on the Motor Carrier Act of 1980 (November 17, 1981).

2/ Rebuttal Testimony of Marcus Alex Before the Joint Economic Committee (November 17, 1981).

3/ Applications are also scaled down because evidence of shipper support is being ruled inadequate i.e., the "public need" test is not being met.

4/ Certificates authorizing service between a single plant site and all points in the U.S. for example were being counted as nationwide. Reported in the Wall Street Journal (November 18, 1981).

5/ See Remarks of Interstate Commerce Commission Chairman Reese H. Taylor Jr., Press Briefing (December 15, 1981), pp. 1-2 and attached proposal to amend the Interstate Commerce Act.

If Congress does not resist this trend, the ICC will be returning to the pre-MCA days where fitness was considered at great length on a case-by-case basis, a process that artificially restricted both the number of new competitors and the scope of their operations.

Second, Congress also preserved the traditional common carrier obligation to serve, placing special emphasis on the maintenance of service to small communities. Licensees cannot pick and choose their customers on the basis of profit considerations, as is true in unregulated markets; they are expected to hold themselves out to serve all shippers up to the limits of their operating authorities. Deregulation-minded commissioners no doubt realized that issuing broadly written certificates in an effort to open up the industry might put carriers in jeopardy because it would be virtually impossible for them to fulfill the traditional service obligation. The Gaskins-led Commission proposed to deal with this MCA "Catch 22" by relaxing--in effect defining away--the common carrier obligation through a rulemaking proceeding. 1/ This was a reasonable position to take since studies show the ICC has not enforced a common carrier obligation; nevertheless, small communities manage to get trucking service.

With the proposed rules on service obligations left unsettled by his predecessors, Chairman Taylor took an active interest, soliciting further briefs and holding oral argument. He considers

1/ Ex Parte No. MC-77 (Sub-3), Elimination of Certificates as the Measure of "Holding Out", Federal Register (January 27, 1981), pp. 8604-8606.

the common carrier obligation to be an important cornerstone of ICC regulation, 1/ which has created considerable uncertainty about how the Commission will eventually vote on the proposed rulemaking. A vote to relax the common carrier obligation means that regulatory reform can proceed, while the preservation and enforcement of the common carrier obligation, like a stiffer fitness standard, would necessitate a reversal of the policy of granting broad certificates.

Third, as a practical matter the MCA did little to modify the ICC's power to regulate the structure and level of motor carrier rates. "Unreasonable" rate levels and "unjustly discriminatory" rates continue to be prohibited. Since statutory definition of these terms is absent, interpretation becomes a matter of administrative discretion. In the more competitive post-MCA environment carriers began experimenting with a variety of rate discounts as downward pressure was placed on the overall rate level and incentives were created to align rates more closely with costs. Some carriers offered across-the-board percentage reductions on truckload and less-than-truckload traffic. Others were more selective offering discounts to specific shippers and multiple tender rates. A few carriers tried rate discounting as a promotional device to enter new marketing territories. The ICC led by Gaskins and then Alexis generally permitted proposed rate reductions to go into effect without delay.

1/ Position Paper of Chairman Reese H. Taylor, Jr., Regarding Implementation of the Motor Carrier Act of 1980 (August 14, 1981), p. 9.

More recently, however, the Taylor-led Commission has been taking a closer look at motor carrier tariffs. The presumption seems to be that since pre-MCA rates had ICC approval and were therefore lawful, despite being non-competitive and discriminatory, recent rate discounting should be viewed with suspicion. The Chairman, for example, would have imposed on Roadway Express, the burden of proving that its promotional discounts to shippers in the Northwest were not predatory. 1/ In another case discounts for specifically named shippers were declared prima facie illegal, precluding any consideration of a possible cost justification for the discounts or the useful role that hard bargaining by individual shippers might play as a first step in undermining collusively set rates. 2/ The ICC's recent hard line on selective rate discounts is discouraging competitive rate initiatives and has caused at least one group of carriers to petition the ICC to promulgate standards for the determination of permissible discount tariffs. 3/ Selective rate discounts may be discriminatory in some legal sense under certain provisions of the MCA, but to prohibit them would be a chilling effect on rate competition.

1/ Reported in "Rate Discount Battle Between Roadway, PIE Held Up by Court Action," Traffic World (September 21, 1981).

2/ ICC Special Tariff Authority No. 82-0150, Recission of Authority to Show Shippers' Names (Decided: October 9, 1981).

3/ See "Truck Lines to Seek ICC Guidelines on Permissible Types of Discount Tariffs" Traffic World (October 26, 1981).

Fourth, the MCA did not abolish price-fixing in the trucking industry. Antitrust immunity for agreement on single-line rates is scheduled to expire on December 31, 1983 but even this is subject to the recommendations of the MCRSC and subsequent Congressional action thereon. An agreement by two or more single-line carriers to charge a uniform rate on shipments between points A and B eliminates price competition to the detriment of the shipping public, but consistent with Congressional intent to implement changes "with the least amount of disruption to the transportation system," single-line immunity will be phased out gradually. Former Acting Chairman Alexis has offered the following observation on this approach:

The phased approach was adopted as insurance against unexpected adverse effects; nevertheless, with the benefit of hindsight, it now appears that the feared adverse effects of less regulation have not materialized and that this insurance was acquired at considerable cost. 1/

Also unresolved is whether other aspects of collective ratemaking should continue to enjoy antitrust immunity. For example, the joint consideration of across-the-board rate increase proposals by rate bureau members is still permitted, despite the upward bias this tends to create for rate levels and the protection it provides for relatively inefficient members. Also permitted is agreement on commodity classification ratings, an essential determinant of relative transportation rates for commodities hauled by trucking firms.

1/ Statement of Marcus Alexis, Before the Subcommittee on Surface Transportation, op. cit., p. 12.

This system discriminates against shippers of higher valued commodities whose demand for trucking service tends to be less responsive to the transportation charge but for which the actual costs incurred by the carrier may be no greater than with a lower valued commodity.

Collective ratemaking can continue to impose net costs on society regardless of the pace at which entry reform, for example, proceeds. When entry is restricted, collective ratemaking tends to impose a welfare loss on society corresponding to the value of lost output as price is held above a competitive level, and there is a redistribution of income from shippers and their consumers to the trucking industry in the form of monopoly profits. Even if entry is not restricted, collective ratemaking can waste society's scarce transportation resources. The social costs consist of the net welfare loss, as in the case of restricted entry, and also include excessive non-price competition as non-competitive rates induce carriers to expand service beyond the optimal point. While monopoly profits tend to be eroded by this cost-inflating service competition, the industry's output is produced at a higher cost to society than necessary. The MCRSC has the opportunity to play an important role in eliminating the social costs of collective ratemaking by recommending to Congress that antitrust immunity be lifted as soon as possible for all aspects of collective rate determination. In the meantime, collective ratemaking, along with a stiffer fitness test, an effective common carrier obligation, and ICC interference with rate discounting will continue to impose social costs that cannot be justified by any benefits generated.

VII. Summary and Conclusions

The MCA, as written by Congress and interpreted by the ICC, was intended to stimulate competition in the trucking industry. During the first year following passage of the MCA, a substantial number of firms were permitted to enter the trucking industry and existing carriers took advantage of increased freedom to expand the scope of their operations. Competition among an increasing number of carriers has created downward pressure on rates and forced firms to increase productivity e.g., by seeking removal of restrictions on operating certificates and by seeking concessions from labor. Lower rates and costs will insure that society gets more out of each dollar spent on trucking service. Increased competition also means that the monopoly profits made possible by protective regulation are being squeezed out of the system.

Congress was concerned that increased competition might somehow disrupt the transportation system and for that reason was unwilling to undertake more sweeping reforms. The post-MCA experience demonstrates however that this concern was misplaced. Competition is feasible in the trucking industry. There is simply no good evidence to support assertions that competition is destructive, predatory or leads to natural monopoly, or that service to small rural communities would be abandoned. What has become apparent is that the gradual, piecemeal approach to regulatory reform that Congress adopted was unnecessary and costly.

Price-fixing has yet to be uprooted and attempts are being made to re-regulate entry through a stiffer fitness test, preservation of a common carrier system, etc. The full benefits of competition will not be realized until the regulatory framework for trucking is completely dismantled.

The MCRSC has the responsibility to determine whether anti-trust immunity should continue for motor carrier collective ratemaking. Since collective ratemaking imposes substantial costs on society while alleged benefits are either illusory or could be achieved through less anticompetitive means, the Study Commission should recommend the lifting of antitrust immunity for all aspects of collective ratemaking. The Study Commission should also report on the feasibility of competition as indicated by the post-MCA experience. This report could then serve as a basis for further legislative action to free the trucking industry from regulation.