REPORT ON THE REGULATORY REFORM
PROVISIONS OF THE
RAILROAD REVITALIZATION AND REGULATORY REFORM ACT OF 1976

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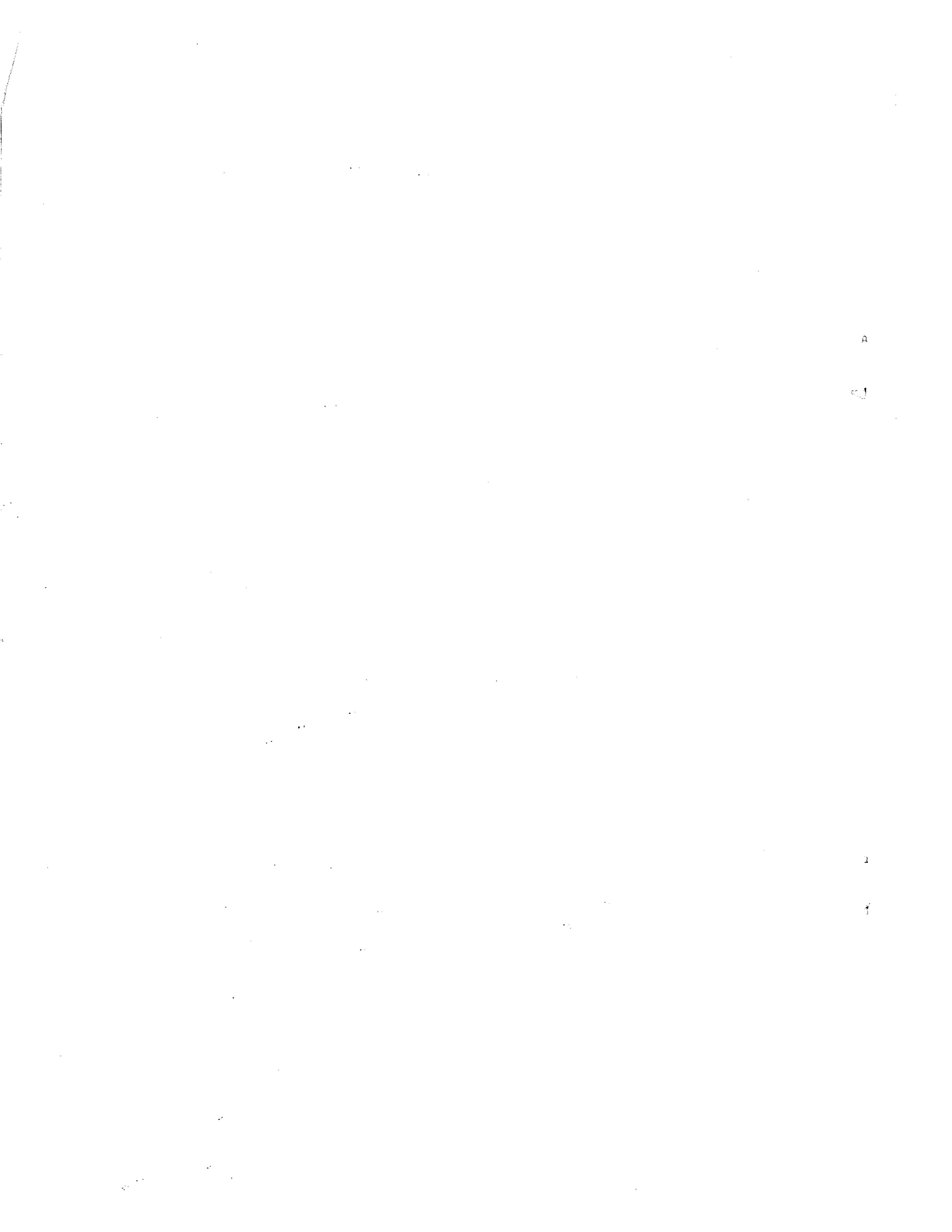

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Table of Contents

	Page
I. INTRODUCTION	1
II. A BRIEF DESCRIPTION OF THE 4R ACT REGULATORY CHANGES	
A. RATE-RELATED CHANGES	4
1. Maximum and Minimum Rate Regulation	4
2. Rate Bureaus	5
3. Demand-Sensitive Rates	5
4. Distinct Service Pricing	7
5. Capital Incentive Rates	7
6. Recyclables	8
7. Intrastate Rates	8
8. Revenue Divisions	8
9. Adequate Railroad Revenue Levels	9
10. Accounting and Costing	9
11. Tariffs	10
B. OTHER REGULATORY CHANGES	11
1. Abandonments	11
2. Mergers	12
3. Demurrage and Per Diem	13
4. Exemptions	14
III. ANALYSIS OF THE 4R ACT REGULATORY REFORMS AND THEIR EFFECTS	
A. RATE-RELATED REFORMS	15
1. Maximum Rate Regulation	15
a. Experience under the Market Dominance Provision	15
b. Legislative History	17
c. The ICC Regulations	19
d. The Court Challenge	22
2. Minimum Rate Regulation	28
3. The No-Suspend Zone	30
4. Procedural Changes in ICC Rate Regulation	32
5. Rate Bureaus	34
6. Demand-Sensitive Rates	39
7. Distinct Service Pricing	43
8. Capital Incentive Rates	48
a. The Statute	48
b. The Regulations	49

	Page
c. The Cases	51
d. Conclusion	56
9. Recyclables	57
10. Intrastate Rates	60
11. Revenue Divisions	64
12. Adequate Railroad Revenue Levels	67
a. Revenue Need Assessment	67
b. Umbrella Ratemaking	72
13. Accounting and Costing	74
a. Accounting	74
b. Costing	77
14. Tariffs	81
B. NON-RATE-RELATED ISSUES	85
1. Abandonments	85
2. Mergers	93
3. Per Diem	102
4. Demurrage	107
5. Exemptions	111
Footnotes	i-v

REPORT ON THE REGULATORY REFORMS
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I. INTRODUCTION

This report is in response to a request from the General Counsel of the Senate Commerce Committee for a list of the regulatory reform provisions of the Railroad Revitalization and Regulatory Reform Act of 1976 (4R Act), for a description of how the Interstate Commerce Commission (ICC or Commission) has implemented its responsibilities under those provisions, and, generally, for a discussion of the impact and efficacy of the 4R Act reforms.

The 4R Act made changes in virtually all of the ICC's regulatory responsibilities. In the rate-related area, various provisions of the 4R Act addressed: ICC maximum and minimum rate regulation authority; rate bureaus; separate rates for distinct rail services; demand-sensitive ratemaking; capital incentive rates; rates on recyclable materials; intrastate rates; and divisions of revenues from rates jointly made by two or more railroads. In addition to these changes, and, in a sense, governing all of them, is a 4R Act requirement that the ICC determine what revenue levels would be adequate for an efficient, well-managed rail system, and then assist the railroads in achieving those revenues. Finally, in order to implement these changes and the ICC's other regulatory responsibilities as fairly and accurately as possible, Congress

mandated an entirely new cost and revenue accounting and reporting system.

In areas other than rate regulation, the 4R Act mandated changes in ICC abandonment and merger policies and procedures, demurrage and car-hire formulas, and tariff publication requirements. A new provision was added also requiring the Commission to exempt certain persons or transactions from any or all ICC regulations if such exemptions were found appropriate.

Section II of this report describes in some detail the statutory changes themselves. Section III describes the manner in which those changes were actually carried out by the ICC, the results of the changes, and the general impact of the 4R Act.

Three important conclusions should be noted at the outset: first, the 4R Act did not contain numerous sweeping changes -- many, in fact, were quite minor and others were vague or inconsistent; second, there has never been a full test of the reforms that were enacted. The caution of the railroad industry in using the new provisions, the time taken by the ICC (and, often, the courts) in promulgating and reviewing standards and procedures, and ICC interpretations of several crucial 4R Act provisions, have effectively precluded such a test. Finally, patchwork reforms like the 4R Act superimposed on an entrenched regulatory system are not likely to succeed.

Time after time, statutory changes thought to be simple become ensnared in regulatory webs or protracted courtroom litigation. In the discussion below we attempt to show both how the ICC thwarted some reforms as well as the ways in which the reforms themselves were either too limited or too ambiguous.

II. A BRIEF DESCRIPTION OF THE 4R ACT REGULATORY CHANGES

A. Rate-Related Changes

1. Maximum and Minimum Rate Regulation

Section 202 of the 4R Act amended section 1(5) and section 15 of the Interstate Commerce Act (IC Act). Revisions of section 1(5) provided for the establishment of new standards and procedures for determining whether rates charged by railroads are just and reasonable and removed the Commission's authority to determine whether proposed rates are too high on traffic for which effective competition exists. This provision was intended to remove ICC maximum rate regulation authority in situations in which railroads faced effective competition, but retain it in situations of rail "market dominance." The ICC was required to develop regulations to be used in determining whether a railroad had market dominance with respect to any particular traffic or movement.

Section 202 also limited the Commission's power to find a proposed rate to be too low. Changes in section 1(5), for example, provide that a proposed rate that contributes to the "going concern value" of the proposing carrier cannot be found unjustly or unreasonably low. A rate that equals or exceeds the carrier's variable cost of providing the service to which the rate applies is presumed by the statute to contribute to the carrier's going concern value.[1/]

The revisions to section 15 also prescribed time limits for Commission investigations of proposed rates and modified the Commission's power to suspend rates. A reallocation of the burden of proof in suspension cases was specifically mandated, as well.

The most major change in the ICC's suspension power was the creation of an experimental "no-suspend" zone that allowed a railroad to increase or decrease a rate within specified limits (7% a year) without fear of its being suspended on the ground that it is too high or too low. Specifically, the provision prohibited the ICC from suspending a rate within the zone (although it could be investigated and subsequently declared unlawful), unless: (1) the rate would violate the anti-discrimination provisions of the IC Act; (2) the railroad had market dominance over the affected service; (3) the rate was predatory; or (4) the rate was part of a general or broad territorial rate increase.

The no-suspend provision expired in February 1978, was re-enacted in October 1978, and now remains in effect until July 1980. Both no-suspend provisions were self-enforcing -- that is, no ICC implementing regulations were required or developed.

2. Rate Bureaus

The 4R Act, in amending section 5 of the IC Act, changed the operations of railroad rate bureaus. Section 208 of the 4R Act prohibited railroads from agreeing to or voting on single-line rates (although discussion of such rates was permitted). Section 208 further specified that only those railroads that could "practicably participate" (as defined by the ICC) in an interline movement (one requiring two or more railroads) could agree to or vote on the rate associated with that movement. General or broad territorial rate increases were exempted from these limitations. The right of any one carrier to take independent action was guaranteed, and the ICC's power to grant antitrust immunity to rate bureaus was continued.

Approval of any rate bureau agreement was conditioned on the ICC first finding that the agreement would be "in furtherance of the national transportation policy."

3. Demand-Sensitive Rates

Section 202 revisions also required the Commission to promulgate standards and expeditious procedures for the establishment of seasonal, regional, and peak-period rates (sometimes called "demand-sensitive" rates). The statute directed the ICC to develop procedures that would: "(a) provide sufficient incentive to shippers to reduce peak-period shipments...(b)

generate additional revenues for the railroads; and (c) improve (i) the utilization of the national supply of freight cars, (ii) the movement of goods by rail, (iii) levels of employment by railroads, and (iv) the financial stability of markets served by railroads."

4. Distinct Service Pricing

Section 202(d) of the 4R Act called for the ICC to assist the railroads in developing separate prices for distinct rail services. This provision was intended to "encourage competition...promote increased reinvestment by railroads, and...encourage...increased non-railroad investment..." This was to be accomplished by encouraging the railroads to disaggregate or unbundle tariffs covering a wide variety of services, not all of which were needed or wanted by every shipper, and price each service separately. This would help to tailor rates and services to individual shipper needs.

The Commission was required by section 202(d) to develop rules that would "encourage the pricing of...services in accordance with the carrier's cash-outlays for such services and the demand therefor, and (b) enable shippers...to evaluate all transportation and related charges and alternatives."

5. Capital Incentive Rates

Section 15(19) of the Interstate Commerce Act was added by section 206 of the 4R Act, and provided for establishment

of "capital incentive rates." A capital incentive rate is based on an investment by a shipper, railroad, or interested third party of $1 million or more in rail-related equipment or facilities. Once the rate is approved by the Commission it cannot be found unlawful for a period of five years (except that it can be raised to cover the railroad's variable costs).

6. Recyclables

Section 204 of the 4R Act required the Commission to investigate the rail rate structure for recyclables and competing natural resource materials, and to consider especially the effect of general rate increases on that structure.

7. Intrastate Rates

Section 210 of the 4R Act changed the law with respect to ICC authority over intrastate rates. This section vests jurisdiction over intrastate rates with the ICC if a railroad files a proposed intrastate rate change with the appropriate state regulatory body, and that body fails to act within 120 days. Section 210 also contained a clause specifically preempting inconsistent state laws.

8. Revenue Divisions

When two or more railroads participate in a particular movement, the railroads often offer a single "joint" rate to the shipper. The railroads may either decide among themselves, or ask the Commission to decide, how the revenues generated

under that joint rate should be divided. The so-called "divisions cases" that arise when railroads cannot agree are some of the longest, and most acrimonious, heard by the Commission.

Section 201 of the 4R Act attempted to improve these proceedings by requiring the Commission to establish standards and procedures "for the conduct of proceedings for the adjustment of divisions of joint rates or fares [whether prescribed by the Commission or otherwise]..."

9. Adequate Railroad Revenue Levels

Section 205 of the 4R Act contained a new "rule of rate-making" for railroads, directing the Commission to develop standards and procedures to assess the level of rail revenue needs adequate to cover rail operating expenses, generate a fair rate of return, cover the effects of inflation, and attract private capital investment. Section 205 directed the ICC to make "an adequate and continuing effort to assist [the railroads] in attaining such revenue levels."

This section of the statute also prohibited the Commission from keeping a railroad rate high in order to protect another carrier or another transportation mode. (Similar statutory prohibitions had been enacted twice before.)

10. Accounting and Costing

Section 307 of the 4R Act required the Commission to develop a new uniform system of accounts and a new regulatory costing methodolgy for railroads. The new system was to

be designed to "assure that the most accurate cost and revenue data can be obtained with respect to light density lines, mainline operations, factors relevant in establishing fair and reasonable rates, and other regulatory areas of responsibility." The statute further required that the new uniform system of accounts (USOA) be: (1) in accordance with generally accepted accounting principles; and (2) "cost effective, nonduplicative, and compatible with the present and desired managerial and responsibility accounting requirements of the carriers." No specific requirements were given for the new costing system.

The new costing and accounting systems were to be announced by June 30, 1977, and to become effective on January 1, 1978.

11. Tariffs

Section 203 of the 4R Act made two changes affecting rail tariffs. First, the statute required that in considering whether to permit a railroad to cancel a through route or joint rate, the ICC must compare the old and new routings in terms of differing distance, transportation time and expense, energy consumption, and impact on affected shippers and carriers.

Second, section 203 required the ICC, in considering any proposed rail rate increase or decrease, to consider whether the new rate would "change the rate relationships between commodities, ports, points, regions, territories,

or other particular descriptions of traffic...and [whether] such increase or decrease would have a significantly adverse effect on the competitive position of shippers or consignees served..." If it is shown that a proposed rate change would affect any of these relationships, the Commission is required to investigate the lawfulness of the proposed rate.

B. Other Regulatory Changes

1. Abandonments

Sections 303, 802, and 809 of the 4R Act require the ICC to speed up its abandonment procedures, develop guidelines for a subsidy program for lines subject to abandonment, and develop definitions and rules governing abandonment cases generally. Each railroad was required to prepare and submit to the Commission a map of its system showing proposed abandonments as well as each line that is "potentially subject to abandonment" as that term was to be defined by the Commission. The Commission was prohibited from approving any abandonment protested by a "significant user" of the line unless the line was identified on the map at least four months prior to the date of the abandonment application.

If the Commission finds that the "public convenience and necessity" require or permit the requested abandonment, it must then determine whether a "financially responsible person" has offered a subsidy for continuation of the line,

and whether the subsidy would cover the difference "between the revenues which are attributable to such line...and the avoidable cost of providing...service on such line..." All of these terms were to be defined by the Commission, and the statute allowed the Commission to delay issuance of a certificate of abandonment for as long as six months to resolve subsidy issues.

2. Mergers

Title IV of the 4R Act contained new standards to be used by the ICC in deciding merger applications, and put forward new procedural requirements and time limitations for merger proceedings, as well.

Section 402 of the 4R Act modified section 5(2) of the IC Act. Section 402 laid out a precise timetable for all stages of merger proceedings, and required all hearings to be concluded within 24 months of the application. A final ICC decision is required within 180 days thereafter. The substantive standard for judging mergers -- that they be "consistent with the public interest" -- was retained.

Section 403 provided for an expedited merger procedure that would commence with a proposal made to the ICC by the Secretary of Transportation. Special time limits were imposed on ICC actions on such proposals, and the ICC decision was to be based on "the public interest." Inconsistent (competing)

applications covering the same subject matter were precluded from ICC consideration of section 403 proposals.

The ICC was required to develop implementing regulations for both 402 and 403 merger proposals.

3. Demurrage and Per Diem

Demurrage is the term for the amount of money paid by a shipper to a railroad for the hours in which a rail car is in the shipper's possession for loading, unloading, or any other purpose. Typically, 48 hours are permitted without charge. Section 211 of the 4R Act amended section 1(6) of the IC Act by requiring the ICC to re-examine its existing regulations on demurrage to assure that demurrage charges are established "in such a manner as to fulfill the national needs with respect to (a) freight car utilization and distribution, and (b) maintenance of an adequate freight car supply..."

Per diem (or car-hire) is the term used to describe the payment exchanged between railroads when one railroad's car is on another's tracks (for example, in an interline movement). Section 212 of the 4R Act permitted (but did not require) the ICC to establish per diem rules governing the amount of compensation, contractual terms between railroads, and penalties. Compensation was to be fixed "on the basis of the elements of ownership expense involved in owning and maintaining each...type of freight car..." Incentives designed

to encourage optimal car ownership and use were expressly allowed. Section 212 states that Congress' intention in adopting this provision was "to encourge the purchase, acquisition, and efficient utilization of freight cars."

4. Exemptions

Section 207 of the 4R Act required the Commission to exempt certain persons, services, and transactions from any or all of its regulations if it found that continued regulation: (1) was unnecessary because of the limited scope of the affected activities; (2) was not needed to carry out the national transportation policy; (3) would be an undue burden on interstate commerce; and (4) would serve little or no useful public purpose. The exemption could involve any or all ICC regulations, and could last for as long as the Commission found appropriate.

The legislative history of the 4R Act makes clear that the ICC was to look specifically at those commodities that are already exempted from regulation when carried by motor and water carriers.

III. ANALYSIS OF THE 4R ACT REGULATORY REFORMS AND THEIR EFFECTS

A. Rate-Related Reforms

1. Maximum Rate Regulation

a. Experience Under the Market Dominance Provision

The "market dominance" provision of the 4R Act was, in many respects, the Act's most glaring failure. Intended to eliminate ICC regulation over most railroad rates, the vagueness of the market dominance concept and inappropriately restrictive ICC implementing regulations resulted in continued ICC regulation, even where unnecessary or unintended. Although, as discussed below, the legislative history of the 4R Act makes clear Congress' belief that rail market dominance was the exception, not the rule, the ICC's rules implementing the market dominance concept result in a substantial portion of all rail rates remaining subject to ICC maximum rate regulation. Because of the nature of the ICC's market dominance rules, proposed rate increases on traffic that could provide needed revenue are often challenged by protesting shippers or blocked by the threat of a challenge. In those areas where rate adjustments could go furthest to make up revenue shortfalls of the railroads, the rates are still set by the ICC.

According to informal estimates from ICC staff, there have been 88 protests filed under the market dominance provisions of the 4R Act. This count does not include cases where a

rate was protested on several grounds, one of which was market dominance. For example, some of the coal rate cases appear to have been counted only as "rate incentives for capital investment" proceedings, even though the rates were also protested under the market dominance provision. The number also appears to exclude protests arguing that a proposed rate was unlawfully high, but not alleging market dominance. Such protests were rejected on procedural grounds. Most important, it does not count increases not sought by the railroads because of the Commission's rules or because of experience with similar rates already proposed.

Of the 88 reported market dominance cases, 15 were reported to have been both suspended and investigated, and an additional 15 were not suspended but were investigated. Thirteen of the suspended cases were cancelled and the proceedings discontinued. Carriers have argued in general rate increase pleadings that the time, cost, and difficulty of securing an increase on individual rates under current market dominance rules make it more practical to seek rate increases through the general rate increase process.

Further, the very concept of market dominance was so vague, and its implementation problems so complex, that it

did not operate to release any rates from regulation automatically. While the ICC's regulations dramatically lessened the chances of this provision having a significant deregulatory effect, some of the problems are inherent in the concept itself.

b. Legislative History

The legislative history of the 4R Act is especially important with respect to the market dominance provision, and makes clear the Congress' intent to reduce Commission rate regulation and place more reliance on rates set by market forces. In order to increase their revenues, attract capital investment and react to competitive pressures, the railroads must be able to raise or lower their rates in a timely fashion, free from regulation in markets characterized by effective competition. The market dominance provision was intended to be the primary tool for accomplishing these goals since effective competition was assumed to be the norm, not the exception, in most rail markets.[2/]

The Conference Report on the 4R Act repeats a phrase that appears throughout the legislative history of section 202 of the Act, saying that the changes contained in this section "are intended to inaugurate a new era of competitive pricing."[3/] The history makes clear that this new era is to be marked by less reliance on rates set by

Commission regulation and greater reliance on rates set by market forces. Congress recognized that the passage of time had dramatically changed the competitive position of the railroads. The Senate Report speaks to this point quite explicitly:

> Railroads were the first large business to be regulated by the Federal Government. The regulation was called for by the industry's dominance of the market and its ability to price some service monopolistically while engaging in predatory competitive practices in other markets. These problems exist today, but in a very different transportation environment. Railroad regulation therefore warrants reexamination. . . Growth of other modes in the past century has raised questions whether protection against rail monopoly is any longer necessary in many markets. It seems clear that in addition to protecting shippers from the exercise of rail monopoly, the current regulatory system should work to permit railroads to effectively compete for the kind of traffic they can best handle. Competition is particularly important because many of the railroads' competitors are not regulated. 4/

The legislation resulting from these concerns thus had two major premises: that the dominant position of the railroads had been severely eroded; and that in order to gain back some of their lost traffic the railroads needed enough ratemaking flexibility to compete effectively with unregulated carriers. From these conclusions came the mandate in the Act for a substantial diminution of the Commission's ratemaking powers, and for greater railroad freedom to set rates. The Senate report states:

> Railroad regulation has failed to assure adequate industry profits and rates of return and has retarded the industry's ability to compete with competitors ...
>
> If railroads are to regain lost traffic, they must be able to lower their rates, innovate new services, and respond to new and changing circumstances. If railroads are to increase their revenues and attract the resources necessary to revitalize the industry, they must be able to raise their rates in a timely fashion, free from regulation in markets sufficiently competitive to prevent abuses of monopoly power... In placing a premium on the status quo and focusing managements' attention on the intricacies of the complex regulatory schemes, the present regulatory system has sapped the ability of railroads to respond, compete, innovate, and develop their full service capacity.
>
> Less restrictive rate regulation is essential to the achievement of these goals... . (Senate Report at 10, 11).

The same conclusion is reflected in the House Report:

> Underlying the regulatory reform provisions of the entire bill is a conviction that competitive market forces, rather than regulation, should be used to set price and service levels where effective competition exists....[5]

c. The ICC Regulations

Nonetheless, the Commission, in promulgating rules to determine the existence of market dominance, initially proposed seven fact patterns, the existence of any one of which would have established a rebuttable presumption of the presence of market dominance.[6] The ICC failed to propose any fact patterns that would result in a presumption of effective competition. The fact patterns in favor of market dominance included: 1) rates discussed in a rate bureau; 2) traffic not carried

in significant amounts by other carriers for at least a year; 3) traffic carried by other carriers but not subject to price competition; 4) rates set at more than 50% above fully allocated cost; 5) rates set 25% above certain other ICC-approved rates; 6) movements of greater than 1500 miles; and 7) commodities customarily moved in bulk.

Comments on this initial proposal were generally critical. The Department of Transportation (DOT or the Department), the Federal Trade Commission, and the Department of Justice argued that the Commission's proposal failed to fulfill the Congressional mandate because it was premised on assumptions radically different from those on which the 4R Act was based.7/ DOT argued that the Commission assumed that market dominance, rather than effective competition, existed in virtually every market, while the data DOT and others submitted in the proceeding showed the opposite to be the case. DOT's thorough market analysis showed, in fact, that even where railroad rates were well above costs, and the movements involved heavy weights or long distances, the railroads encountered "extensive" intermodal competition. DOT concluded that the Commission's proposed regulations would prove a self-fulfilling prophecy: that is, they would yield erroneous findings of market dominance in most proposed rail rate increases.

The Department of Justice found the ICC's proposals "inconsistent with Congress' intent in adopting

the Act and . . . unsound as a matter of economic policy." Comments of the Department of Justice, at 2. The railroads made similar comments. Shippers commenting on the proposal were generally critical of one or more of the seven fact patterns, although favorable to the idea of presuming market dominance rather than effective competition.

Because of the considerable criticism of its proposed rule and the amount of data submitted showing the existence of effective competition in most transportation markets, the Commission proposed new rules setting forth revised fact patterns. The revised rules still resulted in presumptions in favor of market dominance, and no fact pattern was geared to a finding of effective competition. Proving the existence of any one of the fact patterns would give rise to a rebuttable presumption that the railroad proposing the increase had market dominance over the affected traffic.

Under these rules, market dominance would be found to exist if: (1) the proponent railroad carried more than 70% of the traffic in the relevant market; (2) the proponent railroad would, under the proposed rate, earn more than 180% of its variable cost of providing the service; or (3) affected shippers had made a "substantial investment in rail-related facilities." In connection with the first, or market share, test, the market share of any railroad that had discussed

the proposed rate in a rate bureau was added to the share of the proponent railroad. The rules were, with some modifications, eventually promulgated. The most major modification was to reduce the cost/price ratio presumption to 160% of variable cost. And still, no presumptions in favor of effective competition -- even proof of the reverse of the fact patterns exists -- were established. Thus, for instance, even a showing that the railroads had only a minimal market share of the traffic would not, in and of itself, suffice to show effective competition. And the railroads had to disprove every one of the presumptions running in favor of market dominance.

The revised rules are excessively restrictive and result in inappropriate findings of market dominance. Specifically, the market share test fails to accord full consideration to geographic and product competition, or any consideration to competition from private and exempt carriage. The revised rules also fail to set forth a rational basis for the 160% figure used in the ratio of price-to-cost presumption. Our objections to the third presumption are based on vagueness since it fails to specify the number, amount, or type of investments necessary to invoke the presumption.

d. <u>The Court Challenge</u>

In November, 1976, the railroads, as well as certain utility companies, appealed for review of the Commission's

decision in the United States Court of Appeals for the District of Columbia Circuit. The railroads questioned the Commission's exclusion of certain types of competition in the market share test as well as the absence of a matching presumption of effective competition. They charged that the price-to-cost ratio presumption is arbitrary, unsupported by the record in the administrative proceeding, and frustrates the Congressional desire to allow the railroads to generate additional revenues in competitive markets. Moreover, the railroads argued, the investment presumption is without a rational basis and void for vagueness. The utility companies, in their petition for review, argued that the Commission is required to establish a rule that market dominance exists wherever a rate has been discussed or considered in a rate bureau.

DOT and the Department of Justice agreed that the Commission's final rules failed properly to implement section 202 for the reasons discussed above. Since the United States was automatically named as a statutory defendant in the lawsuits challenging the final market dominance rules, the Department of Justice filed a brief with the Court. In its filing, Justice urged that the Commission's final rule be overturned. The Federal Trade Commission urged the same result based

on similar arguments. With respect to the utilities' review petition, the Department of Justice's brief argued that the Commission was correct in concluding that discussion of a rate by members of a rate bureau was, in and of itself, irrelevant to the issue of whether a railroad had market dominance over given traffic. The National Industrial Traffic League and a group of chemical, grain and other shippers submitted *amicus* briefs supporting the Commission's rules.

The Court acted on May 2, 1978, to uphold the ICC's regulations in a decision based almost entirely on deference to the ICC's presumed expertise.

The Court said:

> Our judicial function must combine restraint with scrutiny. Although [the ICC's] presumption regulations do not have the same protection as a statutory presumption, they are entitled to deference, even on the issues of law involved in statutory interpretation. And that deference is heightened where, as here, the regulations at issue represent the Commission's initial attempt at interpreting and implementing a new regulatory concept. 8/

As to the lack of a presumption in favor of effective competition, the Court held that the statutory language "suggests a legislative focus on procedures for determining the presence of market dominance rather than its absence." *Id* at 16-17. As to the ICC's failure to consider all types of competition in its market share test, the Court found that: "The Commission's reading of the statutory definition of market dominance insures

that the highly complex issues of geographic and product competition will not create delay in the determination of market dominance..." Id at 22. The shipper investment test was also upheld on the basis that the ICC rules sufficiently constrained its application as to make it "rational." Id at 29.

As to the utilities' claim that discussion of a rate in a rate bureau is itself grounds for a finding of market dominance, the Court made a general finding that:

> The statute establishes a new mechanism for reconciling the goal of revitalizing our rail system with the need for continued protection of those who use its services. The rate bureau presumption strikes an appropriate balance between these sometimes conflicting policies, and as such represents a reasonable exercise of the Commission's discretion. Id at 33.

The Court did remand the rules to the Commission for further findings on the cost/price ratio presumption saying only: "We in no way intimate that we think the Commission erred in its approach or result. We only say that we do not sufficiently comprehend its reasoning." Id at 26.

To date, the ICC has taken no action in response to the remand, although it did recently announce that it had let a contract for a study of its market dominance rules generally, and expected to have a report in about a year.

The ICC's rules implementing this crucial 4R Act provision violate the letter and spirit of the 4R Act, and are, more generally, unsound as a matter of economic and

regulatory policy. The ICC's interpretation inhibits the rail ratemaking freedom intended by Congress in two basic ways. First, and most obviouslv, to the extent that traffic facing effective competition is found to be market dominant under the ICC tests, the Commission improperly retains maximum rate regulation over the traffic, and makes rate adjustments on such traffic harder to achieve. More important, the existence of such restrictive market dominance tests is, itself, sufficient to prevent railroads from even proposing many rate adjustments. That is, the expectation that the rate change could be protested and litigated at costly length, and with little hope of eventual success, prevents many rate changes from even being proposed.

Thus, the railroads have not been granted the ratemaking freedom intended by the Congress. To some extent, the statute itself is to blame. It relies on a concept that is difficult to understand and implement in a clear and expeditious way. Further, it was almost inevitable that a test as ambiguous as market dominance would be interpreted by the ICC in a way that retains its regulatory jurisdiction in as many instances as possible. In sum, a clearer test is needed -- one that automatically removes rates from regulation when effective competition exists, or when the increase is reasonable, one

under which the ICC is required in each case to make specific findings of fact on the record that are reviewable in the courts, and one that cannot be administratively abused. That is a difficult task, but it must be accomplished if the railroads are to innovate new services, provide a wide variety of price and service options, meet and beat the competition of unregulated competitors, and remain in the private sector as a healthy, unsubsidized private enterprises.

2. Minimum Rate Regulation

It is particularly difficult to assess the effect of the changes in the ICC's authority over minimum rate regulation since the ICC did not even begin a proceeding to define the relevant terms underlying the 4R Act minimum rate regulation provision until November, 1978. Section 202 of the 4R Act states that no rate that contributes to the "going concern value" of the proponent railroad can be found to be too low. The statute says further that: "A rate which equals or exceeds the variable costs (as determined through formulas prescribed by the Commission)...shall be presumed...to contribute to the going concern value of the carrier..." Today, three years after passage of the 4R Act, the Commission has not yet defined the cost terms used in this provision.

This means that minimum rate regulation is still premised on out-of-date definitions and on an archaic, widely discredited rail costing methodology that the ICC was required (by other sections of the 4R Act), to change three years ago. Thus, no test of the 4R Act provision in this regard has occurred at all. It must, however, be noted that reliance on any costing methodology for minimum rate regulation will be controversial, and in fundamental ways, inappropriate. Any costing method is complex, and relies on necessarily arbitrary cost

estimating procedures. This is discussed in some detail in the accounting and costing section below. Therefore, even if the ICC complies with the 4R Act mandate, minimum rate regulation proceedings will still be lengthy, inexact, and controversial.

3. The No-Suspend Zone

Section 202 of the 4R Act modified the Commission's power to delay the effective date of proposed railroad rates by creating an experimental, two-year, "no-suspend zone" that allowed a railroad to increase or decrease a rate within specified limits (7% per year) without fear of suspension on the grounds that the proposed rate is too high or too low. The rate could, however, be investigated and ultimately declared unlawful. (This provision is sometimes referred to as the "yo-yo" clause.) The provision expired in February 1978, and was re-enacted in October 1978 to remain in effect until July 1980. No ICC implementing regulations were required.

The provision was not used until the summer of 1977. There were several hundred proposals under the provision beginning in August of that year and continuing through February when the provision expired. We have no record of any such proposals at the Commission since the October 1978 legislation extending the life of the no-suspend zone, although there appear to be some working their way through the rate bureaus.

The relative disuse of the no-suspend provision (it must be borne in mind that there are many thousand rate proposals submitted to the ICC each year), cannot be blamed on the

ICC -- it is, rather, the inevitable result of serious flaw in the legislation itself. The legislation ties the no-suspend clause to the question of market dominance. That is, an increase proposed under the no-suspend provision could be suspended, even if it met all of the other statutory criteria for a no-suspend rate, if the proponent railroad had market dominance over the affected service. While this sounds superficially reasonable, it must be borne in mind that the result of this is that if a railroad has market dominance, the rate can be suspended under other provisions of the law, and if the railroad does not have market dominance it need not be bound by 7% limits of the no-suspend clause, since the ICC has no jurisdiction over the rate at all. Therefore, the no-suspend clause provides little or no more freedom than the railroads had already.

4. Procedural Changes in ICC Rate Regulation

Section 202 of the 4R Act made two other changes in ICC rate regulation authority. It further modified the Commission's suspension power by prohibiting suspension of a rate on the grounds of unreasonableness unless a protestant shows by verified complaint that, without suspension, the proposed rate would cause substantial injury to the protestant, and that the protestant is likely to prevail on the merits in any subsequent investigation of the protest.

This change represents a significant shift of the burden of proof in suspension proceedings. The results reached in the cases brought under the maximum rate regulation provision show the effects of this major procedural change. That is, many unsupported challenges to rates were filed, but the challengers could not sustain this burden of proof requirement. Thus, this apparently procedural change did, in many ways, have a more significant substantive impact than did the substantive changes themselves.

Additionally, section 202(e) of the 4R Act places certain time constraints on the Commission when it deems hearings to be necessary in rate cases. Such hearings must be completed

within seven months of the date on which the proposed rate was to become effective, unless the Commission requests and receives from the Congress permission to extend that period by three months. Should the Commission fail to comply with this requirement, the proposal will automatically become effective on its own terms.

The carriers and shippers with whom the Department spoke in preparing this and other reports voiced no concern about the prompt handling of administrative proceedings by the Commission. The Department cannot, of course, estimate what administrative burdens these new procedural requirements have placed on the Commission, but we believe the Commission has carried out this new requirement fully and fairly.

5. <u>Rate Bureaus</u>

Although the rate bureau provision of the 4R Act (contained in section 208) did not, on its surface, seem sweeping, the ICC has interpreted the rate bureau provision in a way that may produce significant change. In fact, the ICC has, for the moment, denied all rate bureau antitrust immunity on the grounds that the railroads failed to justify adequately the need for such immunity. The ICC has, however, stayed implementation of its decision in order to accord the railroads another opportunity to justify the need for rate bureau antitrust immunity.

The 4R Act amended section 5a of the IC Act by making that section applicable only to carriers other than railroads, and by creating a new provision, § 5b, for railroads. Under section 5b, the carrier members of a bureau are prohibited from agreeing or voting on single-line rates, although such rates may be discussed, and only those members who "practicably participate" in an interline movement may agree or vote on the rate for that movement. Further, the right of a single railroad to take independent action on a rate is guaranteed.

On the other hand, none of these restrictions applies to general rate increases (simultaneous across-the-board increases on all or almost all rates by all railroads), or

to "broad tariff changes." The terms "practicably participate" and "broad tariff changes" were left to the Commission to define. Additionally, the ICC cannot approve an agreement -- even if it complies with these terms -- unless it is also found to further the national transportation policy.

In the summer of 1976 rate bureaus submitted new agreements to the ICC, embodying changes required by section 208. The agreements became the subject of extended hearings before an ICC Administrative Law Judge (ALJ). The ALJ ruled on several significant issues, providing the first interpretation and definition of fundamentally new rate bureau concepts. The ALJ defined the term "practicably participate" as participation by the voting carrier in any route from any origin to any destination point covered by a proposed tariff. This is essentially the definition proposed by the carriers. On single-line rates, the Judge went beyond the exact wording of the statute, which forbids carriers to agree or vote on single-line rates, but permits them to be discussed, and required the bureaus to process each proposal covering a single-line movement separately from proposals covering joint-line or other single-line movements, so as to assure that single-line carriers cannot effectively or tacitly agree with other single-line and joint-line carriers.

The ALJ also held: (1) that the ICC is not empowered to grant antitrust immunity for collective intrastate ratemaking; (2) that independent action of a single carrier member of

a bureau could not be conditioned on the right of connecting carriers to "concur" in the independent action; (3) that affiliated carriers (parts of the same overall corporation) should not be treated as a single carrier for purposes of rate bureau voting restrictions; and (4) that the term "broad tariff changes" should be loosely defined as changes of general application from, to, or within the territory covered by the bureau's members. The ALJ granted antitrust immunity for all rate bureau transactions.

Had the ALJ's decision represented the end of the process, the 4R Act would have resulted in relatively little change in rate bureau operations. But the most important ICC action in the rate bureau area did not occur until July 1978 -- almost 2-1/2 years after passage of the Act -- when the full Commission issued its decision on the appeals from the ALJ's findings, and reversed the central decision that the agreements should be approved.

The Commission consolidated the three major rate bureau agreements into a single case, and resolved all of the appeals from the ALJ's decisions in a single decision. In its most important finding, the Commission interpreted the section 5b requirement that a rate bureau agreement must be in furtherance of the national transportation policy to necessitate three findings:

> (1) whether the proposed agreement would enhance one or more national transportation policy goals, (2) whether the advantages of the agreement override other considerations such as the anticompetitive nature of the agreement, and (3) whether the agreement is necessary or whether the objectives of the parties could be accomplished instead by some other means. Decision of the Commission, section 5b Application Nos. 2, 3, and 6, served July 21, 1978, at 4.

The ICC then found that none of the three major rate bureaus had proven these points, but concluded that:

> Applicants did not fully understand their burden of proof concerning the [national transportation policy] issue . . . . Accordingly, the Commission will withhold an order terminating the interim approval granted to these agreements for a specified period to afford applicants an opportunity to submit additional evidence . . ." Id. at 8.

The ICC upheld the ALJ's decisions in all other respects except the definition of "practicably participate". The ICC found that the ALJ's definition failed to consider new traffic and adopted a modified version of a definition proposed by the Federal Trade Commission. The decision allows voting and agreement by carriers who will participate in the carriage of "new traffic", and defined the situation in which traffic could be said to be "new". While the ICC generally upheld the ALJ's decisions regarding single-line rates, it limited discussions of such rates to issues involving possible discrimination between shippers, localities (etc.), as defined under sections 2, 3, and 4 of the IC Act. Finally, and also very importantly, the ICC added a new requirement -- that all rate bureau meetings be open to the public, on the grounds that "Close monitoring of the rate bureau meetings will be

necessary . . . to insure that the pro-competitive aspects of section 5b are not circumvented . . . [but] the Commission does not have suffiicent personnel to monitor every . . . meeting." Id. at 17.

The ICC permitted the rate bureaus to submit new evidence on the national transportation policy issue only. The bureaus have done that, and have also challenged the ICC's decision in the courts on the grounds that the ICC exceeded its authority. Neither the ICC nor the court has issued a further decision.

The Office of Rail Public Counsel -- not in existence at the time of the original rate bureau hearings -- has recently filed comments on the bureau's new justification statements, concluding: "There is no convincing reason to believe that continued rate bureau activity is needed to permit the establishment of joint interline rates, to avoid discrimination against shippers or regions, or to prevent the imposition of burdensome . . . costs upon shippers and railroads." Comments of the Office of Rail Public Counsel on Section 5b Application Nos. 2, 3, and 6, filed January 5, 1979, at 38. This conclusion echoes the findings and recommendations issued separately by the Department of Justice and the Federal Trade Commission.

While the ultimate outcome of these proceedings is uncertain, it is clear that the ICC and others have taken a hard look at the continued need for railroad rate bureaus to receive antitrust immunity. It may be that one of the 4R Act's least sweeping changes thus results in one of the most far-reaching innovations in rail operations.

6. Demand-Sensitive Rates

As of October 1978, the railroads had proposed at least nine demand-sensitive rates, of which many are still pending at the ICC.[9/] The reason for this limited use appears, once again, to be attributable to restrictive ICC regulations. The regulations are, in fact, so wrongly conceived that the demand-sensitive rates may themselves cause traffic diversion whenever demand conditions do not change in the way foreseen by the rate. This means that seasonal and peak-load pricing is functioning to exacerbate peaks and troughs of demand -- the exact opposite of the Congressional goal.

Section 202(d) of the 4R Act adds a new paragraph 1(17) to the IC Act requiring the Commission to establish, by rule: "standards and expeditious procedures for the establishment of railroad rates based on seasonal, regional, or peak-period demand for rail services."

On June 10, 1976, the Commission instituted a proceeding to implement section 202(d) and to:

> [E]ncourage the publication of seasonal, regional, and peak-period rates for rail service by removing any impediments to their publication and by establishing a regulatory climate conducive to experimentation in railroad ratemaking. 10/

The Commission's original proposal in this proceeding did little to accommodate the Congressional intent to provide

rail management with sufficient flexibility to experiment with these new forms of demand-sensitive rates. Although many of the proposed definitions and guidelines recognized that by their very nature demand-sensitive rates must not be rigidly regulated, the regulations eventually promulgated still do not allow rail management sufficient flexibility to initiate and cancel rates in accordance with rapidly fluctuating demand.

The rules relating to seasonal and peak period rates suffer from two major faults. First, they must be filed with the Commission and can be protested. Thus, they may require substantial lead time to implement. Second, only rate levels proposed and approved in advance can be implemented. That is, even though a rate increase may be warranted as a result of changing market conditions, only the peak rate approved and published in advance can be put in effect, and only when the tariff indicates it is to go into effect. Thus, unless both the magnitude and timing of the peaks and troughs in demand can be precisely forecast, there is no way to design a peak or seasonal rate that accurately reflects changing market conditions. The Commission declined to permit railroads to publish maximum and minimum rates in advance and to change their rates between the two limits as market conditions indicated. However, large, unforeseen changes

in demand for service, and changes in the prices competitors charge for service create the conditions under which railroads need additional pricing flexibility most. It is in these two areas that the Commission's peak and seasonal rate rules did least to increase pricing flexibility.

The statute itself could have done much to minimize these problems had they been foreseen. The statute could, for example, have permitted contract rates and could have modified or voided notice and publication requirements in many demand-sensitive situations. Further, the difference between seasonal and peak pricing is unclear, and the meaning of regional pricing, not set out in the statute, and not defined by the ICC is so unclear that no regional rate has ever been proposed.

Some help may be forthcoming as the result of a peak-load pricing proposal challenged in the courts. Almost two years ago the Southern Freight Association proposed a 20% increase in the peak-load rates on grain and soybeans, with no offsetting off-peak decrease. The ICC rules permit such a tariff, and it was approved without investigation. A group of grain shippers challenged the rates on the grounds that they were unreasonable and not in fulfillment of the objectives of the statute . The U.S. Court of Appeals for the Eighth Circuit remanded the case to the ICC. The Court did not

rule on the legality of the rates, only on the failure of the ICC to order an investigation. Although the Court ordered the ICC to handle the remand on an expedited basis, in the three months since the Court's decision, the ICC has done nothing. The eventual investigation should, however, lead to additional, clarifying regulations.

In general, however, the 4R Act was seriously flawed in the area of demand-sensitive rates. Peak-load pricing must be set free of Commission regulation if the railroads are to take it seriously. When one considers that peaks are most commonly associated with agricultural products, as to which trucks and barges that compete with rail are totally deregulated, then it is clear why this provision has been so little used and of so little help.

7. Distinct Service Pricing

Section 202(d) of the 4R Act added two new subsections to existing section 15 of the IC Act. The second of the two reads as follows:

> In order to encourage competition, to promote increased reinvestment by railroads, and to encourage and facilitate increased non-railroad investment in the production of rail services, a carrier by railroad subject to this part may, upon its own initiative or upon the request of any shipper or receiver of freight, file separate rates for distinct rail services. Within 1 year after the date of enactment of this paragraph, the Commission shall establish, by rule, expeditious procedures for permitting publication of separate rates for distinct rail services in order to (a) encourage the pricing of such services in accordance with the carrier's cash-outlays for such services and the demand therefor, and (b) enable shippers and receivers to evaluate all transportation and related charges and alternatives.

This provision was addressed to the prevalent railroad practice of aggregating or bundling a wide variety of services (including, particularly, transit, reconsignment, and diversion of shipments) into a single tariff with a single rate. This means that a shipper wishing to purchase only some of the services included within the tariff had to purchase all of them, at a rate higher than necessary. By separating or disaggregating services from a tariff and pricing them separately, a railroad could more closely tailor both price and service to the needs of individual shippers.

To our knowledge, this provision has been used only five times. In November, 1978, the Denver and Rio Grande Western Railroad proposed to lower its single-car rate for

the transportation of bulk molybdenum between two points in Colorado to Iowa and Pennsylvania. The distinct service removed from the tariff was the provision of insurance above $100 a ton. To date, no information on the other four cases has been available from the Commission.

The lack of use of this provision is, again, attributable to two causes: a vague and limited statute, interpreted restrictively by the ICC. The statute failed to permit railroads flexibility in providing and pricing separate services -- indeed, such pricing remained subject to the full panoply of ICC regulation. In interpreting the provision the ICC not only required rigid adherence to all of its regulations, it failed even to implement the one change mandated by the statute -- expeditious procedures. Other serious flaws are that the ICC's rules: (1) do not allow varying qualities of line-haul service to qualify as distinct rail services; (2) fail to consider "demand" in judging the reasonableness of a proposed rate as required by the statute; and (3) are too rigid in prescribing the nature and timing of data submitted in support of rate proposals.

Most importantly, the Commission reaffirmed an earlier decision that effectively requires railroad management to publish a line-haul rate decrease in every situation in which a distinct service is disaggregated from an existing tariff.[11]

The relevant portion of the Commission's decision in the earlier case held that not only must the price for a distinct service be reasonable, the underlying line-haul rate must be proven reasonable as well. The concern that appears to have motivated the Commission was that failure to change the line-haul rate, when a distinct service is separated from it, would have the effect of increasing that rate. Actually, this result would occur in some cases, but not all, depending on how many of the shippers affected by the rate were taking advantage of the distinct services embodied within it in the first place. Those shippers paying the full rate, but not utilizing all the distinct services associated with it, would not be disadvantaged if some of those unused distinct services were no longer available, except at additional cost.

Further, requiring a lessening of the rate for the line-haul service to offset the disaggregation of and separate charge for the distinct service thwarts one of the fundamental objectives of the 4R Act. The Act is explicitly aimed at increasing railroad ratemaking flexibility not only as an end in itself, but also as a means of increasing railroad revenues and the attractiveness of investing in the railroad industry. Strict application of past Commission decisions to all distinct service pricing proceedings simply

results in the substitution of one rigid regulatory policy for another. It deprives the railroads of additional revenues in markets in which demand could accommodate price increases and of the ability to compete intermodally in markets served by regulated and unregulated carriers.

Additionally, neither the statute nor the Commission's rules attempts to reconcile distinct service pricing with the anti-discrimination provisions of the IC act. It seems likely that one reason that distinct service pricing has not been used is the railroads' concern that such prices would be thwarted by routine protests arguing that distinct services and prices offered to a given shipper must be available to all shippers, or that the shippers who are offered such services must all be charged the same rates. The statute is clear that a railroad decision to separate services and price them separately should be a reflection of the competitive and other transportation conditions surrounding a particular movement. Thus, if the railroad is able to separate, say, reconsignment and diversion privileges in connection with lumber movements in a paticular geographic area, this does not mean that movements other than lumber or shippers in other areas must have the same service available, or that those to whom it is offered must all be charged the same rate. The ICC recognized this problem in the decision promulgating its rules, but explicitly declined to deal with it, preferring case-by-case adjudication.

In light of these several problems with the statute and the Commission's implementing rules, it is not surprising that the distinct service pricing provision of the 4R Act has not often been used. In fact, it is doubtful that any provision as limited as this one will ever be used widely. Attempting to insert a statutory change of this kind into the multitude of the other and often inconsistent statutory and regulatory rules will result in little innovation.

8. Capital Incentive Rates

a. The Statute

Section 15(19) of the IC Act was added by §206 of the 4R Act, and reads as follows:

> Notwithstanding any other provision of law, a common carrier by railroad ... may file with the Commission a notice of intention to file a schedule stating a new rate, fare, charge, classification, regulation, or practice, whenever the implementation of the proposed schedule would require a total capital investment of $1,000,000 or more, individually or collectively, by such carrier, or by a shipper, receiver, or agent thereof, or an interested third party. The filing shall be accompanied by a sworn affidavit setting forth in detail the anticipated capital investment upon which such filing is based. Any interested person may request the Commission to investigate the schedule proposed to be filed, and upon such request the Commission shall hold a hearing with respect to such schedule... Unless, prior to the 180-day period following the filing of such notice of intention, the Commission determines, after a hearing, that the proposed schedule, or any part thereof, would be unlawful, such carrier may file the schedule any time within 180 days thereafter to become effective after 30 days' notice. Such a schedule may not, for a period of 5 years after its effective date be suspended or set aside as unlawful under section 2, 3, or 4 of this part, except that the Commission may at any time order such schedule to be revised to a level equaling the variable costs of providing the service, if the rate stated herein is found to reduce the going concern value of the carrier (Emphasis supplied).

On October 19, 1976, section 15(19) was amended by the Rail Transportation Improvement Act. That amendment added section 1 of the IC Act to the list of regulatory provisions that may not be used to challenge a capital incentive rate once it is approved. (Sections 2, 3, and 4 of the IC Act prohibit various forms of discrimination. Section 1 requires that a rate be just and reasonable).

b. The Regulations

On July 27, 1976, the ICC initiated a rulemaking proceeding (Ex Parte No. 327), 12/ whose purpose was to "encourage the filing of capital incentive rates by facilitating publication and by establishing expedited procedures to resolve controversies associated with the filing of rates based on a capital investment of $1,000,000 or more." On June 8, 1977, the Commission issued its Report. The Report failed to address many of the most fundamental problems inherent in the concept of capital incentive rates, and established regulations that are confusing and inconsistent. These problems, and the two primary cases under the statute, are discussed below.

1. Innovation. Although the legislative history of §15(19) indicates some intention to require capital incentive rates to be premised on innovative or entirely new services, no such requirement appears explicitly in the statute, or in the implementing regulations at all.

2. Qualifying Investment. The ICC Report accepted the DOT suggestion that car investments be dedicated to a particular shipper, but made no finding with respect to locomotives. The Report also concluded that a "major investment affecting traffic generally" would not qualify for §15(19) treatment, but does not rule out investment in main line

track. To confuse matters further, the ICC Report suggested that the capital investment must be for equipment or facilities without which the rail service could not be performed, but elsewhere concluded that the test should be whether the investment has "an identifiable effect upon specific traffic [that] would satisfy the requirement of a nexus between the investment and the implementation of the proposed schedule." This inconsistency lies at the heart of the two capital incentive rates cases discussed below.

3. Discrimination. The ICC explicitly refused to decide whether a non-investing shipper who competes directly with an investing shipper is entitled to the same rate.

4. Changes in the terms of the rate. The ICC Report concluded that capital incentive rates could be adjusted or cancelled prior to the end of the 5-year period. The Commission did not, however, require that such changes be agreed to by both parties to the rate. Thus, a shipper who makes a large investment on the assumption that a particular rate would remain in effect for five years could be faced with numerous increases in or early cancellation of that rate. Although a change in or cancellation of the rate could be protested, the regulations do not provide for special consideration of the unusual nature of the rate.

Similarly, a railroad investment could be based on a projected five-year, minimum volume of traffic, but the ICC regulations do not call for the shipper to guarantee such traffic. A related problem would arise if the investment project took an unexpectedly long time to complete -- such that the 5 years were nearing an end before the fruits of the investment were realized.

5. Shipper/Railroad Disagreement. Central to the shortcomings of the statute, and not addressed in the ICC regulations is the failure to recognize that a §15(19) rate may not have been negotiated by the shipper and the carrier. In fact, the first two section 15(19) rate proposals were put forward by the railroads when negotiations with the affected shippers failed. In each case the shipper protested the rates. Thus, ambiguities in the statute, not resolved in the regulations, are now being litigated in the courts. While the first two litigated cases deal with the qualifying investment problem, it is not difficult to imagine subsequent litigation over unilaterally proposed changes in the level of a capital incentive rate, incompleted investments, or termination of the rate in less than five years.

c. The Cases

As observed earlier, the first two cases brought under the capital incentive rates provision highlight the problems with the statute and the regulations. The cases were decided on November 28 and 30, 1977, under the rules adopted in Ex Parte No. 327. 13/

1. The Cochise Case

On June 1, 1976, the Santa Fe and Southern Pacific Railroads filed with the ICC a Notice of Intent to file a capital incentive rate for coal movements between Gallup, New Mexico and Cochise, Arizona (523 miles). The rate applied to shipper-owned cars, in unit train service, with a 1,000,000 ton per year minimum. In affidavits accompanying the Notice of Intent, the railroads stated that the following capital investments would be needed:

Locomotives and related equipment (Santa Fe):	$3 million +
Construction and upgrading of track (Santa Fe):	$2.41 million
Locomotive and related equipment (SP):	$2 million +

Arizona Electric Power Co. (AEPC), which had entered into a contract to purchase coal mined in Gallup for two new generating plants at Cochise, protested the proposed rates, partially on the ground that the associated capital investment did not qualify under section 15(19).

AEPC claimed that since the eight locomotives proposed to be purchased by the railroads would not be dedicated to

the traffic moving under the proposed rate, the purchase does not satisfy the §15(19) test. Interestingly, AEPC also argued that if the locomotives were dedicated, the railroad would be violating its common carrier obligation, but offered no resolution of this no-win argument. With respect to the proposed investments in construction and upgrading projects, AEPC witnesses testified that they had made careful on-site inspections and concluded that the proposed improvements were desirable, but not required to enable the railroads to carry the AEPC traffic.

The railroads replied that the investment in new locomotives was directly attributable to AEPC traffic, although they acknowledged that the locomotives would not be dedicated to that traffic. The railroads argued further that the proposed investment in track was needed for safe, efficient, reliable service of the type associated with unit trains.

On the important question of whether equipment must be dedicated to a particular service if it is to qualify as a 15(19) capital investment, the ICC said:

> Since it is clear that the usual practice of a railroad offering coal unit-train service is to pool available locomotive power ... we do not believe that the total cost of all the new locomotives should necessarily be considered as qualifying the proposed schedule for capital incentive rate treatment. <u>While we reject an interpretation of section 15(19) that would make 'dedication' of plant or equipment ... a prerequisite ... under section 15(19) there must be a proper allocation between</u>

> existing and new equipment and a showing that the additional locomotive power is needed for the new service rather than for the carrier to fulfill its statutory obligation. However, in this instance we are convinced that the threshold $1 million requirement has been met... (Report and Order at 18; emphasis supplied).

The decision made no mention of the Ex Parte No. 327 criteria that require dedication of cars purchased in connection with a capital incentive rate. The ICC offered no comment at all on AEPC's contention that dedication of a locomotive would be a violation of the railroads' common carrier obligation.

On the issue of roadway investment, the ICC quoted its decision in Ex Parte No. 327, requiring a proposed capital investment to have "an identifiable effect upon specific traffic..." The decision then concluded:

> We think that respondents have adequately demonstrated, with specific details of needed improvements, that major capital investments in roadway will be required to implement the proposed schedule and that such investments are directly identified with the specialized service requirements demanded by AEPC. Protestant's emphasis on the adequacy of the track in its present condition ... ignores safety and service factors which must be considered if 1,000,000 tons per year of AEPC coal is to move safely and reliably under the proposed schedule ... (Report and Order at 20).

On March 13, 1978, AEPC challenged the ICC's decision in the U. S. Court of Appeals for the District of Columbia Circuit (Docket No. 77-2071). While other issues were again raised, the first ground of appeal was that the proposed rate did not qualify for §15(19) treatment. The AEPC brief

quoted extensively from the Congressional debates on the 4R Act, in an effort to prove that section 15(19) was meant to apply only to "service innovations," and that the service involved here fell within the railroad's common carrier obligation.

2. The Smithers Lake Case

The issues in this case are essentially the same as those in Cochise. The Burlington Northern, Colorado & Southern, Fort Worth & Denver and Santa Fe Railroads filed with the ICC on June 3, 1977 a Notice of Intent to file a capital incentive rate of $15.60 per ton for the transportation of coal in shipper-owned unit train cars from Cordero, Wyoming to Smithers Lake, Texas (a distance of 1607 miles). No minimum tonnage requirement was involved. The accompanying affidavits stated that the following capital investments were needed to implement the proposed rate:

Locomotives and related equipment (BN)	$27 million
Improvements and increased maintenance in track structure (BN)	$1 million +
Construction of new rail line	$1 million +
Locomotives and related equipment (Santa Fe)	$9 million +

The rate was protested by Houston Lighting and Power Co. (HL&P), on the ground, among others, that the rates should not have been handled under §15(19).

HL&P argued that the proposed investments do not have the requisite "identifiable effect" upon their traffic, since the locomotives would not be dedicated, and the roadway investment would benefit all traffic, and, in any event, is an operating expense, not a capital costs. Further, HL&P argued that even the new rail line proposed to be built would handle traffic other than that provided by HL&P. The ICC concluded:

> Contrary to protestant's contention, respondents' evidence regarding the purchase of locomotives ... satisfies the requirement of a reasonably direct effect upon the rail transportation service to which the proposed ... rate applies ... While we reject an interpretation of section 15(19) that would make 'dedication' of plant or equipment ... a prerequisite ... there must be proper allocation between existing and new equipment and a showing that the additional locomotive power is needed for the new service rather than for the carrier to fulfill its statutory obligation ... (Decision at 24).

This decision was appealed the same day as Cochise and on the same grounds.

d. Conclusion

Neither the Cochise nor the Smithers Lake case has yet been decided, and it is, therefore, impossible to assess how this 4R Act provision is going to work, notwithstanding the long, expensive, and complex litigation already endured. It is clear, however, that the ICC regulations failed to resolve the complexities and ambiguities of the statute, and its case decisions failed to reach clear findings on the fundamental issues. This is another example of the difficulties of trying to fit innovative, but limited, ratemaking proposals into the inconsistent and confusing morass of other statutory and regulatory restraints.

9. Recyclables

Section 204 of the 4R Act required the ICC to study and compare the rates on recyclable materials and those on competing virgin materials. The Commission issued its decision on February 1, 1977. The decision was appealed to the United States Court of Appeals for the District of Columbia by representatives of recycling industries and the Justice Department (on behalf of the United States). The Court reversed the ICC's decision and remanded it to the ICC on October 16, 1978.14/ On December 18, 1978, the ICC reopened the proceeding and began again.

The Court found that the ICC had, in the last ten years, approved a series of annual rate increases in rates on recyclables, nothwithstanding claims that the increases would discourage use of recyclables and have an adverse effect on the environment and on the supplies of virgin resources. In all of those cases, the Commission found that the recyclables industries had failed to meet their burden of proof in protesting a rate increase, an unexplained variation on the long-standing statutory mandate that the proponent of a rate change must prove it is just and reasonable. Section 204 in requiring an overall study of recyclables, specifically placed the burden of proof on the railroads.

The Commission's decision in the 4R Act proceeding found that the demand for transportation of recyclables was inelastic, and, therefore, that the railroad rate increases had not decreased the amount of recyclable materials transported by rail. Further, the ICC held again that not all recyclable materials directly competed with their virgin material counterparts. From these findings, the ICC concluded that competition between shippers of recyclable and virgin materials was not adversely affected by the disparate rail rates applied to each.

The Court, in reversing the ICC decision, noted that section 603 of the Regional Rail Reorganization Act of 1973 required the ICC to "eliminate discrimination against the shipment of recyclable materials in rate structures ..." thus signalling its belief that transportation rate structures were discriminatory. The court found that the ICC disregarded this:

> By reversing the burden of proof ... Congress accomplished more than a mere change in the procedural format for presentation of evidence ... Specifically, it erected an evidentiary presumption against the lawfulness of the rate stucture ... [T]his investigation was to proceed from the premise that disparate rate structures were not justified by the revenue need of the railroads... Id at 533.

The Court took the Commission decision to task on other grounds, as well:

> [T]he Commission ... found that recyclable and virgin products do not compete for transportation purposes. These findings, based more on the Commission's perceptions

> of industry structures than on articulated determinations with respect to rate structures, neither comport with the Commission's mandate nor rationally flow from the record... Id at 540.

In remanding the case to the Commission for "further proceedings consistent with this opinion," the Court was careful to note:

> [W]e ... emphasize that our discussion of the standards employed by the Commission to determine the lawfulness of these rate structures, and of the evidence submitted by the railroads, is not intended to set forth our view of the lawfulness of any of the rate structures involved. They may be lawful, or they may not.

The ICC has not as yet received any evidence in its recently reopened proceeding. The recyclables matter thus stands where it did when the 4R Act was enacted. It is, clear, however, from this discussion that the statute itself is hardly unambiguous. A reconciliation between the recyclables provisions of the 4R Act and the 3R Act was required, and a clearer statement of Congressional intent would have eliminated the need for much of this protracted, expensive, and thus far unproductive litigation. Most importantly, if, as a matter of social policy, recyclables are to be treated differently than other commodities, we must have a full debate on whether the railroads are to bear the costs of that policy.

10. Intrastate Rates

Prior to passage of the 4R Act, section 13(4) of the IC Act provided that the Commission shall prescribe an intrastate rate when that rate:

(a) causes unreasonable discrimination against persons or localities in interstate commerce, or

(b) causes unreasonable discrimination against or imposes an unreasonable burden on interstate or foreign commerce.

Section 210 of the 4R Act added a new subsection to the IC Act, section (13(5)), giving the ICC jurisdiction to prescribe an intrastate rate when:

(a) a carrier files with a state authority to change an intrastate rate to adjust that rate to the rate charged on similar traffic moving in interstate commerce, and

(b) the state authority does not finally act on the change by the 120th day after it is filed.

The standards to be applied by the ICC in setting an intrastate rate are the same under sections 13(4) and 13(5).

In October, 1976 this provision of the 4R Act was amended by adding the following new sentence: "Nothing in this paragraph shall affect the authority of the Commission to institute an investigation or to act in such investigation as provided

in paragraphs (3) and (4) of this section." This new provision means that the ICC may initiate an investigation of an intrastate rate on its own motion.

The legislative history of the 4R Act suggests that the Congress intended to create a prompt and convenient local forum in which local customers may express their views and furthermore that the disposition of a matter by the state forum be prompt. Accordingly, the Commission has decided that it may not act until the 120-day period has expired or until a final state decision is rendered, whichever occurs first.

In two recent cases, Montana Intrastate Freight Rates and Charges - 1976, 355 I.C.C. 644 (1977); and Montana Intrastate Freight Rates and Charges - 1977, 357 I.C.C. 281 (1978), the Commission determined that the intrastate rates were budensome on interstate commerce and ordered increases into effect.

In the 1976 case, the Montana Commission dismissed the case within 120 days on the grounds that a prima facie case for the increase had not been made. The Commission decided that the fact the state had considered and denied the requested relief within 120 days meant that they did not have § 13(5) jurisdiction, but that none was necessary in light of § 13(4).

In the 1977 case, the carrier failed to supply the Montana Commission any evidence in support of the increase, and suggested to the state commission that the case be dismissed, which it was. The ICC noted in this case that there was a serious substantive inconsistency between ICC and Montana ratemaking standards, and that the railroads should not be forced to litigate twice under different standards, particularly since

> Section 13(5) is intended to curtail delays in the State proceeding, including insurmountable delays in obtaining evidence, without infringing upon the State authority. Id at 283.

The Commission thus assumed jurisdiction in the 1977 case, presumably on the basis of §13(4) - although it does not specifically say so.

In a recent, and more troubling case, the ICC reached an essentially opposite conclusion, finding that the failure of West Virginia railroads to observe the filing requirements of the West Virginia Public Service Commission (PSC) meant that the 120-day waiting period never began to run. West Virginia Intrastate Rates-Ex Parte No. 343, 357 I.C.C. 678 (1978). Although the West Virginia railroads, like the Montana railroads, argued that the West Virginia requirements were burdensome and inconsistent with ICC requirements, the ICC dismissed the argment as "feeble," and cited the fact that the railroads' rate proposal was never actually "filed" with

the PSC. The ICC also noted that although the October amendment to the 4R Act allows the ICC to institute an investigation on its own, and that the breach of state filing requirements was, therefore, not fatal, "primary jurisdiction is traditionally with the States." Id at 681. The railroads were, thus, required to begin again at the state level.

In reality, the 4R Act provision does not give the ICC new jurisdiction over intrastate rates. The scope of the ICC's jurisdiction is outlined in § 13(4). Section 13(5) merely adds a provision that grants exclusive authority over intrastate rates to the ICC in the event of a state failure to act promptly.

All three of these cases could have been decided without benefit of the 4R Act, which neither changes the substantive law, nor confers original jurisdiction on the ICC in any circumstance. Additionally, as the cases show, the 4R Act provision is unclear as to whether the railroads must comply with all state requirements before invoking ICC jurisdiction. We are also concerned that by permitting states 120 days to decide cases, the statute would permit a state effectively to block a railroad's peak-load pricing or similar demand-sensitive rate. We are not aware of any such instances -- but some railroads cite this concern as another reason for limited use of their peak-load pricing authority.

11. Revenue Divisions

Section 15(6) of the IC Act was amended by section 201 of the 4R Act which added new procedural provisions to expedite the handling of divisions of revenue cases. The principal change in section 15(6) is the requirement that within one year of the filing of a divisions of revenue complaint the evidentiary proceeding must be completed, except that a two-year period is provided for proceedings instituted on the Commission's own initiative and the two-year period may be extended if the ICC finds it necessary.

Complaints with respect to divisions of revenue are filed when the parties to joint rates are unable to decide between them how to split the revenues generated by the joint rate. Such proceedings are, therefore, highly controversial, complex, and lengthy (some last 15 years). As the ICC noted in its proceeding under section 201, it is necessary in such a proceeding to identify the traffic at issue, the joint rates on the traffic, and the cost associated with its transportation, as well as the other factors set forth in section 15(6)(a). The length of divisions cases is often attributable, at least in part, to reuqests from all parties for time to conduct traffic or cost studies or counter-studies to refute the contentions of the other side.

The goal of the 4R Act legislation is to assure that a final decision can be rendered expeditiously in divisions cases. To implement this goal the ICC proposed that divisions disputes not be submitted to the Commission until it is clear that the

issues cannot be resolved on a voluntary basis. To encourage the parties to resolve their differences in a voluntary manner, the ICC required that prior to submitting a notice of intent to file or submitting a formal complaint, the parties must show that they sought to negotiate the divisions arrangement in issue. Additionally, the complainant must summarize the negotiations and specify areas where agreement could not be reached.

The ICC also established a new layer of proceeding -- the "notice of intent to file a complaint." The notice must state the problem, and indicate when the filing of a formal complaint is contemplated. The ICC offered no explanation as to why this new, and obviously lengthy, procedural requirement would help to expedite the hearing and resolution of a divisions case.

The ICC has no estimates of the average time expected to be consumed in a divisions case brought subsequent to the 4R Act as compared to those brought before 1976. Informal contacts with railroad lawyers suggest that proceedings are likely to last a minimum of five years (six months for the notice of intent period to run, six months of negotiation, at least two years (provided by the statute) for the ICC to act, and two years for appeals). While this is an improvement, it is still not an inviting prospect. We understand that only one divisions case has been brought before the

ICC since passage of the 4R Act, and it has not, of course been decided.

The primary problem about divisions is not, however, the length of time required to resolve them, but rather the notion that the ICC need be brought in at all. If railroads cannot agree on how to split the revenues under a joint rate, then no joint rate need be established. Interline movements do not require joint rates; summing the relevant local or proportional rates[15/] would allow interline movements to occur under single-factor rate quotations, and would eliminate entirely the expensive and protracted litigation associated with divisions. It is necessary only to prohibit a railroad with both single- and joint-line service from discriminating against the interline movement. The 4R Act thus addressed only the symptom, not the problem itself.

12. Adequate Railroad Revenue Levels

A. Revenue Need Assessment

Section 205(2) of the 4R Act added section 15a(4) to the IC Act, and reads, in pertinent part:

> With respect to common carriers by railroad, the Commission shall within 24 months after the date of enactment of this paragraph, ... develop and promulgate (and thereafter revise and maintain) reasonable standards and procedures for the establishment of revenue levels adequate under honest, economical, and efficient management to cover total operating expenses, including depreciation and obsolescence, plus a fair, reasonable, and economic profit or return (or both) on capital employed in the business. Such revenue levels should (a) provide a flow of net income plus depreciation adequate to support prudent capital outlays, assure the repayment of a reasonable level of debt, permit the raising of needed equity capital, and cover the effects of inflation, and (b) insure retention and attraction of capital in amounts adequate to provide a sound transportation system in the United States. The Commission shall make an adequate and continuing effort to assist such carriers in attaining such revenue levels.

Pursuant to the requirements of section 205, the ICC issued its report and accompanying regulations in January 1978.16/ In its Report, the Commission accepted DOT's recommendation that annual revenue adequacy assessment proceedings be established to determine the revenue needs of each railroad.

The Commission also concluded that the effects of the rising cost of debt and changing conditions in the equity market make it necessary to reevaluate periodically the level of return needed by the railroads to attract capital. In that connection, DOT urged that the standard by which revenue adequacy be measured is whether rate of return on net invest-

ment equals the cost of capital. The Commission, however, decided that revenue adequacy should be determined upon consideration of other financial indicators, as well, including other financial ratios and the flow of funds. 17/ The Commission further decided not to assign predominant weight to any single standard.

As to railroad operating and management efficiency, the Commission concluded that satisfactory specific means of measurement were not available, but that it would give its continuing attention to establishing standards for honest, efficient, and economical management. As to the use to which the annual revenue need assessment would be put, the ICC decided that once determined, adequate revenue levels will be regarded by the Commission as an "important factor" in general and individual rate increase proceedings and that "Section 15a(4) places no limitation on the regulatory contexts in which revenue adequacy is to be given consideration." 18/ The Commission went on to find:

> The setting of rates for individual services is complicated by the fact that a railroad incurs fixed or overhead costs from its general operations, in addition to the specific costs caused by the provision of the particular service. Thus, its rates cannot be set simply to cover the costs incurred in providing the particular service, but must be set at a higher level where possible to make a contribution to the coverage of fixed costs. A further complication is that fixed costs cannot be recovered in equal proportions from each service because demand and competitive factors place varying limits on the rates that can be maintained on different types of traffic. Thus, while the Commission is required to limit rates to levels that are just and reasonable, there is not simple formula that can be followed for doing so.

> Where the reasonableness of a rate is questioned in an indivudual proceeding, we consider, among other things, cost evidence, comparative rate evidence, and circumstances relating to demand and competition. The effect of section 15a(4), we believe, is to require that revenue adequacy also be given explicit consideration in these proceedings. In order to facilitate such consideration, we shall make findings in our periodic independent proceeding as to the adequacy of the overall revenue level of each class I carrier. In individual proceedings, then, the revenue adequacy status of each proponent carrier can be taken into consideration. *Id* at 17. Emphasis supplied.

On June 7, 1978, the Commission instituted the first yearly proceeding, designated as Ex Parte No. 353, for the 1978 determination of railroad revenue adequacy. On December 5, 1978, the Commission issued a partial decision discussing only the question of the railroads' cost of capital -- a figure that can, for some purposes, be translated into needed rate of return. The Commission determined that the composite cost of capital for *all* railroads is 10.6%, a figure contrasting dramatically with the industry's current 0.24% rate of return on net investment.

In order to compute the composite cost of capital, it was necessary for the Commission first to determine the cost of debt, the cost of equity, and the overall capital structure. Once these computations are made, the cost of capital can be measured by a simple calculation.

In determining the cost of debt, the ICC adopted DOT's recommendation that called for the embedded debt rate rather

than the current debt rate. For the purposes of this proceeding, the Commission held that the cost of debt capital was 7.0 percent.

With respect to the cost of equity capital, the Commission rejected DOT's proposed comparable earnings approach, emphasizing the problems encountered in selecting firms of comparable risk and in determining suitable time periods from which to draw data, and adopted instead a method of analysis that involves market value studies, including a discounted cash flow approach. This methodology relies on stock market data to show the rate of return required by stock investors, and resulted in a determination that a reasonable estimate for the cost of equity capital is 13 percent.

Finally, concluding that the carriers' actual capital structure was 40 percent debt and 60 percent equity, the ICC found the overall cost of capital to be 10.6 percent.

These are the only conclusions thus far reached by the Commission in Ex Parte No. 353, and they deal with only half the issue. The ICC promised to deal, in a subsequent decision, with the question of how to apply the 10.6% figure in rate

increase cases, and how to comply generally with the 4R Act requirement that the ICC "assist" the railroads in achieving the rate of return the Commission finds appropriate. While a great deal of time and effort has been spent in implementing section 205 of the 4R Act, there is relatively little to show for it.

Once again, however, much of the problem lies in the statute itself. The statute recognizes the need for the railroads to earn a rate of return that will allow them to attract capital investment and remain privately owned, yet the statute does not require the ICC to take any specific steps to assure that any or all of the railroads actually earns such a return. For example, the market dominance provision does not set a floor, related to adequate rate of return, below which the ICC cannot set a rate. Although the ICC itself has recognized that highly transportation competitive commodities will be diverted if rail rates are raised, it nonetheless keeps rates on less easily diverted commodities to levels that barely cover the full costs of the service. That pattern of decision-making effectively precludes the railroads from earning the adequate rate of return sought by the 4R Act. The 4R Act failed to address this practice.

B. Umbrella Ratemaking

Section 205(2) also addresses the problem of "umbrella ratemaking," the term used to describe the ICC practice of keeping railroad rates artifically high to protect other transportation modes (primarily water carriers). Prior to 1920 the ICC had been concerned about unreasonably high or discriminatory rates. The Transportation Act of 1920 gave the ICC for the first time authority to determine minimum rates. This led to intermodal protection problems almost at once, and the Transportation Act of 1940 introduced the concept of a "national transportation policy" to deal with intermodal competition. The policy required the ICC to administer the IC Act in a "fair and impartial" manner that would "recognize and preserve the inherent advantages of each [mode]." The ICC promptly interpreted this language to say that the inherent advantage of water carriage was its low costs, and thus continued its umbrella ratemaking policy. In the Transportation Act of 1958, the rule of ratemaking was amended to eliminate umbrella ratemaking. The ICC was specifically directed not to keep railroad rates high for the purpose of protecting another mode. But ten years later, in the famous Ingot Molds case, the ICC held that fully distributed costs (not variable or out-of-pocket costs) was the proper basis for comparing rail and barge rates, thus preserving barges' "inherent advantage"

and assuring barges of the lower rate and the greater share of the traffic. 323 I.C.C. 758 (1965). The case was affirmed by the Supreme Court. American Commercial Lines, et al. v. Louisville & Nashville RR Co., 392 U.S. 571 (1968).

The 4R Act addressed the problem once again, saying: "No rate of a common carrier by railroad shall be held up to a particular level to protect the traffic of any other carrier . . . ." Although this provision in and of itself is unlikely to have any more effect than its predecessors, and the "inherent advantage" language of the national transportation policy remains intact, the other provisions of § 205 -- dealing with adequate rail revenues -- may effectively preclude the ICC from practicing umbrella ratemaking. Again, however, it is important to note that the IC Act remains inconsistent in this regard, and because the 4R Act did not guarantee adequate rail revenues, or require specific affirmative ICC action to assist the railroads in attaining such revenues, or set a floor below which rail rates could not be lowered by the ICC, the ICC has no more guidance regarding intermodal competition than it did before passage of the 4R Act.

13. Accounting and Costing

A. Accounting

Section 307 of the 4R Act requires the ICC to develop a new "uniform cost and revenue accounting and reporting system" for railroads. The 4R Act requires the new accounting system to provide "the most accurate cost and revenue data," including identification of operating and nonoperating revenue accounts for enumerated items, and requires that costs be assignable to particular functions, services or activities.

On August 2, 1976, the ICC a proposed a revision of the Uniform System of Accounts for Railroads ("USOA"). The proposed revision was identical to one that had been released by its Bureau of Accounts in draft form on March 31, 1976, before the 4R Act was enacted. On June 24, 1977, the Commission published final regulations and procedures, prescribing a new uniform cost and revenue accounting and reporting system for all railroads, making only relatively minor changes in its original proposal.

The new USOA does not comply with the requirements of section 307, and does not, in our opinion, call for the collection and reporting of data sufficient to allow the ICC to perform its regulatory functions adquately. Only through the use of cost center accounting can all of the requirements of the Act be achieved. Under cost center or "responsibility"

accounting, a railroad divides its firm into segments to reflect the geographical area of activity controlled. The lowest level of detail is the cost center, *e.g.*, crew districts, yards, stations, shops, etc. Each cost center is accounted for separately. A cost center is charged with only those expenses that are controllable at the level of that center; apportionments that require arbitrary formulas are unnecessary. Thus, in order to determine most accurately the costs associated with a particular movement or service -- as required by the 4R Act -- one need only collect the appropriate costs at each cost center involved. With a direct cost approach for cost centers, the contribution of relevant centers or groups of centers to the overhead and profit of the firm is ascertainable if revenues are allocated to those centers on some appropriate basis. In an industry with joint or common costs, the contribution approach is the most relevant and is clearly contemplated by section 307 of the Act, which requires such costs to be specifically determinable, and by Section 202, which relies on ascertaining a contribution to overhead in determining whether a rate contributes to a firm's going concern value.

The ICC acknowledged the importance of developing a cost center-based accounting system in meeting the mandate of the 4R Act, stating:

> (W)e ... believe this type of information must be accumulated to meet the requirements of the 4R Act ... Because of the time constraints placed on railroads, by the 4R Act, we have decided to delay implementation of this requirement until January 1, 1979 ... (Report and Order in Docket No. 36367, served June 1, 1977, at 14).

DOT's petition for reconsideration of this decision repeated our conclusion that the ICC must, under the statute, develop cost center accounting by the statutory deadline of January 1, 1978, and argued that sufficient time remained for that to be done. We argued further that the USOA adopted in the Report and Order called for a substantial number of unnecessary and arbitrary data allocations, most or all of which would be eliminated or simplified if cost center oriented accounting were adopted. Only in this way, we argued, would the new USOA conform to the requirement of section 307 that data yielded by the USOA be as accurate as possible, and provide information regarding the direct and variable cost of particular services.

Finally, we argued that the schedules of supporting data that would accompany railroad accounting reports are fundamental to the integrity and completeness of the accounting method. The Commission's Report and Order nonetheless concluded that "Comprehensive revisions of other schedules will be handled in a separate rulemaking procedure next year . . . Id at 21. Since preparation of the data for the schedules

to be reported depends on whether cost center accounting is used, preparation of the schedules will necessarily change when cost center accounting is implemented. Thus, not only was the USOA incomplete, but the railroads are required to incur the expense of collecting and reporting one new set of data now, and a different set in a year or two. This, runs contrary to the requirement of the 4R Act that the revised USOA be "cost effective."

The ICC turned down DOT's petition for reconsideration in all respects, and the USOA went into effect on January 1, 1978 essentially as proposed by the ICC. The Commission has never complied with its promiseto implement cost center accounting by January 1, 1979. In fact, no such proceeding has even been commenced.

B. Costing

The 4R Act requires the ICC to do two things with respect to costing: develop definitions; and establish a methodology for ascertaining the cost to a railroad of performing specific functions. Both of these steps are fundamental to the ICC's ability to perform its regulatory functions fairly, since knowing the cost of providing a service is the *sine qua non* of pricing it properly. In fact, the 4R Act's entire minimum rate regulation concept is premised on ascertaining variable costs, and the ICC's implementation of its maximum rate regulation powers (market dominance) also turns on variable cost.

Nonetheless, the ICC has never defined costing terms or developed a methodology.

With respect to the definitions, the ICC recently proposed a set, and received comments on them from interested parties. 19/ However, definitions alone are not sufficient; formulas for actually deriving the numbers relied on in the definitions are the basics of costing, and formulas are not proposed in the recent ICC proceeding. Thus, even when this proceeding is concluded, little advancement in the state of the art will have occurred.

Although the ICC has never proposed a recommended costing methodology for comment, it has made available a report prepared for it by two large accounting firms. 20/ This report represents a step towards development of an interim costing system that will be usable with the new uniform system of accounts. It should be more reliable than the old costing methodology -- called Rail Form A--in providing "ballpark estimates" of costs for specific traffic movements and for specific operations. It will not, however, provide an accurate measure of the cost of specific services. Rather, the report proposes a way to allocate, on a wholly arbitrary basis, system-wide aggregate costs to specific services. The rules for allocating costs are more complicated and sophisticated than those used

in the past, but are not a substitute for cost information secured from a uniform accounting system that provides information on a cost center and activity basis.

The reason that aggregate data are used is the failure of the new USOA to require specific, cost-center level data. When the USOA is improved, it will be possible to develop far more accurate and specific costing information based on data derived from specific cost centers. The methodology proposed by the ICC contractors yeilds no more than gross estimates of costs that, when disputed, will have to be evaluated in light of more specific cost and revenue data relating directly to the traffic or services in question. Again, the need for the railroads to perform additional cost studies in connection with specific ICC activities (especially ratemaking and abandonments), and the likelihood that the entire costing methodology will change when the USOA does, is wholly at variance with the 4R Act requirement that the new costing system be cost-effective.

Until the remaining accounting and costing work is completed, the regulatory structure will remain premised on faulty and incomplete information. Again, the statute was not as specific as it might have been. For example, some allocation is unavoidable in any costing methodology, but the statute did not expressly require allocation on a cost-and-output - specific basis,

notwithstanding its mandate in section 202 that minimum rate regulation be expressly premised on cost findings. The failure of the Commission to develop more specific accounting and costing units on its own suggests that section 307 must be made more specific.

14. Tariffs

Section 203 of the 4R Act deals with joint rates and through routes, and with rate relationships. The first sentence of section 203 relates to the ability of a railroad either to terminate a joint rate if it feels it is earning inadequate revenue, or to cancel a through route if it no longer wants to carry traffic over a particular routing.

In Fibreboard or Pulpboard, Montana to California, the Commission identified three factors to be taken into account in considering whether to permit termination of a joint rate. The rates could be terminated if the routes that are still to be retained are: "(a) shorter, more direct and efficient than those to be cancelled, (b) less costly, involve less switching, fewer yard interchanges, and shorter transit times than the routes to be closed, (c) more economical and efficient of operation than the routes to be closed." 21/

In Cancellation of Intermediate Routing, Michigan Northern Railway 22/ the railroad industry had applied for a general rate increase but the Michigan Northern Railway declined to participate in the increase. According to the rules for the establishment of joint rates, no change in the joint rates involving the Michigan Northern could occur unless the Michigan Northern concurred. By declining to participate in the joint rate, the Michigan Northern forced all rates

on traffic moving over its lines to continue to move at the old rate. Other parties to the joint rates involving the Michigan Northern, including the Southern Pacific, Santa Fe, and Conrail, responded by applying to cancel joint rates applicable to traffic that moved over the Michigan Northern but neither originated nor terminated on the railroad.

In refusing to allow the cancellation, the Commission concluded that a railroad, by declining to participate in a rate increase, could not only prevent other carriers from participating in the rate increase, but could also prevent them from withdrawing from a joint rate. Thus, a railroad only a few miles long caused traffic to be diverted from other routes by refusing to allow its interline partners to participate in the increase. One reason for this result is the statutory language that allows one carrier to compel a lower rate without giving other carriers the opportunity to cancel participation in the affected joint rates.

The second sentence of section 203 requires the Commission to consider allegations that a change in any rate will change rate relationships. Since it has long been common to challenge rates under section 3 of the IC Act on the basis that a rate change unjustly prefers or prejudices a particular locality, the main function of this provision was to confirm current Commission practice.

The ICC has taken one specific step toward implementing this provision. In the summer of 1978, the ICC's Rail Services Planning Office (RSPO) issued a Preliminary Report on "Rail Rate Equalization To and From Ports." The Report recognized that the ICC had no real "port equalization" policy *per se*, but, rather, dealt with rate issues affecting ports under the discrimination prohibitions contained in § 3 of the IC Act. Technically, "port equalization" is the practice of setting railroad rates at the same level for movements from common inland points to competing ports. To the degree that railroads incur different costs in moving to different points, the railroads absorb those costs.

The RSPO Report noted that while there are equalized port rate structures affecting some Atlantic and Gulf ports, the rates are primarily the result of railroad action, not ICC regulation, although the ICC has approved the resulting rate structures. *See*, *e.g.*, *Export and Import Rates to and from Southern Ports*, 205 I.C.C. 511 (1934), and *Equalization of Rates at North Atlantic Ports*, 314 I.C.C. 185 (1961).

The 4R Act does nothing to change existing ICC policy with respect to port equalization. However, as DOT said in its comments on the RSPO study: "[T]he practice of imposing rate relationships on rail carriers independent of cost and competitive conditions is wasteful of society's resources

and, on balance, damaging to the national transportation system. Therefore, the practice should be eliminated . . ." Comments filed September 25, 1978, at 1. DOT drew the inescapable conclusion that port equalization merely artificially switches cargo among ports, to the benefit of some and the detriment of others. It is, thus, not uniformily beneficial even to the ports. The statute, by failing to address these substantive issues, while drawing special attention to them as a procedural matter, continues unexamined and often indefennible ratemaking practices, and ratifies inconsistent ICC decisions that are often at odds with other 4R policies.

B. Non-Rate-Related Issues

1. Abandonments

The 4R Act repealed the abandonment and discontinuance provisions contained in sections 1(18)-1(22) of the IC Act, which apply to railroads other than those in the northeast, 23/ and substituted a new regulatory scheme. The statute required the ICC to implement the new rules through a public proceeding. That proceeding began on July 30, 1976; a decision was served on November 5; and a second decision, responding to (and denying) several petitions for consideration was served on May 3, 1977. Those decisions were appealed by a group of railroads to the United States Court of Appeals for the Seventh Circuit. On May 30, 1978 the Court reversed the ICC on several crucial points, and remanded the case to the Commission "for further proceedings consistent with [its] opinion."24/ The Supreme Court declined to hear an appeal, and the ICC has not yet acted on the remand.

Thus, as with so many provisions of the 4R Act, we have little basis on which to judge the full efficacy of its reforms. Nonetheless, abandonments are proceeding, and the following data was provided by ICC staff.

From February, 1976 to December, 1978, the ICC received 341 abandonment applications, covering as much as 145 miles each. In all, applications to abandon approximately 7700

miles have been submitted. Of the 341 applications, 120 (covering 4200 miles) are still pending, 6 (189 miles) were denied, 192 (2806 miles) were granted, 3 (37 miles) were partially granted, and 20 (460 miles) were withdrawn or dismissed. The single longest approved abandonment was 144.14 miles, the average was 22.56 miles.

These figures should be compared to a 198,000-mile rail network. Thus, submitted applications cover approximately 3.7% of total rail miles, and granted applications, even less.

The time elapsed in abandonment proceedings averages 259 days each, but the actual time elapsed ranged from 8 to 750 days.

These numbers represent the concrete results of the new abandonment procedures. To understand fully how the abandonment provisions of the 4R Act are likely to work in the long run, however, it is necessary to consider at some length the ICC procedures, and the court opinion reversing them. The Court set out the workings of section 1a as modified.

> Paragraph (1) provides that a railroad may not abandon a line or discontinue any service without first obtaining from the Commission a certificate declaring that the present or future public convenience and necessity require or permit such abandonment or discontinuance. An application for a certificate must be submitted to the Commission, together with a notice of intent to abandon or discontinue, at least 60 days before the

proposed effective date of the abandonment or discontinuance . . . Paragraph (2) requires the railroad to give interested parties notice of its intent to abandon or discontinue.

Paragraph (3) provides that during the 60-day period between submission of the application and the proposed effective date the Commission may on its own initiative, and must upon petition, institute an investigation of the proposed abandonment or discontinuance. If no such investigation is ordered, the Commission shall issue such a certificate, in accordance with this section, at the end of such 60-day period. If, however, an investigation is ordered, the Commission is to order a postponement of the proposed effective date for such reasonable period of time as is necessary to complete such investigation . . . . Paragraph (4) provides that if a certificate is issued without an investigation, the abandonment or discontinuance may take effect 30 days after the certificate is issued. If an investigation is conducted, the Commission may issue the certificate as requested, issue it with modifications or subject to terms and conditions, or refuse to issue it. When a certificate is issued after an investigation, abandonment or discontinuance may take effect 120 days after the certificate is issued. . . .

Subsidization offers are dealt with in paragraphs (6) and (7) of § 1a. Under paragraph (6), when the Commission finds that the public convenience and necessity permit the abandonment or discontinuance, that finding is to be published in the Federal Register. A subsidization offer may then be made. In that event the Commission is to determine within 30 days . . . whether the potential subsidizer . . . is financially responsible and whether the offer is likely to

> (A) cover the difference between the revenues which are attributable to such line of railroad and the avoidable cost of providing rail freight service on such line, together with a reasonable return on the value of such line; or
>
> (B) cover the acquisition cost of all or any portion of such line of railroad.

Upon an affirmative finding, the Commission shall postpone the issuance of the certificate for such reasonable time, not to exceed 6 months, as is necessary to enable

> the potential subsidizer to enter into a binding subsidization agreement with the railroad. . . . The terms avoidable cost and reasonable return are defined in paragraph (11) of §1a. Id at 6-7.

The ICC's regulations permit it, among other things, to postpone issuance of a certificate of abandonment indefinitely (after one has been found to be merited) if a subsidizer offers financial assistance but cannot come to terms with the railroad. The regulations even permit the ICC to reopen the underlying abandonment application. DOT challenged this particular regulation in its petition for reconsideration. citing the ICC's own regulations to the effect that: "The Commission shall not consider an offer of financial assistance or any resulting agreement in making its initial finding on the merits of abandonment ... applications."

The Court held the regulation unlawful, saying: "Paragraph (6) of §1a states that the postponement of the issuance of a certificate is 'not to exceed 6 months.' We do not know how Congress could have made it any plainer..." Since the Court's remand the ICC has issued no new regulations.

It is important to recognize that during the negotiation period (and for any amount of time thereafter that the ICC withholds the certificate of abandonment), the railroad incurs costs in operating the line -- a line that the ICC has already found suitable for abandonment. Thus, the railroad cost reduction feature of abandonments has been substantially lessened by ICC regulation.

The second set of regulations overturned by the Court has to do with computation of "avoidable costs" -- that is, those costs that would not be incurred by the railroad if the line were abandoned. Section 1a(11)(a) of the IC Act defines avoidable cost to include "all cash outflows which are incurred" in the operation of the line, including, specifically, "the current cost of freight cars, locomotives, and other equipment." It is difficult to understand, therefore, why the ICC defined "current cost" to mean that portion of the original (historical) cost allocable to the line proposed for abandonment. The railroads defined current, not unreasonably, as "present." The Court found that the railroads "have the better of the argument." Id at 13. The Court also overturned ICC regulations that "disregard the different costs of equity and debt capital in providing [the railroads] ... return on investment." Id at 23. None of these provisions has been changed by the ICC.

DOT has one further concern about the ICC abandonment regulations that was not brought before the court. The regulations state that upon receipt of a petition to investigate a proposed abandonment, the Commission "shall" initiate an investigation. DOT and others recommended that the Commission require certain minimum information to be submitted with

any such petition so as to minimize frivolous protests and long, expensive, automatic investigations. The ICC refused to do so.

Generally, the regulations are detailed, cumbersome, and confusing. Abandonment applications typically run to one or more volumes, and the proceedings take 1 to 3 years. Further, the basic standard for deciding on abandonment cases -- the public convenience and necessity -- remains undefined and subject to ad hoc and inconsistent ICC decision-making.

The ICC did conduct a proceeding to amend its abandonment rules this past summer -- although this proceeding predated the Court order. The purpose of the new proceeding was to

> issue a statement of general policy describing the way in which [the ICC] would deal with ... abandonment applications in situations where the territory served by the line proposed to be abandoned is also served by other lines which are the subject of pending abandonment applications or have been identified by the railroads as potential candidates for abandonment. Notice dated March 23, 1978 in Ex Parte No. 274 (Sub. No. 2A), at 1.

The ICC's concern was well-placed, since neither multiple abandonments in the same area, nor procedures that result in a race to abandon is good policy. However, the result of this proceeding is yet another investigation, and another overlay of procedural requirements in connection with every abandonment request.

The statute itself has led to many of these problems. The statute requires a multi-stage, complex, lengthy, and expensive abandonment process. Unless the cost savings from

abandoning a line are very great, they can easily be overwhelmed by the cost of seeking the abandonment itself. Conrail, one of the railroads greatly needing to reduce its costs, recently announced that it would defer all abandonment activities for a year in hopes of getting better legislation. Conrail Chairman Edward Jordan was reported to have said:

> Conrail now carries a significant amount of traffic that does not generate a sufficient financial contribution. The regulatory environment impedes corrective action ...
>
> While [ICC abandonment] procedures may suffice for profitable railroads having different plant rationalization needs, the procedures consume too much time and produce too little benefit to be of use ... Further, the costs -- in time, as well as dollars -- of ... preparing abandonment applications are in themselves large and offset the prospective benefits ... Speech reported in Traffic World, December 11, 1978 ed., at 87.

Other railroads have also had recent frustrating experiences under ICC abandonment rules. The Southern Pacific, for example, was recently denied authority to abandon approximately 85 miles of line in California, that had experienced declining traffic, had been washed out in a recent storm, and would cost almost $1.5 million to rehabilitate. Although the ICC Judge agreed that shipper projections about future traffic growth were exaggerated, he concluded that the "future is bright" for the area, and required the railroad to rehabilitate its line and continue its little-used service. ICC Docket No. AB-16. There are many other stories like this, and many

more in which the railroads allege that they have sought only the least controversial abandonments or have simply been discouraged from seeking abandonments at all.

Abandonments should be made simpler, less lengthy, and less costly. Essentially, the statute needs to address only notice and subsidy. In order to be consistent with the rest of the 4R Act the subsidy must cover the total costs of keeping the line in operation, including the opportunity cost of capital tied up in the line. The willingness of a subsidizer to pay the full cost of operation is the true test of public convenience and necesity.

In sum, most of the provisions of the current abandonment statute yield little protection to shippers and communities, and increase significantly the time and cost of abandonment proceedings. Further, the current subsidy provision denies the railroads the opportunity to earn a competitive rate of return.

2. Mergers

Title IV of the 4R Act made extensive changes in Commission procedures for handling railroad mergers and consolidations. The major changes were well summarized in the Report of the Conference Committee on the 4R Act:

> The most significant features . . . are that the Secretary of Transportation is given a significant role as a catalyst in the studying, developing, and negotiating of railroad mergers. Further, the Secretary is authorized and, under the new 'expedited merger proceedings', is directed to appear before the Commission with the result of his studies.
>
> Second, alternative merger procedures, with different standards for review by the Commission, are made available to railroads attempting to merge.
>
> Third, strict time limits are placed upon the Commission for the completion of merger proceedings. 25/

The Conference Committee adopted from the Senate version of the bill[26/] a new merger procedure involving the Secretary of Transportation. As the Conference Committee notes the new provision

> offers to railroads an alternative procedure for seeking approval of a merger that differs in signficant functional aspects from section 5(2) of the Interstate Commerce Act in that (1) the initial planning or review process is undertaken by the Secretary rather than in a hearing before the Commission (however, after the plans are finalized, they are submitted to the Commission for its approval), (2) it establishes public interest as the standard for the Commission's approval of a merger rather than the standards established under section 5(2) of the Interstate Commerce Act, and (3) the Commission is directed to approve, disapprove or modify the application before it, based on the public interest test and without concerning itself with inclusion applications. Conference Report at 175.

Thus the most important of the substantive changes created by the 4R Act is the creation of two separate merger procedures[27/] governed by separate substantive standards and the creation, in section 401, of a process for developing plans for less comprehensive restructuring.

Section 401 states that: "The Secretary [of DOT] may develop ... feasible plans, proposals, and recommendations for mergers ... and other unification or coordination projects for rail services (including ... joint use of tracks or other facilities...) which the Secretary believes would result in a rail system which is more efficient, consistent with the public interest." Section 401 also empowers the Secretary to study cost savings and operating efficiencies that might result from: "elimination of duplicative ... operations and facilities; the reduction of switching operations; utilization of the shortest, or the most efficient, and economical routes; the exchange of trackage rights; the combining of tracking and of terminal or other facilities... and other measures." The Secretary may seek information from the railroads in connection with these studies and hold conferences with one or more railroads for this purpose. Depending on how the proposal is submitted to the ICC, it may be judged under either section 5(2) or 5(3).

Section 5(2) provides that a consolidation proposal is to be approved when it is "consistent with the public interest" and the terms and conditions of the proposal are

"just and reasonable". In determining whether this standard is met, the Commission is required to give weight to the following considerations, among others:

> (1) The effect of the proposed transaction upon adequate transportation service to the public; (2) the effect upon the public interest of the inclusion, or failure to include, other railroads in the territory involved in the proposed transaction; (3) the total fixed charges resulting from the proposed transaction; and (4) the interest of the carrier employees affected. Section 5(2)(c).

The courts have read into the words "among others" a requirement that the Commission also consider the effects of the merger on competitors and on the general competitive situation in the industry in light of the objectives of the national transportation policy.[28]

The phrase "consistent with the public interest" has been construed to mean compatible with the public interest or not contradictory or hostile to the public interest.[29] In assessing the public interest, we note again that the Commission is not restricted to the specific proposal advanced by the applicants. Section 5(2)(d) allows the ICC to consider modifications suggested by opposing parties, including requests for inclusion by another railroad or railroads.

Judging a 401 proposal under these standards results in a long and cumbersome process and, primarily for this reason no 401 proposal has yet been submitted to the Commission.

Even for a minor coordination activity for example, a complete section 5(2) analysis must be conducted. This process is sufficiently long and expensive that even with respect to full-scale mergers, Congress offered the railroads an alternative, expedited procedure in Section 5(3).

As the legislative history makes clear, section 5(3) differs significantly from section 5(2). The initial analysis of a 5(3) proposal is to be made by the Secretary of Transportation, who is directed to study each proposal with respect to the following nine factors:

> (A) the needs of rail transportation in the geographical area affected;
> (B) the effect of such proposed transaction on the retention and promotion of competition in the provision of rail and other transportation services in the geographical area affected;
> (C) the environmental impact of such proposed transaction and of alternative choices of action;
> (D) the effect of such proposed transactions on employment;
> (E) the cost of rehabilitation and modernization of track, equipment, and other facilities, with a comparison of the potential savings or losses from other possible choices of action;
> (F) the rationalization of the rail system;
> (G) the impact of such proposed transaction on shippers, consumers, and rail employees;
> (H) the effect of such proposed transaction on the communities in the geographical areas affected and on the geographical areas contiguous to such areas; and
> (I) whether such proposed transaction will improve rail service .... Section 5(3)(f)(iv)

The Secretary is directed to report to the Commission on the results of this study. The Commission is directed

to give "due weight and consideration" to the report in determining whether the transaction is "in the public interest". However, public interest standards under section 5(2) are not the same as under section 5(3), since, as noted above, the Commission must review each application submitted under section 5(3) on its own merits without concerning itself with inconsistent applications or petitions for inclusion. [30]

The reason for the alternative merger procedure under §5(3) were detailed in the House Report:

> The Committee's Subcommittee on Transportation and Commerce, began this session considering various problems surrounding the bankrupt Rock Island Railroad. One of the major reasons for the plight of that railroad was that nearly twelve years elapsed before the Commission adjudicated whether or not it should be allowed to merge with a strong railroad.
>
> The Committee reorganizes [sic] that to a great extend the plight of the Rock Island is the inadequacy of existing merger provisions. Therefore, Title V of the bill provides an expedited merger procedure with prior evaluation, analysis and assistance by the Secretary.
>
> The changes made in existing law can best be illustrated by comparing existing law with the changes recommended by the Committee.
>
> Under existing law, the Commission would handle each merger through its adjudicative process, and try to accommodate all the conflicting requests of the various groups - the carriers, labor, and the affected communities. Further, any railroad could petition to be included in such merger at any time during the merger proceedings.
>
> This situation brought before the Commission a never-ending series of proposals for inclusions. Further, the Commission does not have a planning staff in which to study the proposed mergers, and therefore remains at the mercy of the railroads, who many times would

> submit an infinite number of petitions for Commission consideration. The Commission would have to deal with the petitions as they were filed, and as the parties appeared before them, rather than attempting to have a period of time in which to study the proposed merger.
>
> Lastly, there are no time limits under existing law in which the Commission is required to complete the merger proceedings.31/

The ICC regulations implementing these statutory changes were published on March 17, 1977, and deal only with evidentiary rules and procedures. No attempt to implement or explain the differing substantive standards was contained in the regulations.

The regulations set up three groups of applications, each having different evidentiary requirements. Group I applications, which have the greatest impact, on the rail system, are those involving two or more Class I railroads. Proponents of these mergers bear the greatest evidentiary burden. The second group involves two or more Class II railroads, or a Class I and a Class II road, and Group III involves trackage rights, joint use or joint ownership of a line, or coordination projects. Most Group III transactions require considerably less evidence than those in the previous categories. A "major market extension" is a Group III transaction that would result in an end-to-end extension of the carrier's routes and service, or in a carrier participating in more

through routes or joint rates. For major market cases, the ICC regulations require the railroads to submit additional evidence.

The railroads argued repeatedly, during the regulation-drafting process, that these requirements were excessively burdensome. And, in fact, in the two merger proposals that have been submitted to the Commission 32/ since these rules were developed (both under the section 5(2) procedures), the required data has filled 4-5 volumes.

Recently, the ICC issued a "general policy statement" governing merger procedures, and purporting to indicate the weight to be given various factors in a merger proceeding. However, the statement is both internally confusing and inconsistent with the overall regulations. Both DOT and the Rail Public Counsel urged the ICC not to issue the statement on the grounds that it would mislead the public and distort the law.

The policy statement sets forth those issues that "The Commission considers ... to be among the most significant factors in determining whether a particular merger proposal should be approved." The factors are:

(1) Retention of essential rail services, whether provided by the merging companies or by other railroads which may be affected by the merger. 'Essential services' include but are not limited to those required by the national defense and those shown necessary to achieve other established goals, such as energy conservation and rural and community development.

(2) Increased opportunities to achieve operating efficiencies.
(3) Elimination of redundant facilities.
(4) Enhanced ability of the merged system to attract new business.
(5) Financial viability of the merged company.
(6) The maintenance of effective intra-modal competition, wherever economic realities make this possible.
(7) Minimum adverse impact on the environment of the region served.

The policy statement originally listed labor concerns as among the most significant. That item was, however, deleted from the final statement for the entirely inconsistent reason that the ICC was already required by the statute to consider labor matters. This makes little sense since the other items listed are, for the most part, covered by the statute also.

The policy statement then contains a section on "public interest considerations" -- apparently a different set of concerns than the eight listed. The statement says only that "the Commission will examine the results which the proposed merger would have on the total rail system and the needs of the users of rail service." The policy statement also contains a section on "merger procedures" that, as DOT said in its comments on the proposal "can be construed . . . to constrain the scope of proceedings far more than was intended by Congress." Further, DOT and the Rail Public Counsel both argued that the selection of some criteria to the exclusion of others is confusing and may result in an unlawful limitation on the issues considered in a merger proceeding.

As always, it would have been far better if the statute itself had spelled out what criteria were to be considered by the ICC and how they were to be weighed. The ICC's attempt to do so has led only to confusion and inconsistency.

3. Per Diem

The ICC has authority over car service activities including "per diem", which is the payment made by one railroad to another for the time a car owned by one railroad is on the tracks of the other. It is extremely important to a well-functioning rail system that per diem payments be set correctly so as to assure that cars keep moving promptly and efficiently. For example, if payments are too small, it may benefit one railroad to continue to use another's cars rather than buy its own.

Section 212 of the 4R Act directed the Commission to revise its rules, regulations and practices with respect to per diem. Specifically, section 212 states:

> It is the intent of the Congress to encourage the purchase, acquisition, and efficient utilization of freight cars. In order to carry out such intent, the Commission may . . . establish reasonable rules, regulations, and practices with respect to car service by common carriers by railroad subject to this part, including (i) the compensation to be paid for the use of any locomotive, freight car, or other vehicle, (ii) the other terms of any contract, agreement, or arrangement for the use of any locomotive or other vehicle not owned by the carrier by which it is used (and whether or not owned by another carrier, shipper, or third party), and (iii) the penalties or other sanctions for nonobservance of such rules, regulations, or practices. In determining the rates of compensation to be paid for each type of freight car, the Commission shall give consideration to the transportation use of each type of freight car, and to other factors affecting the adequacy of the national freight car supply. Such compensation shall be fixed on the basis of the elements of ownership expense involved in owning and maintaining each such

> type of freight car, including a fair return on the cost of such type of freight car (giving due consideration to current costs of capital, repairs, materials, parts and labor). Such compensation may be increased by any incentive element which will, in the judgment of the Commission, provide just and reasonable compensation to freight car owners, contribute to sound car service practices (including efficient utilization and distribution of cars), and encourage the acquisition and maintenance of a car supply adequate to meet the needs of commerce and the national defense.

Pursuant to these requiements, the Commission began Ex Parte No. 334 on November 11, 1976, and proposed adoption of a revised formula for the computation of basic per diem charges.

In its decision in this case the Commission laid out a cost formula that separately identified costs of 15 different types of freight cars. The formula takes into account the transportation use to which the car is put, and the age and the value of the car, and it bases depreciation for each car on the service life and average salvage value for that type of car. Repair costs are based on a 3-year moving average of car repair costs. The cost formula is also intended to account for cost of capital, an issue the Commission has not yet decided, and which will be discussed in more detail below. The ICC has not yet decided the question of compensation for privately-owned cars.

The Commission chose to not consider incentive per diem in its proceeding, concluding, "[I]ncentive per diem is a consideration inapposite to the issues of basic per diem

presented within the scope of this proceeding. Ex Parte No. 252 (Sub No. 1), Incentive Per Diem Charges - 1968, encompasses the issue." It is, therefore, difficult to conclude anything about the efficacy of the incentive per diem provision of section 212. Many people have criticized the current incentive per diem program on grounds that it does not address the basic question of car shortage. (Shortages are more fairly attributable to inadequate revenue and the absence of flexible demand-sensitive pricing rather than inadequate per diem payments). Another criticism is that incentive per diem causes funds to flow out of the rail industry to short-line railroads whose business is not transportation but, rather, buying and sending cars out on per diem.

The cost of capital component of the per diem formula has been particularly controversial. Several railroads filed petitions for reconsideration of the Commission's August decision in this regard, and the Commission agreed to reconsider the issue. The Commission initially concluded that the cost of debt applicable to per diem payments was the cost of floating new debt. It calculated the cost of equity using a "discounted cash flow" methodology that rested on two assumptions: (1) that historically earned return was adequate to attract and retain capital; and (2) that prospective return on investment should be the same as the historical return. Trial computations

demontrated that the estimated under this method varied from more than 20 percent to substantially below 10 percent. DOT suggested that the Commission use a "comparable earnings" measure of the cost of equity capital, and argued that the Commission had confused the cost of existing debt for cars already purchased with the cost of current debt for cars about to be purchased. Since the debt payment associated with a car is an equipment trust, which is directly linked to the car, and the cost continues for the life of the loan, that is the appropriate estimate of the cost of debt capital for cars. Equity capital, on the other hand, is not related to a particular asset and is not fixed by contract. Rather, it is equal to whatever the market determines the cost to be at any point in time. To date, there has been no new decision from the Commission reconsideration.

In general, establishment of per diem payments is an adjudicatory role for the Commission undertaken when the participating railroads cannot agree among themselves. For this reason § 212 is permissive, not mandatory. Since interchange of cars is, however, a vital part of a national rail network, per diem payments will continue and the ICC or some other independent arbitrator will be needed to resolve intra-industry disputes. In this area, the Commission has made a good faith effort to identify the cost of car hire for

purposes of establishing per diem payments in conformity with both the needs of commerce and the dictates of the 4R Act.

4. Demurrage

Demurrage is the term for the payment made by a shipper to a railroad for the time the railroad's cars spend on the shipper's siding for loading or unloading. Typically, a tariff provides a certain number of free hours (usually 48), before demurrage charges start accruing. Section 211 of the 4R Act modified section 1(6) of the IC Act, which gives the ICC authority over car service-related activities such as demurrage, by adding the following new sentence:

> Demurrage charges shall be computed, and rules and regulations relating to such charges shall be established, in such a manner as to fulfill the national needs with respect to (a) freight car utilization and distribution, and (b) maintenance of an adequate freight car supply available for transportation of property.

Just as it is important to set per diem charges in a way that discourages a railroad from holding on to another's cars for a prolonged period, it is similarly important to set demurrage charges at a level that discourages shippers from using rail cars as storage facilities or holding on to them for reasons unrelated to loading and unloading. The per diem and demurrage issues become intertwined when the shipper siding is on the lines of one railroad, but the car being loaded or unloaded belongs to another.

Recognizing the importance of these issues, and their interrelationship, the ICC, in 1972, had initiated a proceeding

to consider whether to require a railroad with another railroad's car on its lines to remit to the car-owning railroad demurrage charges over $10 a day collected by the non-owning railroad.[33/] On February 5, 1976, when the 4R Act was signed, the ICC had not yet concluded this proceeding, although several sets of comments had been received and an Interim Report issued. On February 27, 1976, the ICC issued a notice seeking comment on what effect, if any, section 211 would have on the decision in Ex Parte No. 289. Thus, to understand the impact of section 211, it is necessary to review some pre-4R Act history.

Although per diem and demurrage charges have distinct purposes, both affect the acquisition and availability of freight cars. If either is set too high or too low, economic distortions are created that may lead to over- or under-investment in freight cars and to the use of these cars by shippers and receivers for non-transportation services, such as temporary warehousing of goods. The House Report on the 4R Act makes clear Congress' belief that problems associated with demurrage, car service, and per diem are closely related, and should be dealt with by the Commission in a consistent, coherent way.[34/] DOT argued before the Commission that it was unreasonable to conclude that the 1972 proceeding dealt adequately with the concerns reflected in Sections 211 and 212 of the 4R Act. First, this proceeding had been under way for four

years when that Act was passed. If Congress felt that this proceeding dealt adequately with demurrage problems in light of the overall policy of the 4R Act, there would have been no reason to enact Section 211. Second, this proceeding dealt only with a narrow aspect of demurrage practices. It is clear that Congress desired a simultaneous, comprehensive examination of demurrage, car service, and per diem practices. The pre-existing proceeding made no attempt to accomplish that goal. DOT urged the Commission to suspend Ex Parte No. 289 and undertake a broad investigation to determine the best method for assuring sufficient availability and proper utilization of freight cars. DOT suggested that the ICC consider alternatives as innovative as permitting a market pricing mechanism to set demurrage charges instead of the current system of predetermined, rigid demurrage prices and rules.

The ICC denied DOT's request (saying that it would "only complicate and postpone the Commissions efforts to alleviate car shortages"), simply proclaimed that the rule it had proposed in 1972 would meet the goals of the 4R Act, and promulgated its proposed rule.[35] The basis on which the ICC decided to promulgate the rule (and, presumably, the basis on which it decided that the rule would meet 4R Act goals), was explained as follows:

> As demurrage regulations presently exist, the delivering carrier, who may not own one freight car, is nevertheless entitled to the costs incurred. In addition, there is no indication that this demurrage revenue is presently being used by the delivering road to purchase additional cars. This money is, therefore, a bonus to a carrier who has no interest in whether or not a car is being detained. However, the owner . . . has its equipment detained and unavailable for further use, and thereby loses revenue. 36/

The Commission ignored the fact that its rule provides no incentive to turn cars around more quickly, and ignores also the idea of considering alternatives to regulatory formulas.

To some degree the statute encourages the Commission's narrow viewpoint by focusing only on the Commission's own role in setting rules and regulations, rather than encouraging experimentation with other pricing mechanisms. Given the myriad situations in which both demurrage and per diem prices are set, and the differing needs of particular railroads and particular shippers, formulas and standardized rules could hardly be expected to produce the best result. Thus, the statute addresses only symptoms -- faulty or narrowly conceived. Commission rules -- not the problems themselves.

5. Exemptions

Section 207 of the 4R Act amended section]2(1) of the IC Act by adding a new paragraph, and, indeed, a whole new regulatory concept. Section 207 says:

> Whenever the Commission determines, upon petition by the Secretary or an interested party or upon its own initiative, in matters relating to a common carrier by railroad subject to this part, after notice and reasonable opportunity for a hearing, that the application of the provisions of this part (i) to any person or class of persons, or (ii) to any services or transactions by reason of the limited scope of such services or transactions, is not necessary to effectuate the national transportation policy declared in this Act, would be an undue burden on such person or class of persons or on interstate and foreign commerce, and would serve little or no useful public purpose, it shall, by order, exempt such persons, class of persons, services, or transactions from such provisions to the extent and for such period of time as may be specified in such order. The Commission may, by order, revoke any such exemption whenever it finds, after notice and reasonable opportunity for a hearing, that the application of the provisions of this part to the exempted person, class of persons, services, or transactions to the extent specified in such order, is necessary to effectuate the national transportation policy declared in this Act and to achieve effective regulation by the Commission, and would serve a useful public purpose.

Section 207 does not require the ICC to develop rules and regulations or take other implementing actions. And, in fact, the ICC did nothing whatever on this issue until March 6, 1978 when the Southern Pacific Transportation Company (SP) petitioned the ICC to exempt them from regulation with respect to the carriage of all agricultural commodities that are exempted from regulation (under section 203(b)(6) of the IC Act) when carried by truck.

Notwithstanding the ICC's failure to take action on this provision before, it decided, upon receipt of the SP petition, to develop general rules and regulations regarding exemptions. Thus, on May 31, 1978, the ICC issued an Advance Notice of Proposed Rulemaking, "to obtain the views of all interested persons on the issues involved before the Commission formulates proposed rules or standards governing the scope of the exemption and before it determines how to proceed with an exploration of the issues raised in the SP's petition."37/ Simultaneously, the SP petition was dismissed, with the ICC statement that the issues raised by the SP would be dealt with in the rulemaking proceeding. This action brought a prompt protest from the Office of Rail Public Counsel arguing that the SP was entitled to a hearing on the merits of its petition, and that such a hearing was being unreasonably delayed by the Advance Notice procedure. The Rail Public Counsel argued further that the rulemaking proceeding concerned issues far broader than those raised by the SP, concluding: "The advance notice proceeding is neither legally nor practically a sufficient substitute for the hearing on the SP petition..."38/ These concerns were dismissed by the ICC.

The Advance Notice requested comments on a wide range of exemption-related issues, including: (1) the scope of the exemption statute; (2) whether an exemption should extend

to all common carrier obligations; (3) what information should be submitted in support of a requested exemption; (4) whether an exemption should automatically cover all railroads or be limited to a particular time period; and (5) whether agricultural commodities specifically (the scope of the exemption sought by the SP) should be exempted from regulation.[39]

The ICC received a wide range of views on all these questions. The debate was especially heated on the first issue: the intended scope of the exemption statute. DOT, the Rail Public Counsel, and the SP argued that it was quite broad, and that, subject to the findings required by the language of the statute itself, the Commission may exempt the carriage of any commodity from any or all provisions of the IC Act. The relevant legislative history received considerable attention in this debate.

The Commission itself first proposed the exemption authority, arguing:

> There are many ways in which this exemption authority could be exercised. There may well be many relatively unique commodites such as homing pigeons or race horses, the transportation of which is not likely to have any effect on the maintenance of an adequately stable transportation system. Commodities such as these would be likely candidates for exemption., Also, it could be that certain services, because of their nature, are simply not appropriate for Federal regulation. The services that may fall in this category could include local mass transit motor or bus rail operations that cross state lines and passenger boat operations conducted on bodies of water located in more than one state. There may also be some logical

extensions of presently existing statutory exemptions. Letter of George M. Stafford to Warren G. Magnuson, Harley O. Staggers, and Robert E. Jones, September 12, 1975.

There is no evidence in the legislative history, however, that Congress adopted a view of the exemption authority as narrow as that proposed by the Commission. Indeed, the legislative history suggests the opposite. As finally enacted, the statute contains explicit standards to be employed by the Commission in deciding on an exemption request, expands the list of parties who could initiate exemption proceedings, and adds of a requirement for "full proceedings"[40/] prior to exercise of the exemption authority. Despite testimony by witnesses opposing the Commission's original draft provision[41/] and fears that the provision gave the Commission a "blank check" so that "some years down the line, another group of Commissioners . . . [might be] willing to make wholesale exemptions which would emasculate economic regulation,"[42/] Congress broadened the scopy of the original draft. It added a section empowering the Secretary of Transportation to seek such exemptions [43/] inserted a requirement for "notice and reasonable opportunity for hearing," and spelled out in detail standards to be applied by the Commission. These elaborate safeguards would not have been required for an exemption provision applicable only to racehorses and homing pigeons.[44/]

A particular important section of the legislative history was pointed out by DOT and others as addressing explicitly the agricultural commodity exemption:

> This provision is also addressed to the present inequity of the Interstate Commerce Act which regulates certain commodities for the railroad, but exempts them for other modes. The Committee is particularly desirous that the Commission, by its own action, thoroughly study and review this inequity and take the necessary steps to place the rail industry on equal footing in terms of competition. 45/

Several parties submitted voluminous data tending to show that transportation of fresh fruits and vegetables was highly competitive (the railroads hauling only about 11% of it). Grain data were less clear, showing that in some areas, grain moved predominantly by rail, and in other circumstances predominantly by other modes.

As to the procedural issues raised by the ICC, the bulk of the comments suggested that petitions for exemption should be resolved on a case-by-case basis.

Notwithstanding the fact that the ICC had delayed the SP petition for nine months to begin a rulemaking proceeding, and received comments on the form the rules should take from 132 different parties, the ICC decided, on December 13, 1978 that:

> [G]eneral regulations governing the application of Section [207] are not necessary at this time and might in fact inhibit initiative of petitioning parties...The purpose of section [207] is deregulation under specified circumstances. Promulgating additional regulations, not shown to be necessary...is inconsistent with this basic objective...The statute encourages innovation and experimentation....By further defining the statutory standards in regulations or formulating a general policy...we

> could unintentionally restrict the opportunity for innovative proposals. Since these issues bear directly on the substance of individual petitions, they will for the present be resolved on a case-by-case basis.46/

With respect to the scope of section 207 in general, and the possibility of exempting agricultural commodities, in particular, the ICC referred to the legislative history, and concluded only that the statutory language "does not summarily preclude an exemption of unmanufactured agricultural commodities."47/

The ICC then dismissed the SP petition once again, and initiated a new subproceeding (Ex Parte No. 346 (Sub No. 1), Rail General Exemption Authority - Fresh Fruits and Vegetables), in which it proposed to exempt the transportation of fresh fruits and vegetables, but not other agricultural commodities, from all ICC regulations except those related to accounting and reporting. The exemption would be nationwide and would cover all common carrier obligations for an indefinite period. Thus, the commodities covered were more limited than those proposed by the SP, and the scope of the exemption sought by the SP was broadened by including all railroads.

As to other agricultural commodities, the ICC concluded: "While [an] inequity exists with regard to all agricultural commodities which are exempt from regulation for other modes...the record does not support the requisite statutory findings for an exemption..." The ICC failed to consider the explicit statement in the House Report that the ICC itself should

investigate the need for an exemption for all agricultural commodities, and failed also to consider that a rulemaking proceeding was not the appropriate forum for gathering the needed data. The ICC should, at a minimum, initiate its own investigation into exemption of grain and other agricultural goods. Although the ICC notice covering fresh fruits and vegetables says that petitions would be accepted with respect to such goods, in view of the legislative history the ICC must take more affirmative action.

Of equally great concern is the statement in the ICC Notice that market share data must accompany any exemption petition. This suggests that such data will be conclusive -- a far narrower standard than contemplated by the statute. Since other ther agricultural commodities will not be addressed until another petition is received the SP's request continues to ignored.

The complex substantive and procedural issues raised (and then dismissed) by these ICC actions are the inevitable result of piecemeal deregulation. The foot-in-the-door theory leads many to oppose any exemption even if their own interests are not directly affected. The ambiguity of the statutory standards led to needless controversy about the scope of ICC authority. The failure of the statute to address procedural questions and the handling of the SP matter, create yet another

ad hoc ICC process. Finally, further thought needs to be given to the commodity approach of the statute. A comprehensive approach to the question of when regulation is needed would be more productive. That approach necessarily involves identifying circumstances, not goods, in which the public would (or would not) be fully protected by the regulation of the marketplace -- and substituting that for regulation by bureaucracy.

<u>Footnotes</u>

<u>1</u>/ Section 202(f) of the 4R Act provides that none of these ratemaking changes shall be construed to modify Sections 2, 3 or 4 of the IC Act (prohibiting undue discrimination, preference or prejudice), to make lawful predatory or other anticompetitive practices, or to affect existing law governing rate relationships between ports and equalization of rates within a port.

<u>2</u>/ That Congress wished to afford rail management wide latitude in upward rate revisions is clear from both the House and Senate Reports. The House Report spoke of a "substantial increase" in flexibility. Report of the Committee on Interstate and Foreign Commerce, U.S. House of Representatives, on H.R. 10979, Report No. 94-725, dated December 12, 1975 ("House Report"), at 69. The Senate Report spoke of flexibility sufficient to allow the railroads to "increase their revenues and attract the resources necessary to revitalize the industry..." Report of the Senate Committee on Commerce on S.2718, Report No. 94-499, 94th Congress, 1st Session, dated November 26, 1975, ("Senate Report"), at 11.

<u>3</u>/ Report of the Committee of Conference on S.2718, Report No. 94-595, 94th Congress, 2d Session, dated January 27, 1976 ("Conference Report"), at 148.

<u>4</u>/ Senate Report at 10, 11.

<u>5</u>/ House Report at 76.

<u>6</u>/ Notice of Proposed Rulemaking, Ex Parte No. 320, <u>Special Procedures for Making Findings of Market Dominance as Required by the Railroad Revitalization and Regulatory Reform Act of 1976</u>.

<u>7</u>/ Section 202 explicitly required the Commission to solicit the views of the Department of Justice and the Federal Trade Commission before promulgating market dominance rules.

<u>8</u>/ <u>Atchison, Topeka and Santa Fe Railway Co. v. ICC and United States,</u> 580 F.2d 623 (D.C. Cir., 1978), at 629.

9/ The demand-sensitive rates approved include: (1) corn, soybeans and wheat, between points in North Carolina, December 1976; (2) Limestone, ground or pulverized, between points in the Southern Territory, August 1977; (3) Whole grains and soybeans, from, to, and between points in the Southern Territory including Illinois and Indiana, September 1977; (4) Whole grains and soybeans, from Southern Territory, Illinois and Indiana origins to Florida, Gulf, South Atlantic, and Virginia Ports; also from specific origins in the Southern Territory to Norfolk, Virginia, September 1977; (5) Limestone, from Hodges and Jefferson City, Tennessee to Cordele, Georgia, May 1978; (6) Limestone, from one town in Alabama, and several towns in Tennessee to Gibson Junction, Jimps, and Waynesboro, Georgia, May 1978; (7) Limestone, between points on the Southern Railway System, June 1978; (8) Grain and related commodities for domestic and export traffic from Chicago and Northwestern Railroad origins, June and October 1978; and (9) Residual fuel oil from Colorado to Chicago, Illinois, Milwaukee and Lake, Wisconsin, and St. Paul, and Minneapolis, Minnesota, November 1978.

10/ Notice of Proposed Rulemaking, Ex Parte No. 324, Standards and Expeditious Procedures for Establishing Railroad Rates Based on Seasonal, Regional or Peak-Period Demand for Rail Services.

11/ The decision the Commission reaffirmed is Inspection in Transit, Grain and Grain Products, 349 I.C.C. 89 (1975). The Department acknowledged that the 4R Act did not explicitly overrule the decision. We argued, however, that the thrust of the Act, particularly those portions aimed at generating additional revenues for the railroads, necessitate limiting application of the case to fact situations essentially similar to that of the case itself.

12/ Ex Parte No. 327, Rate Incentives for Capital Investment.

13/ Docket No. 36612, Incentive Rate on Coal--Gallup, New Mxico to Cochise, Arizona, November 28, 1977; (Cochise); and Docket No. 36608, Incentive Rate on Coal -- Cordero, Wyoming to Smithers Lake, Texas, November 30, 1977 (Smithers Lake).

14/ National Association of Recycling Industries v. I.C.C., 585 F. 2d 522 (D.C. Cir., 1978).

15/ A "local rate" is a rate published from an origin on a particular railroad's lines to a destination on that same railroad's lines. A proportional rate appled between an origin and a destination on a single railroad's lines and the traffic either originated or terminated on another railroad's lines. In the absence of a joint rate, traffic moving over two roads would move on the sum of the local or proportional rates.

16/ Report of the Commission, Ex Parte No. 338, Standards and Procedures for the Establishment of Adequate Railroad Revenue Levels, served February 3, 1978.

17/ The adopted regulations allow the Commission to authorize departure from the procedural and evidentiary provisions where warranted (49 CFR §1109.25(b)(8)). After several unsuccessful attempts to develop a funds flow projection, the Commission concluded that it could not issue a funds flow projection for use in the first annual revenue adequacy proceeding. Notice in Ex Parte No. 353, served July 21, 1978.

18/ Report in Ex Parte No. 338, at 17.

19/ Definitions are proposed for: "going concern value;" "variable costs;" "costs of capital;" and "incremental costs." Notice of Proposed Rulemaking, Ex Parte No. 355, Cost Standards for Railroad Rates, 43 Fed. Reg. 46877 et seq., October 11, 1978.

20/ This work was done for the ICC by a joint venture composed of representatives of Deloitte, Haskins, and Sells, and Peat, Marwick, & Mitchell & Co.

21/ Decision served July 29, 1977.

22/ Investigation and Suspension Docket No. 9179 served August 29, 1978, and Investigation and Suspension Docket No. 9179 (Sub-No. 1), served October 19, 1978.

23/ Abandonments on the Northeast railroads are covered by provisions of the Regional Rail Reorganization Act of 1973.

24/ Chicago and Northwestern Transportation Co. et al v. ICC and United States, Commonwealth of Pa. Intervenor, Nos. 76-2283, 77-6008 and 77-1487, decided May 30, 1978, at 33.

25/ Conference Report at 174.

26/ The Senate bill (S. 2718) is contained in the Senate Report at 209-309.

27/ Sections 5(2) and 5(3) of the IC Act, as amended by the 4R Act (but not as recodified).

28/ United States v. I.C.C., 396 U.S. 491, 504 and 519 (1970); McLean Trucking Co. v. United States, 321 U.S. 67, 83-87 (1944). However, both the courts and the Commission have recognized that insistence upon preservation of maximum competition among rail carriers is no longer essential to the protection of the public interest.

29/ Seaboard Air Line R. Co. - Merger - Atlantic Coast Line R. Co., 320 I.C.C. 122 (1963), at 130.

30/ Conference Report at 175.

31/ House Report at 62.

32/ The two pending cases are: a merger application from the Burlington Northern and St. Louis-San Francisco RRs, and a joint application by the Chessie and Norfolk and Western RRs for control of the Detroit, Toledo & Ironton RR. This latter application has been contested by the Green Bay & Western RR who has filed an inconsistent application to acquire the D,T&I as well as the Detroit & Toledo Shore Line RR.

33/ Ex Parte No. 289, Remittance of Demurrage Charges by Common Carriers of Property by Rail.

34/ The House Report states, for example:

> The Committee recognizes that better freight car utilization can significantly help to increase the financial viability of the rail industry . . . . The bill requires that rules and regulations be established . . . for the computation of demurrage charges so that freight car utilization is maximized and car owners receive adequate compensation. It is anticipated that one effect of adequate demurrage charges would be a radical decrease in the use of railroad cars for storage purposes. House Report at 73.

35/ Report and Order of the Commission on Further Hearing, 353 I.C.C. 567 (1977).

36/ Id. at 589.

37/ Advance Notice of Proposed Rulemaking Ex Parte No. 346, Rail General Exemption Authority, served May 31, 1978, ("Advance Notice") at 4. The use of the Advance Notice format signalled further delay by the ICC in acting on the SP petition, since an advance notice cn lead only to a notice, not to a rule or regulation.

38/ Docket No. 36868, Petition of the [SP] for Exemption..., Response of the Office of Rail Public Counsel to Administrative Appeal of [SP], July 10, 1978, at 9.

39/ Advance Notice at 5-7.

40/ Senate Report at 53.

41/ See, e.g., testimony of John A. Creedy, President of the Water Transport Association, Hearings before the Subcommittee on Surface Transportation of the Committee on Commerce, United States Senate, Serial No. 94-31 (1975), at 2006.

42/ Testimony and letter of Peter T. Beardsley, Vice President and General Counsel, American Trucking Associations, Inc., Id., at 1992, 1994.

43/ If Congress intended only "unique" commodities like homing pigeons and race horses to be exempted from regulation, it seems highly unlikely that it would have encouraged the Secretary of Transportation to initiate §207 proceedings under his general planning authority for all modes of transportation.

44/ For a fuller discussion of the legislative history of the exemption provision, see the Comments of the Office of Rail Public Counsel, Ex Parte No. 349, August 7, 1978, at 10-13.

45/ House Report at 75; emphasis supplied. The Conference Report states (at 153) "the conference substitute follows the House provision . . . ."

46/ 43 Fed. Reg. 58305 et seq. at 58305.

47/ Id. at 58306.