# Collective Ratemaking by Motor Common Carriers: Economic and Public Policy Considerations*

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## I. INTRODUCTION

The justification for collective ratemaking in trucking and for the antitrust exemption that makes it possible must in the last analysis turn upon how the public interest is affected. The public interest necessarily embraces the interests of all groups affected by trucking service—carriers, shippers, communities, consumers. Each is relevant and important, but not to the exclusion of the others, and it is elementary that to achieve equitableness among all a balancing process is unavoidable.

Shippers are entitled to minimize transportation costs, but not by exacting favored treatment over competitors, and the shipper's interest in the transportation he buys extends not only to the quality and the cost of the service but to a reasonable degree of stability in the rates he pays. Rates must not exploit the users of trucking service and place an unjust burden on

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ultimate consumers, but still must be high enough to permit carriers to finance the amount and kind of service the public wants and needs. Carriers should be motivated to vie for the traffic of customers, but not by undermining competition among the enterprises they serve or the communities in which those enterprises are situated. Communities have a right to expect that rates to resident industries will reflect any natural advantages of location, but they have no claim to preferential rates having nothing to do with superior location. Clearly, the interest of the public as a whole demands not simply the lowest possible rates, but the lowest possible rates consistent with economic soundness in the broadest sense of that term.

Collective ratemaking, by definition, involves a limitation on motor-carrier price competition and, when carried on under procedures required by statute or prescribed by the Interstate Commerce Commission, is exempt from the antitrust laws.[1] Some critics choose to refer to rate bureaus as "cartels" and to collective ratemaking as "price-fixing" or "collusion" that "would be a felony in most American industries."[2] Colorful as such phrasing may be, it is merely a pejorative and inflammatory expression of the simple, prosaic, straightforward fact that with respect to the pricing of common carriers in surface transportation, including trucking, Congress has authorized a limited departure from usual antitrust policy considerations where collective ratemaking furthers national transportation policy.

Competition has a deservedly high place in the roster of public policies that help to promote the economic interest of the nation. As a matter of common observation and experience, the prod of competition can be, and frequently is, the most reliable means of assuring good economic performance in the public interest. In general, there is a public policy presumption in favor of competition. But there is no iron law of public policy that competition must, without exception, play exactly the same role and take exactly the same form in every type of economic activity in the country. In special situations, where Congress recognizes that rigid application of antitrust strictures would defeat rather than promote the public interest, it modifies the basic policy of competition and implements that modification by means of an antitrust exemption. No opprobrium attaches to the resulting moderation of competition. The exemption is merely a formal recognition by Congress that unusual circumstances are involved.

A congressional decision regarding an antitrust exemption always reflects a choice between alternative impacts on the public interest. When Congress confers antitrust immunity upon farmers to permit them to price

1. Interstate Commerce Act, § 5a (Reed Bulwinkle Act), 49 U.S.C. § 5b (1976).

2. *Hearing before the United States Senate Judiciary Comm., Subcomm. on Antitrust and Monopoly*, 95th Cong., 1st Sess. (1978) (Testimony of Assistant Atty. Gen. John Shenefield).

and market their crops or livestock collectively,[3] it is making a public policy decision that in this area of the economy collective selling of output can be more beneficial to the public interest as a whole than unrestrained competition or, stated in reverse, that unrestrained competition would be more harmful to the public interest than collective pricing would be. In the case of motor freight transport, the policy of Congress for the past thirty years has been that the public interest as a whole is better served by permitting carriers a carefully controlled freedom to price their services collectively than by insisting on conventional price competition.

Good public policy requires that whenever an area of economic activity is freed from the operation of the antitrust laws, the procedures under which prices are established and the prices themselves should be subject to stringent public control to make sure that the interests of affected groups in the economy are properly protected. The controls exercised over Interstate Commerce Act rate bureaus meet this requirement. These controls are unquestionably far more strict than the controls applied to other areas of antitrust exemption.

For example, ocean shipping rate conferences enjoying antitrust immunity are permitted to operate under agreements that contain dual-rate provisions designed to penalize shippers who patronize non-conference carriers, and conference members have no right of independent pricing action.[4] Insurance companies subject to state regulation are exempt from antitrust no matter how weak or inadequate that regulation may be.[5] The prices charged by antitrust-exempt agricultural marketing associations apply not only to the products of their own members but to those of nonmembers which they may handle in substantial volume, and those prices, as well as the procedures under which those associations operate, are for all practical purposes completely unregulated.[6]

The situation is quite different with respect to motor carrier rate bureaus. Every provision of every agreement under which a rate bureau operates must be approved by the Interstate Commerce Commission[7] standing as the guardian of the public interest, and no agreement may be approved except on a specific finding of the Commission that national transportation policy considerations justify an exemption from the antitrust laws.[8] Each carrier belonging to a rate bureau is assured the "free and

3. *See* Clayton Act, § 6, 15 U.S.C. § 17 (1976); Capper-Volstead Act, 7 U.S.C. §§ 451-457 (1976).

4. *See* Shipping Act of 1916, 46 U.S.C. §§ 813a, 814, 815, 817, 819, 841a (1970).

5. McCarran-Ferguson Act, 15 U.S.C. §§ 1012-1013 (1976).

6. Capper-Volstead Act, 7 U.S.C. §§ 451-457 (1976).

7. 49 U.S.C. § 5b(2)-(7), (10) (1976).

8. *Id.* § 5b(2), (9).

unrestrained right''[9] to act independently with respect to any rate at any time without sacrificing the eligibility to remain a bureau member and act on other rates. Regardless of size, all members have an equal vote. Shippers are free, without suffering any economic penalty, to give any portion of their traffic at any time to carriers that are not members of the rate bureau. Rates established through a rate bureau govern only the traffic of its members. All rate actions of a rate bureau are subject to the closest regulatory review:

> (1) Changes in the general rate level or rate structure must meet regulatory standards of reasonableness and must be supported by extensive data specified by the Commission.[10]
>
> (2) The relationships of rates to each other must meet stiff legal tests concerning discrimination and preference and prejudice affecting shippers, industries, communities, points, or any particular description of traffic, and these tests are the same for rates established by a rate bureau as for rates established by an individual carrier (whether or not a bureau member) acting alone.[11]
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> (3) The Commission is authorized to suspend or investigate any rate proposal.[12]
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> (4) Every shipper or other interested party, individually or through an organization, has the right to file with the Commission an official complaint challenging any rate bureau action as unjust or unreasonable or otherwise unlawful.[13]
>
> (5) Any complainant dissatisfied with a Commission ruling may appeal to the courts.[14]

Compare this thorough system and degree of regulatory control with the kind of control which exists concerning prices established by agricultural marketing associations, which sell collectively on behalf of agricultural producers about $40 billion of farm products annually.[15] Under the Capper-Volstead Act of 1922,[16] which exempts agricultural marketing associations from antitrust, an association is not limited to handling the products of its own members; up to half of its business volume may consist of the products of nonmember producers. A Capper-Volstead marketing association, by itself or by agreement with another such association, may control up to 100 % of the market for any farm product it handles. No association is required to notify a government agency of its prices, and no agency has

9. *Id.* § 5b(6).
10. *Id.* § 316(a), (g).
11. *Id.* § 316(d).
12. *Id.* § 316(g).
13. *Id.* § 316(e).
14. *Id.* § 316(j).
15. U.S. DEPARTMENT OF AGRICULTURE, STATISTICS OF FARMER COOPERATIVES (1977).
16. 7 U.S.C. §§ 451-457 (1976).

authority to act in advance to prevent such prices from going into effect. In some associations, voting power is not the same for each member but is in proportion to the amount of capital stock or membership capital owned. The Secretary of Agriculture is empowered to institute proceedings at any time to determine whether the practices of any marketing association have unduly enhanced prices and to issue a cease and desist order, enforceable in the courts, to restrain the offending practices. No other government agency is authorized to proceed against a marketing association on account of unduly high prices. No private party has a right to bring such a suit. Only the Secretary of Agriculture has the power to act against unduly enhanced prices, but in the 56 years since the antitrust exemption and the accompanying investigatory and enforcement power have been on the statute books no proceeding has ever been held.

## II. Rate Bureaus and Carrier Competition

Although collective ratemaking operates to limit price competition among motor freight carriers, competition is far from eliminated. The competition that remains is substantial and vigorous, and takes a variety of forms.

There is first the basic right, reserved by law, for every carrier belonging to a rate bureau to act independently of any bureau action concerning rates or other tariff matters.[17] While restrictions upon price competition are inherent in the very nature of collective ratemaking, it is a mistake to downplay, as some critics are wont to do, the moderating influence of independent action, both actual and potential, upon those restrictions.

Membership in a rate bureau is optional on the part of carriers serving the bureau territory, but every carrier becoming a member has this statutory right of independent action. As a result, no carrier may be bound against its will. The right of independent action is an unqualified one; it may be exercised by a carrier's declining to go along with a rate change concurred in by others or by establishing a rate change unilaterally, and it may be taken before, during, or after any rate-bureau decision. Congress, in providing for antitrust exemption for collective ratemaking in 1948, recognized the crucial importance of assuring such a right of independent action, and made it an absolute condition of any approval of a rate bureau agreement by the Interstate Commerce Commission.[18] The railroad rate bureau agreements struck down by the Supreme Court fifty years earlier as violative of the Sherman Act contained no such unequivocal right of independ-

17. 49 U.S.C. § 5b(6) (1976).
18. *Id.*

ent action.[19]

The Commission has placed tight safeguards around the right of independent action and it represents an important source of competitive pressure upon rates. Both large and small carriers have invoked the right of independent action when their interests, or the interests of shippers they serve, have required it. Most of the independent actions taken by carriers involve rate reductions.

The role of the right of independent action in the collective ratemaking system is an interesting one. The right itself is an important part of the statutory and regulatory design for antitrust exemption, and the timely and judicious employment of that right is an essential means of safeguarding the public interest in motor carrier rates by making sure that no carrier may be committed, merely by the operation of majority rule, to any rate to which he objects, either on his own behalf or on behalf of a shipper he serves. At the same time, it is evident that if invoked indiscriminately so that, contrary to congressional intention, independent actions became more the rule than the exception the public purposes served by collective ratemaking would be undermined.

There is no way of judging the effectiveness of collective ratemaking or of the right of independent action from the numbers of such actions alone. The numbers themselves depend upon the technical definition of independent action. More importantly, the competitive significance of the right of carriers to establish rates independently cannot be measured simply by the independent actions officially taken. Students of antitrust are familiar with the role that potential, as well as actual, competition can play in affecting business behavior, and the impact of potential competition is seen in the processes of motor carrier ratemaking as in other fields of the economy. Even when not actually pressed to the point of formal unilateral rate publication, the power of any carrier to price independently can and frequently does exert a decisive competitive influence on the rate actions of other bureau members.

From time to time one hears it alleged that the competitive significance of independent action is of little consequence because it may be assumed that the more powerful members of a rate bureau will succeed in coercing the less powerful. Evidence of such coercion is lacking and there is no reason to give any weight to that assumption without some substantiation of its validity. Interference with the "free and unrestrained right of independent action" would, of course, be clearly unlawful.

Aside from the actual and potential competitive pressures arising from the right of independent pricing action, competition among bureau mem-

19. United States v. Trans-Missouri Freight Association, 166 U.S. 290 (1897); United States v. Joint-Traffic Assn., 171 U.S. 505 (1898).

bers for traffic on the basis of the quality of the service provided is marked by the same kind of intensive struggle for business as occurs in many other industries on the basis of product or service quality. It is unrealistic to regard competition in factors other than price as a substitute for price competiton, but it is equally unrealistic from a public-interest standpoint to ignore the competitive importance of rivaling for the favor of shippers by means of modern equipment, expeditiousness and reliability of service, adaptation of service to specific transportation needs, and similar factors which can be of crucial importance to shippers. And nothing in the collective ratemaking process interferes with the vigor of these forms of competition.

On any given traffic lane, competition among carriers within a bureau embraces both the services offered by carriers with single-line authority on that lane and the multiplicity of interline services available via joint routings of two or more carriers operating through various points of traffic interchange. Less direct but nonetheless important competition among bureau members occurs between carriers hauling a commodity between one pair of points and carriers of the same commodity to or from a competing point.

Competitive pressures from motor carriers outside the rate bureau membership also affect the level of rates and the struggle for traffic. Such pressures come from the large numbers of carriers in each territory that are not members of any of the major rate bureaus—common carriers that choose to belong to other bureaus or to no bureau at all, contract carriers dedicated to the traffic of one or more shippers under negotiated rates, and, pervasively, shipper-owned private carriers operating truck fleets of varying sizes and, by means of both actual and potential competition, continually exerting a strong downward force on common carrier rates. United Parcel Service, freight forwarders, air cargo, and of course rail transport, including piggyback service, are also, in varying degrees, competitively significant.

On the heavy-traffic lane between Boston and New York, there are 92 member carriers of the New England Motor Rate Bureau offering single-line service. These carriers also provide Boston-New York service in combination with other member carriers via various interchange points, including Providence, Springfield, New Haven, and Hartford. Via Providence alone, for example, all 92 carriers offer joint-line service between Boston and New York in combination with 55 other carriers.

Between Boston and Richmond, there are at least 15 member carriers of the Middle Atlantic Conference operating single-line service. In addition there are 30 joint-line combinations of member carriers operating between these cities via Baltimore, 16 such joint-line combinations via New York, and 10 such joint-line combinations via Philadelphia. Other interchange points include Albany, Hagerstown, Harrisburg, Hartford, New Haven, Prov-

idence, Roanoke, Washington, and Wilmington, and there are still other joint-line routes. Some joint-line routes involve more than two carriers. There are also at least 6 nonmember common carriers, 4 contract carriers, 4 freight forwarders, and UPS actively competing for traffic on the Boston-Richmond route.

Between Philadelphia and New York, a relatively short haul, there are 117 Middle Atlantic Conference members competing for traffic with single-line service. In addition, there are about 20 nonmember common carriers, 11 contract carriers, 4 freight forwarders maintaining class rates, and UPS.

Elsewhere in the country, the pattern is much the same. Between Chicago and Omaha, for example, 25 member carriers of Middlewest Motor Freight Bureau compete for traffic alongside at least 30 nonmember common carriers, 8 contract carriers, 2 major freight forwarders, and UPS, to say nothing of 5 major railroads.

On these routes as on innumerable others, the competition from private carriers is ever-present and extensive. The Census of Transportation for 1972, the latest year for which such data are available, shows, for example, that there were 30 major categories of manufactured goods in which private motor carriers hauled one-fourth or more of the freight tonnage moving by all forms of transportation. In these categories, the share of the total motor carrier traffic tonnage hauled by private fleets ranged from 28% to 78%.

## III. Justification for Collective Ratemaking

Special factors make collective ratemaking in trucking indispensable to the public well-being. They all are rooted in considerations of a practical nature. Where there are thousands of carriers providing service, thousands of commodities being moved, tens of thousands of geographic points to be served, millions or more of point-to-point combinations, countless carrier interline routes and connections, a staggering number of individual rates, and awesome complications of competing origins, destinations, and products, practical considerations in ratemaking can not be either wished away or lightly dismissed as matters of mere convenience which can be overcome with a little technological ingenuity. These considerations are:

(1) There is no other practical way by which the level of motor carrier rates and the relationship of rates to each other can be effectively regulated as the public interest demands.

(2) There is no other practical way to prevent, or at least minimize, the damaging effects upon the economy of serious discrimination in the prices paid for motor carrier service by large and small shippers who are in competition with each other.

(3) There is no other practical way to preserve a well-coordinated network of motor carrier service required for efficient and expeditious distribution of the vast variety of goods which move to and from every corner of the economy by truck.

(4) There is no other practical way to assure the degree of rate stability and certainty producers and distributors must have in order to plan current and projected production and marketing operations efficiently.

(5) There is no other practical way in which the highly desirable involvement of shippers in monitoring and influencing the ratemaking process can be systematically provided.

### A. *Effectiveness of Rate Regulation*

It is assumed here that the continued regulation of rates to protect the public is regarded as desirable. In the absence of collective ratemaking, effective regulation would literally be impossible.

Under existing regulation, rate levels on traffic in each rate-bureau territory are controlled by Commission actions applicable to all of the carriers belonging to that bureau. While the Commission is armed with extensive financial and traffic data of the bureau member carriers, individually as well as on a group basis, its determinations that rate levels are sufficient, but no more than sufficient, to meet reasonable revenue and income needs, are made for the carriers as a whole. This process makes it possible to keep within manageable proportions the task, that would otherwise be necessary, of reviewing mountains of detailed historical and *pro forma* information on the revenues, expenses, profitability, and traffic of thousands of individual motor carriers and determining the reasonableness of rate levels, structures, and relationships on a carrier-by-carrier basis.

If carriers were barred from establishing rates in common and rates were established individually, each carrier would propose its own rates. The Commission would have to determine the revenue and income needs of each carrier separately in order to rule on the reasonableness of its individual rate level. It would also have to rule on the reasonableness of the rate structures and the reasonableness of individual rates in relation to each other for each individual carrier. The enormity of such a regulatory burden and the scale of the regulatory machinery which would be necessary to cope with it at all, much less satisfactorily, defy description. And these towering difficulties would be compounded by gigantic problems of enforcement.

### B. Discrimination, Preference, Prejudice

In a system of individually-established rather than collectively-established rates, flagrant discrimination, preference, and prejudice, with serious impacts upon shippers and localities, would be inevitable, not only because of the breakdown of regulation but because of the inherent nature of a system of individually-established rates.

If regulation of rate levels, rate structures, and rate relationships of carriers on the basis of individual costs and individual revenue and income needs produced significant differences in rates among carriers, the result would be severe competitive inequities to affected shippers and localities served by different carriers. If it is argued that as a result of competitive pressures such rate differences would be eliminated, a question might well be asked as to what purpose would be served by following a circuitous and disruptive course to rate uniformity already prevailing under collective ratemaking. But there is in fact the strongest likelihood that competitive forces would in many cases produce serious sustained rate disparities, and that discrimination, preference, and prejudice would be rampant.

The most common and most difficult problems of discrimination, preference, and prejudice arise not in terms of disparities in rates charged by the same carrier providing trucking service to two shippers of the same commodity under the same conditions between the same origin and destination points, but in connection with the rates charged by different carriers to competing shippers located at the same or different points of origin or destination or both. Where the same carrier charges different rates to shippers of the same commodity under the same conditions between the same points, the practice is on its face unlawful, and in the absence of a regulatory failure, enforcement could presumably be relied on for a remedy. Where different carriers and the same shipper are involved, the problem is one of competition and is not normally a matter for public concern. The more serious problem, however, arises in connection with a more subtle and vexatious, but potentially decisive, form of rate favoritism. That problem derives from the ability of an economically powerful shipper in one locality to gain from the carrier or carriers serving him rates that are more favorable than those a less powerful rival, located there or elsewhere in the territory but competing for the same markets—or located at the same point but receiving similar raw materials or components from the same or different origins—is able to obtain from a different carrier or carriers on whom he must rely for service.

Rate favoritism of this kind toward giant shippers controlling large volumes of traffic would surely be unavoidable under a system of rates established by individual carriers without collective action. Each carrier in its own traffic market would be responding in accordance with normal com-

mercial principles and motivations, and no single carrier could legitimately be accused of itself engaging in discrimination. The plain reality of the situation is that it is not a sufficient protection to the public interest in fostering healthy competition either among carriers or in the industries dependent upon motor transportation that any one carrier abstain from rate discrimination. To achieve the parity of rates among competing shippers that good public policy requires it is necessary that the rates charged by carriers as a group be non-discriminatory. That result can be achieved only by collective ratemaking. The vital principle of equitableness of rate relationships achieved by the collective ratemaking system is that, apart from extraordinary circumstances, the rate charged by a member carrier of a rate bureau for moving any class of goods under given conditions between any pair of points is the same as that charged by any other member carrier, not only between that pair of points but, mile for mile, between any other pair of points in the territory—regardless of the size or power of the shipper.

### C. Coordinated Service

Its growth has been made possible by, and requires for its continuation, a highly developed national transportation system. The National Transportation Policy[20] speaks wisely of the national need for a coordinated transportation system. A coordinated network of trucking service is a natural and vital part of such a system. No carrier, no matter how large, has or can have single-line access to and from each and every point in the country requiring trucking service. Total coverage requires the integration of all common carrier services in a nationwide network of single-line and joint-line operations which together make it possible to reach every part of the country from every other part by common carrier service.

Coordination in terms of a national policy designed to promote the public interest as a whole means more than the physical hookup of the carriers. It means establishing a system that permits taking advantage of opportunities for service efficiencies, increases the competitive service alternatives available to shippers, and assures that every region, community, or locality requiring service will receive it at the same rate regardless of the single-carrier or combined-carrier routings by which it is reached.

Traffic patterns and densities and the imperatives of efficient operation can favor the choice of an interline over a single-line route. Interlining can serve the cause of carrier operating efficiency by routing freight over interchange points where loads can be broken down for consolidation with other shipments consigned to the same ultimate destinations. It contributes to shipper efficiency by making available routings that fit in with a desired

20. *See* Act of Sept. 18, 1940, ch. 722, § 1, 54 Stat. 899 (codified at 49 U.S.C. preceding § 1 (1976)).

distribution pattern. It permits carriers lacking single-line authority to join with others to compete with the single-line services of other carriers. And it protects the competitive position of shippers and communities at those points which are reached only by joint-line service by holding down the rate for any particular movement to that which would be charged on a mile-for-mile basis if single-line service were available; in the absence of such a "through" rate, a substantially higher charge, representing the combination of applicable local rates, would be incurred.

The collective ratemaking system makes it possible to maintain a complete interlock of interline arrangements among all the carriers serving the territory, with the same rate applicable over all joint routes regardless of the innumerable combinations and permutations of interchange points and participating carriers involved, with all through rates equalized with the applicable single-line rates, and with a uniform basis of divisions of the through rates among the interlining carriers. Such total interlacing of trucking service across the nation is inconceivable without the machinery of collective rate action by all the carriers concerned and the antitrust immunity which makes it possible. It is not simply a matter of one carrier entering into a joint rate and service arrangement with a non-competing connecting line, raising limited if any questions of antitrust. What is involved is a total pattern of service interconnections among all the carriers in a territory, including carriers in direct competition with each other, and the establishment of a vast profusion of joint carrier routings competitive with each other and with the single-line carriers participating in the joint routings. And what is also involved is an equalization of rates via all such services for a given movement. Clearly, this could only be accomplished by the process of collective ratemaking.

In the absence of collective ratemaking, the advantages of the present total interline network of motor carrier service joint routes and through rates would be lost or drastically impaired. The scope of the problems and the likely course of events in the absence of collective ratemaking need to be fully appreciated.

There are about 3,500 member carriers of the major rate bureaus. Many individual carriers have joint-line arrangements with literally hundreds of other carriers. One major carrier interlines with more than 1,200 carriers. An interline arrangement ordinarily covers all the points at which the interlining carriers have terminals where freight can be interchanged, and each joint-line arrangement applies to the rates applicable to each of the large number of commodities moving over the multitude of routes concerned. Were rates to be established individually instead of by collective carrier action, the sheer magnitude of the task of negotiating the innumerable complicated terms of the many interline agreements required would deter many

carriers from establishing joint routes and through rates with others, except where advantageous from the standpoint of their own operations.

Interline service is generally more costly than single-line service. Revenue divisions of carriers participating in through rates on interline service are frequently substantially lower than the single-line revenues earned over the same route to or from the point of interchange. Under these circumstances, carriers could be expected to rely to a much greater extent than at present upon their own single-line services in lieu of interline routings. The spread between lower charges in single-line service and higher charges in interline service as a result of combining local rates would inevitably lead to a curtailment of interline service save for those routes where no single-line alternative was available or the maintenance of a joint routing happened to serve the individual interest of the carrier controlling the traffic. Many carriers, especially smaller ones, are highly dependent upon the revenues they derive from sharing in interline traffic. They would be severely damaged by the loss of interline traffic, shippers and communities dependent upon interline service would be saddled with a rate handicap, the efficiency of trucking service as a whole would suffer, and an important aspect of the national policy of a truly coordinated transportation system would be undermined.

### *D. Rate Stability*

In addition to the reasonableness of rate levels, structures, and relationships, shippers must be able to rely upon a fair amount of stability in the transportation charges they pay. Stability of rates is not a substitute for reasonable rates, but there is no doubt that in many commercial activities, including transportation, the purchaser regards the need for a reasonable degree of price stability as inseparable from the need for a reasonable price itself. Under present inflationary conditions costs are continually rising, but there is a marked difference between cost uncertainties resulting from inability to predict the future, an inability shared by all, and cost uncertainties generated by confusion and discrimination. Businessmen do not prize cost stability as a security blanket to insure a "quiet life" in the competitive world but because universally, one of the most disruptive forces in business planning—of plant expansions, distribution programs, marketing strategies—is uncertainty as to costs, including, and sometimes especially, transportation costs, and when that uncertainty extends to the transportation costs paid by competitors the disruption is multiplied.

Collective ratemaking insures a high degree of rate stability for shippers. A system of individually-established rates would be at the opposite pole in this respect in important ways such as lack of ready ascertainability of prevailing charges and tariff conditions under the welter of alternative rates and routes available. The burdens would fall most heavily on small

shippers with limited resources and sophistication for dealing with the intricacies of transport tariffs.

### *E. Shipper Involvement*

One of the most useful aspects of the collective ratemaking system is the opportunity it provides for active involvement of shippers in the discussion and debate of carrier rate proposals before they are acted on, and in the submission of proposals of their own. The rate bureau machinery affords the shipper the unusual means of simultaneously proposing desired rate changes to all of the carriers serving him in a given territory, and of simultaneously responding to rate changes proposed by one or more of the carriers. Whether the rates proposed affect the rates of a shipper or his competitor, each has an opportunity to be heard on equities and impacts of the proposal, to come forth with alternative approaches, or, without waiting for a carrier proposal, to suggest needed changes and improvements in the rates to correct inequities or meet problems created by special market or supply situations. If rates were established by individual carrier actions rather than collectively, a shipper would not only be forced to negotiate with each carrier or combination of carriers separately, but would have no opportunity to air, challenge, and reconcile diverse views of different carriers serving him and his competitors at the same or different points.

The system assures the shipper of a timely and ample opportunity of a hearing; it does not guarantee that he will get what he wants. There is, after all, no more reason to assume that all shipper proposals are meritorious than that all carrier proposals merit approval. No sensible system could be based on either one assumption or the other. Under the collective ratemaking system, the important safety feature is that a federal regulatory body, not an organization of carriers, has the last word as to the reasonableness of carrier rates that are charged.

Given the enormous administrative apparatus inherent in the establishment of rates however accomplished, the collective ratemaking system—with its strong emphasis upon shipper participation in discussions with carriers and upon the opportunity for hammering out differences before formal rate proposals are placed before the Commission—has the distinct advantage of tending to minimize protests and the concomitant burdens of litigation. The right to protest formal rate actions filed with the Commission is not affected but there is a chance for objections that might otherwise result in protests to be ironed out in advance. In the case of general rate increases or major rate restructurings by weight brackets, actions which have a broad effect upon shippers generally, protests by shipper organizations and suspensions and investigations by the Commission in the exercise of it its powers are an indication not that the collective ratemaking system is

not working but that the results of collective action are being subjected to the close regulatory scrutiny which good public policy contemplates.

## IV. Prices and Profits

Collective ratemaking produces important public benefits and the various forms of competition for traffic exert a restraining influence upon the prices charged the public for motor carrier service. But the ultimate protection of the public interest lies in the all-embracing array of powers with which Congress has equipped the Interstate Commerce Commission for the purpose of regulating rates. Armed with these powers, the Commission is in a position to make certain that the level of rates established by collective pricing is no higher than economically necessary to provide good service, that rate structures are reasonably related to costs, that individual rates are equitably related to each other, and that industry profits are not excessive.

So long as rates as a whole are held to levels that are not unreasonably high in relation to the total costs of service, the public's interest in assuring that collective pricing is not producing inordinate returns for the carriers as a whole is protected. It is not essential from a public-interest standpoint that the profitability of each carrier should be identical. Differences among carriers with regard to route structures, traffic composition, operating efficiency, marketing or administrative skill, or managerial effectiveness generally, will inevitably result in differences reflected in the profit and loss statement. Variations in carrier profitability are not a cause for public concern. Where carriers experience different costs, uniform profitability could only be achieved if the rates charged by the various carriers were also different. Such rate differences would be neither competitively viable nor publicly desirable.

It is fallacious to assume, as some commentators seem to do, that cost variations among individual carriers are necessarily attributable to variations in operating efficiency. Carrier differences with respect to such factors as traffic density, length of haul, route congestion, size and handling characteristics of shipments, and quality of service can produce differences in unit cost having nothing to do with efficiency as such. Nor are such cost differences necessarily correlated with profitability. Some of the most profitable—and reputedly most efficient—carriers have relatively high unit costs that merely reflect their manner of operations.

Another fallacy which has received wide currency is that the effect of general uniformity of rate levels established under collective ratemaking is to protect inefficient carriers and stultify incentives for improving efficiency. It is true that under collective ratemaking the general uniformity of rate levels established are geared to the weighted average costs of handling the

traffic in the ratemaking territory so as to produce a degree of profit which is reasonable for the carriers as a whole. But this is a far cry from gearing rates to the costs of the least efficient carriers. As noted, profitability will vary under the uniform rate levels established. But the system reinforces rather than undermines incentives for efficiency improvement. Carriers whose costs are high because of inefficiency will suffer low profits, or losses; carriers whose costs are held down by efficient operation will be rewarded with higher profits. And every carrier, regardless of its relative efficiency at present, will be motivated to operate with increased efficiency in the future in order to maximize its profits.

Aside from rate levels as a whole, it is essential to establish a structure of rates applicable to major shipment-weight categories. The collective ratemaking process seeks to establish rates for the various weight categories in relation to relevant costs, with rates scaling downward as shipment weight increases. The costing techniques used are those either established or approved by the Commission. Cost allocation is far from scientific, and it is not surprising that efforts to structure rates by weight categories in relation to costs should be disputed by shipper groups facing increased rates. Such disputes are for the Commission to decide on the basis of the best evidence which can be applied. But the basic effort to structure rates in relation to costs for different shipment-weight categories must be regarded as economically sound and equitable.

Carrier profitability is frequently measured in terms of return on investment. The return on the capital dedicated to a transportation enterprise is a significant, though not the only, indication of whether or not a reasonable profit is being earned. It is capital that is at risk in a business and the relation of profit to that capital must be adequate to preserve the capital from impairment, reward investors, and induce new investment in modernization and expansion to enable the carrier to serve the public well.

To the extent that rate of return is used as a measure of adequacy of earnings and thus of revenues, however, it is essential to calculate the return in a way that makes proper allowance for the impact of sustained inflation upon the economic cost of supplying transportation service. And it becomes absolutely mandatory to do so before any valid comparisons can be made between the profitability of one carrier with that of another or between the profitability of motor carriers as a group with that of other industries or of industry generally.

There is perhaps no more fundamental proposition in modern economics than that the economic cost of any resource, including capital, consumed in producing a product or service is the "opportunity cost" of the resource. That is economists' shorthand for the basic concept that a company's real cost of capital, for example, is the return that could be earned on that capital in some other use. In order to express return on investment

in sound economic terms, it is fundamental that asset values included in the investment base must be expressed in terms of current replacement cost, not in terms of historic cost as reported in conventional financial statements. In economic terms, the capital invested in an enterprise must be valued not by the original acquisition cost of the physical assets of the firm but by the cost of re-creating the equivalent productive capability of those assets at today's market prices. Similarly, the allowance for depreciation, which reflects the consumption of the capital tied up in fixed assets, must be based upon their current replacement cost rather than their historic or original cost. The necessity to view return on investment in these economic terms has become imperative because of the heavy inflation which the economy has undergone and which has introduced such distortions in asset valuations and in depreciation allowances based on these valuations that conventional accounting measures both of profit and of investment are out of touch with reality.

As the Department of Transportation said in a recent filing with the Interstate Commerce Commission: "In an inflationary period, reliance on historical asset cost misrepresents the asset's value, and, indeed, the entire financial posture of the firm, because the historical cost bears little relationship to the actual, current value of that asset."[21]

The growing spread in the economy at large between depreciation based upon current replacement costs and depreciation based on historic costs has become so significant in the eyes of responsible government economists concerned with the validity of basic national economic measures that corporate profits based upon historic-cost depreciation are no longer regarded as valid. The corporate profit figures now used in the official National Income and Product Accounts (NIPA) published by the Department of Commerce have been restated to reflect depreciation allowances based upon current replacement costs. As is well known, the NIPA measures of national economic activity and its various components provide the statistical underpinning for basic national economic policymaking by the Council of Economic Advisers, other executive departments, and the Congress.

Two years ago, the Securities and Exchange Commission determined that the inadequacies of conventional financial statements with regard to data on asset investment and profits of corporations required that such data be supplemented by data based upon current replacement costs. Present SEC rules require corporations to show in regular financial statements filed with it the current replacement costs of fixed assets (and inventories) and the amount of depreciation expense based on such costs "to enable inves-

21. Petition of the Department of Transportation to the Interstate Commerce Commission for Institution of a Rulemaking Proceeding (April 30, 1976).

tors to obtain more relevant information about the current economics of a business enterprise in an inflationary economy than that provided solely on the basis of historical cost."[22]

Attention has been called to the fact that some motor carriers have earned higher rates of return on equity capital than some corporations in other industries. The inference is that the favorable profit rates of these carriers are the result of insulation from price competition under the collective ratemaking system. The data used in making these comparisons are taken, without any adjustment, from financial statements in which both the asset values included in equity capital and the depreciation expense reflected in profits are based upon original or historic costs rather than current replacement costs.

Accounting data are meaningful for accounting purposes. But it can be stated unequivocally that measures of return on equity drawn from conventional financial statements reflecting original or historic costs can not provide a valid basis for comparing the profitability of one enterprise or industry with another or with industry generally. It can be stated unequivocally that no valid inference concerning competition or monopoly power (the economist's term for insulation from competition) can be drawn from profitability comparisons unless such comparisons are based on economic, as opposed to accounting, concepts of profit and investment.

The irrelevance of an accounting measure of return on equity in determining whether an enterprise is excessively profitable or in evaluating questions of competition or monopoly power is well understood and accepted by economists. As Professor Bain stated many years ago: "The unadjusted accounting rate of profit as computed by the usual methods from balance sheets and income statements, is *prima facie* an absolutely unreliable indicator of the presence or absence either of monopoly power or of excess profits. . . ."[23] Or as Professor Machlup later expressed it: "[T]here are several fundamental pitfalls in the idea that the accounting rate of profit can show the degree to which monopoly power is exercised . . . . But we know for certain that . . . unadjusted accounting rates of profit . . . cannot be accepted as a measurement of the degree of monopoly."[24] Similarly, Professors Douglas and Miller have emphasized the "classic distinction between economic costs and accounting costs." "A price which remains low, consistent with a normal return on accounting costs, will result in deteriorating service," they stress, adding that "for efficiency to obtain, prices

22. Securities and Exchange Commission, Accounting Series Release No. 190 (March 23, 1976).

23. Bain, *The Profit Rate as a Measure of Monopoly Power*, J. OF ECON. (Feb. 1941). For a more recent treatment of this subject, see J. Friedman & M. Friedman, *Relative Profitability and Monopoly Power*, CONFERENCE BOARD RECORD (Dec. 1972).

24. F. MACHLUP, THE POLITICAL ECONOMY OF MONOPOLY (1952).

must reflect economic costs."[25]

Numerous studies analyzing the accounting and economic profitability of many different companies and industries have been made, not only for regulatory purposes but also for internal management use. These studies show that the effect of adjusting rates of return to reflect the effects of inflation upon true economic profitability can vary widely not only from one industry to another but also for enterprises within the same industry. Such variations can occur even for the same enterprise at different periods. A recent study of the profit position of the intercity bus industry analyzed for that industry the difference between return on equity capital on the basis of conventional accounting data and the return on equity when adjusted for inflation to reflect current replacement costs of equipment and facilities. That analysis showed that for the year ending June 30, 1977, adjustment for the effect of inflation upon current replacement costs of depreciable property reduced the bus industry's return on equity from 8.1% to 1.3%.[26]

The conviction among economists who have studied these matters that accounting measures of return on investment cannot, without substantial adjustment, be used with any assurance of validity to indicate either that profits are excessive or that competition is inadequate can be illustrated by referring to the financial data of one of the largest motor common carriers, Consolidated Freightways, which last year had motor freight revenues of about $650 million and total corporate revenues of $1.1 billion. The accounting financial statements filed with the SEC show that for the corporation as a whole the return on equity capital was 24.4 %.[27] Data on current replacement costs, filed with SEC under the new regulations can be used to adjust the accounting return on equity for the corporation. (Similar data are not reported for the motor carrier subsidiary alone.) While replacement-cost data involve an unavoidable degree of estimating, the data submitted conform to the SEC guidelines. Using the same approach used in making studies of profitability in other industries to adjust reported profits and investment for the effects of inflation, the corporate-wide return on equity for Consolidated Freightways is reduced from 24.4% to 12.8% after adjustment for the current replacement costs of fixed assets, and to 13.6% if adjustment is made for the replacement costs of inventories as well as of fixed assets. Before any significant comparison could be made between the true profitability of the motor carrier business of Consolidated Freightways with the returns earned by corporations in other industries it would be necessary to make adjustments of the profit and investment data both for

25. G. DOUGLAS & J. MILLER, ECONOMIC REGULATION OF DOMESTIC AIR TRANSPORT: THEORY AND POLICY (1974).

26. J. FRIEDMAN, REVENUE AND INCOME NEEDS OF THE INTERCITY BUS INDUSTRY (1977).

27. Consolidated Freightways, Inc., Annual Report (Form 10K) to Securities and Exchange Commission for fiscal year ended December 31, 1977.

the motor carrier subsidiary and for the corporations with which it is compared.

## V. Economies of Scale

Repeal of the antitrust exemption for collective ratemaking in trucking is sometimes urged by advocates of substantial deregulation of both rates and entry in the motor carrier industry. One of the main premises on which proponents of such deregulation rely is the statement that there are few if any economies of scale in trucking operations. This view is so frequently repeated that it deserves at least passing scrutiny. An examination of the published literature dealing with economies of scale in trucking lends support to a number of observations and opinions:

(1) The analytical problems are intrinsically difficult in the extreme and the analyses themselves are of widely varying depth, perceptiveness, representativeness as to carrier size, number of relevant variables covered, and quality of reasoning. There are wide differences as to a proper definition of economies of scale and as to proper approaches for measuring them.

(2) The conclusions vary also. Some investigators believe that there are significant economies of scale in trucking, some believe that there are not, and some are undecided or have mixed judgments on the matter.

(3) The cost data relied upon are limited to what is available. The quality of the available data is poor for the purpose in hand. Statistical techniques applied range from low to high degress of sophistication. None of the analyses has succeeded in filtering out extraneous factors, nor is there agreement as to what factors are extraneous.

(4) All of the cost information is of an accounting nature. None of the data has been converted into economic costs. As in the case of profitability analysis, only economic costs would be valid in reaching conclusions as to relative economic efficiencies.

(5) No allowance has been made for the influence of quality of service on cost.

Noteworthy in this connection is the significant comment contained in a recent report of the Council of Wage and Price Stability dealing with carrier purchases of operating authority. Practically every such purchase increases the size or scope of the acquiring carrier's operations. The Council expresses the opinion that a purchase of operating authority "is in almost all cases likely to increase the efficiency of trucking."[28]

28. Council on Wage and Price Stability, The Value of Motor Carrier Operating Authorities (1977).

## VI. Conclusion

How is the public interest, as reflected in the National Transportation Policy, affected by collective ratemaking in trucking? The brief answer is that the public gains advantages that are obtainable only through collective carrier action and, while foregoing some of the possible benefits of rate competition among carriers, avoids the damage and inequities that unrestricted competition would bring.

In the absence of collective ratemaking, the regulatory process, which affords the ultimate protection to the public interest, could not function effectively. It would be impossible to control rate levels, prevent excessive profits, assure reasonable and equitable rate structures and relationships, or forestall flagrant discrimination, preference, and prejudice. The present system, by contrast, makes it possible to achieve these goals while subjecting all collectively made carrier actions to the closest scrutiny of the Interstate Commerce Commission for its approval or disapproval.

The present system is not perfect, neither is any other human institution. As has been said in another connection, some dissatisfaction with a system of this kind would be inevitable even if the process were presided over by the Archangel Gabriel himself. Whatever may be regarded as the drawbacks of the present system, the best justification for its continuation is the widespread economic disruption which its discontinuation could cause. From the standpoint of the public interest, which must be the paramount consideration, the system is better than any alternative which has thus far been suggested.