The Transportation Company: An Economic Inevitability

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The basis of the so-called transportation problem which has plagued the nation for some years is the uncoordinated and excessively competitive operations of transport agencies subject to diversified regulatory acts, different commissions, and unrelated promotional activities. Until such time as a coordinated transportation system is organized to function under integrated regulation, revisions will serve primarily as palliatives.

Solutions put forth in recent years usually revolve around four proposals or combinations of these proposals. These are (a) consolidation of administration under one regulatory body, (b) the merger of regulatory and promotional activity, (c) uniformity of regulation for all transport agencies, and (d) a selective overhaul of the existing pattern with a view to placing greater emphasis on competition and less on control. In spite of the differences in these approaches, all have one characteristic in common—they assume that the solution will be found within the existing framework of interagency competition under some degree of regulatory control.

This paper points out that effective competition between the existing media is a delusion, for the conditions precedent to such competition are lacking. Further, extensive competition and extensive regulation are in themselves contradictory.

It is suggested, then, that the ultimate solution may lie in a change in the economic structure of the firms offering transport service, which will eliminate interagency competition and provide a basis for uniformity of such regulation as might be required. These transportation companies would utilize all or several forms of transport. The management of such companies should be in a position to select the means of transport best suited, from the standpoint of service and economy, for the various operating and demand situations encountered. The transportation company, therefore, is an agency in which coordinated transport service can be effectively accomplished.

• THE TRANSPORTATION SYSTEM is and has been during the entire postwar period the subject of intensive investigation of governmental bodies, transport agencies, and academicians to determine the effectiveness of regulatory policies and practices in promoting sound transportation. Consequently, a great deal of literature has been devoted to the delineation of transportation problems and the formulation of solutions to these problems. Opinions vary as to the nature and importance of these problems. The author has been convinced for over a decade that the primary source of the difficulty is the uncoordinated and excessively competitive operations of transport agencies which are subject to diversified regulatory acts, different commissions, and unrelated promotional policies. Until such time as a coordinated transportation system is organized to function under integrated regulation, revisions in transport regulation will serve as palliatives, at best.

A number of solutions for the transportation regulatory problem have been put forth in recent years, ranging from the simple to the complex. The principal areas in which solutions have been sought have been (a) consolidation of regulation under one administrative body, (b) uniformity of regulation for all transport types, (c) the merger of regulation and promotional activity, and (d) a selective overhaul of the existing regulatory practices in order to place greater emphasis on competition and less on control. A common theme, and common weakness, is evident in each of these approaches in spite of other differences. All assume that an adequate solution can be found within the existing framework of interagency competition under some degree of regulatory control.

Since most Americans are dedicated to a competitive economy, looking with favor upon developments that strengthen the competitive concept and with disfavor upon those which tend to weaken it, interagency competition between transport media fits the basic economic philosophy. It will be proposed, nevertheless, that an adequate, lasting solution will not be found within the framework of interagency competition. It is suggested that the cure for the principal ills of transportation will be found not so much in changes in regulatory practices as in the economic structure of the subject regulated. It is proposed that companies utilizing all forms of transportation should replace the separate operating types of rail, motor, water, and air that now exist. Possibly pipelines should be included. It must be remembered that many of the major pipelines are essentially private in operation, even though they may be chartered as common carriers. Hereafter, such multimedia firms will be spoken of as "transportation companies."

There is a substantial minority which has come to feel that the regulation of transportation has completely outlived its usefulness. Although most do not take so extreme a position, it is true that regulatory activity is seldom popular and, for this reason, legislation affecting transportation has not been the result of careful, long-range planning but a sometimes ill-designed creation based on expediency and custom. Furthermore, the parties concerned become adjusted to existing regulatory patterns over a period of time, the regulation takes on an aura of finality, and anything other than minor repeal and revision becomes exceedingly difficult.

The transportation system of today is not a simple structure. In addition to the well-developed common carrier systems in rail, water, motor, air, and pipeline transport, there is extensive use of contract, exempt, and private carriage. All of this has given rise to a multimedia competitive structure in transportation with which existing regulatory bodies find it increasingly difficult to cope.

A thorough examination of the Interstate Commerce Act, the Federal Aviation Act, and other applicable legislation lies beyond the scope of this paper. It is more pertinent to enumerate some of the more troublesome areas of variation and inconsistency in regulation and promotional activity as applied to the several carriers. No attempt will be made at this juncture to justify or condemn such variations.

1. There is no uniformity of regulation. Even the Interstate Commerce Act is divided into separate parts, with varying treatment of the agencies so regulated.

2. One of the most noticeable distinctions between rail and other forms of transport is the recognition of several classes of the latter; that is, common, contract, private, exempt, and the like. These variations are a major source of difficulty in control of transportation.

3. There is no single regulatory agency. Furthermore, the regulatory policy is not coordinated with promotional policy, although each has critical bearing on the other.

4. The intent of Congress seems to be the compulsion of more competition between the transport agencies, without at the same time abandoning regulation designed to preserve individual competitors. In this respect, the problem is somewhat similar to that encountered in the anti-

trust field, where the same two objectives come into conflict.

The amount of success in eliminating these trouble spots and achieving the necessary coordination of transport depends upon the role assigned to interagency competition and the weight to be given efficient allocation of resources to and among the various means of transport.

No lasting solution will be found within the interagency competitive framework. The agency approach to transport operation and regulation, where the several modes of transport are considered as separate entities, is not adequate to deal with present day situations. Of the questions faced by Federal and state regulatory bodies—not to mention the carriers themselves—probably the most pressing is that of competition between the different forms of transportation, each with specific characteristics which give certain cost and service advantages and disadvantages in relation to the others, as well as overlapping features which make advantages and disadvantages less pronounced.

Except for use as a working model, the idea of perfect competition plays little part in modern economic analysis. The majority of economists feel satisfied if there are enough buyers and sellers, together with some opportunity for entry and withdrawal, to assure reasonably dynamic allocations. To function satisfactorily, competitive conditions of this sort should effect, insofar as the transportation system is concerned, the following achievements: (a) allocate resources between transportation and other industries, (b) allocate transportation resources between the various media, and (c) allocate the services of each transport media in the most effective way.

Concerning the first point, such allocations in the economy are not fully effected by competitive forces. In the absence of government financial assistance, which by and large has been no greater to transportation than to several other segments of the economy, the transportation firms would have had to attract capital on the same basis as anyone else. But it must be recognized that public aids extended to transportation cause some distortion. This complex subject lies beyond the scope of this paper, but it suffices to say that competition has not been the sole basis for the fundamental allocation of resources between transportation and other economic activity.

The allocation of resources between the media of transport and between the firms within a given media is not completely dependent upon competitive conditions either. If a non-transportation firm finds its scale of operation too small for effective production, it may, subject to its financial limitations, expand its operation and sell over a wider area. A common carrier does not find this so easy to do because its territorial operating rights are definitive and permission to expand may not be forthcoming from appropriate regulatory bodies. If useful techniques are developed by the non-transportation firm's competitors (techniques, perhaps, that partially or completely outdate existing methods), the firm would adopt the improvements as rapidly as possible. But transportation firms are rigidly delineated and common carriers of a given mode, although free to adopt new techniques that apply to their type of transportation, are prevented from branching into other forms of transportation.

The efficacy of the individual common carrier is not allowed to resolve itself under competitive conditions with others of its own kind. Common carrier rates between points served by competing lines are ordinarily published by conferences or bureaus. Although the individual carriers may abstain from such tariffs, as a practical matter this is not feasible, so weak carriers may get business as readily as strong ones and circuitous routes may be used as frequently as direct ones, for in either case the rate is the same. The rate is not necessarily geared to the cost of the most efficient carrier. It may and frequently does reflect averaging or umbrella rate-making. Furthermore, controlled entry protects to a considerable extent the vested interests of common and contract carriers. Certainly these firms need not fear the unrestricted onslaught sometimes encountered outside the field.

Since it is apparent that conditions prerequisite for effective competition are lacking in transportation, what results can be expected from competitive pricing among the several agencies of transport? The most hoped for accomplishment is that a more rational allocation of transportation resources would result. The author has serious doubts about the certainty of this occurrence. First of all, there cannot be effective competition in conjunction with regulation. The terms are in themselves contradictory. The regulation of prices and control of earnings by public authority, if followed consistently will, for obvious reasons, undermine a competitive structure. So long as firms are not free to enter and leave an industry at will, to expand whenever the management deems it necessary, or to imitate the methods and devices of more successful modes, a "competitive rate" cannot be relied upon as an economic rationing device. Of the alternatives to the existing method of handling interagency competition, greater reliance upon competitive rate-making is a delusion.

If transportation companies were to be formed, what desirable effects could be expected to accrue? Foremost among these is the removal of the interagency conflicts that now exist between the several modes of transport. At least this would be true of such conflicts as they relate to common carriers. Those associated with contract, private, and exempt carriers would remain unless regulatory policy is changed to restrict such transportation to that which is actually contract, private, or exempt, as the case may be. Among those problems of an interagency nature that should be eliminated or mitigated are, first, the controversies over the effects of the minimum rates of one type of carrier on the traffic of another. Rate cases today are less frequently disputes between shipper and carrier than issues between competing media of transport. Second, an integrated company would make possible uniformity of regulation. It is doubtful that any regulation will ever be fashioned to the complete satisfaction of the carriers involved, but all would be treated alike. Third, with the elimination of interagency competition, the pressures for promotional policies that could tend to enhance the position of one mode of transport at the expense of another would be lessened.

The transportation company offers the only effective medium through which coordinated transport service can be maximized. With the element of interagency competition eliminated, the incentive for most economical operation will dictate the maximum in interchange and substitution of equipment, rather than the minimum. The same may be said for joint routes and joint rates.

The transportation company holds much promise for a more efficient use of transportation resources. There are three ways in which this might be accomplished. One is the elimination of the waste and duplication which the separate agency approach generates. The amount may be debatable, but the waste and duplication is there. Another source of saving is in public aid. It is not suggested that public aid to transportation be eliminated, but it does seem feasible that the total might be reduced under the integrated approach. Finally, there is the matter of economies of scale. Studies have shown that transport efficiency is not a function of size alone, for route structure and density of traffic have greater impact (*1, 2*). For that matter, mere size alone is not the most important characteristic of the transportation company. It is the ability to eliminate duplication and exploit a coordinated transportation system. Troxel (*3*) has expressed the idea in this fashion:

> Concerned with coordination as a transport purpose, organizers must exclude competition—both price and service-quality competition—as a primary public purpose. This is an unhappy choice for some organizers—a particularly unhappy fact among the public men in North America who are attached

> to their many experiences in competitive relationships. A belief in competitive transport organization persists. It is a hope among consumers, legislators, and some regulators—a hope for alternative choices between techniques, as well as between firms with the same technical form. But it is antithetical to a coordinated organization which is concerned with interfirm operations and makes selective choices between technical means. This belief is also antithetical to a transport process that is directed to efficient allocation of resources rather than to price and earnings control of separate firms.

Even the most devout advocate of the transportation company cannot overlook a number of problems that would arise in the operation of such firms, nor the barriers to formation which could prevent the creation of such companies for a considerable period.

One of the most frequently voiced objections is the fear one or several media might be suppressed within the integrated company. This stems from the belief that the organization would be rail dominated, and it must be noted that there is good basis for this assumption. A large rail system would, in all probability, bring the greater amount of assets into the consolidated firm and, as a result, acquire controlling portion of the stock. There are two forces working to diminish this possibility. The financial position of many rail carriers is deteriorating. At the same time, consolidations in the motor carrier field have created some sizable operating firms. Even if the bargaining position of other carriers were not improving, it seems unlikely that bias by the management for one media over another could be successively passed to subsequent managerial groups over a period of time.

> The fear that some express that if railroad companies were permitted to engage in other forms of transportation they would proceed at once to throttle competition, regardless of transportation economies, seems unwarranted. A railroad company, converted to a transportation company, would still be interested in maximum profits. If it proved cheaper to send certain commodities or for that matter all traffic by truck, or bus, or airplane, or boat, as the case may be, such companies would be shortsighted indeed if they failed to use the alternative agencies (*4*).

Another aspect of this same fear is that a transportation company, even though it might use the existing modes of transportation economically and without discrimination between types, might, once entrenched, suppress the development of transportation innovations and media that might have an obsolescent effect on existing investment. If this were not done, it would run contrary to the lessons of transportation history, for the dominant type has always harassed the newer media, sometime with a great deal of success in the short run, but never in the long run. The answer to this problem is the same as it has always been. The independent operation of the innovation as a separate type, with the assistance of public aids and promotion, until such time as sufficient development has occurred for the new form to take its place in the family of transport media.

With the element of interagency competition removed, what incentive will management have to increase the efficiency of operations, either through more economical use of existing techniques or the introduction of innovations? The lack of interagency competition does not necessarily imply the absence of competition. Competition between the transportation companies themselves could be permitted by the means of overlapping territories. While this competition might create problems similar to those encountered in the utility field, at least the structural basis of effective competition would exist. If competition between such firms is not allowed, a more direct monetary stimulant might be provided through the institution of some sort of continuous earnings control under which earnings in excess of what is considered adequate, if such earnings result from increased efficiency, would be shared by both the company and the users of the service.

The weaknesses of the transportation company notwithstanding, probably the most formidable barrier to the transportation company is the difficulty of formation. Although any of the obstacles would be difficult to overcome, probably the most troublesome would be the philosophical objection to the elimination of the interagency competition. There is also the antagonism of the management of the several types of transport to the formation of integrated companies except on their own terms, namely, a dominant position in the firm. This same feeling for the preservation of interest is undoubtedly shared by the several governmental agencies associated with various media of transportation. Finally, there are the legal barriers. The statement of national transportation policy would have to be rewritten and either some amendment to antitrust law or the passage of enabling legislation would be required.

In the face of such opposition, under what circumstances can transportation companies conceivably be established? One possibility is the purchase of the required properties by a holding company formed for the purpose. Such action would have to be preceded by the legal modifications referred to above. It is a means of overcoming the reluctance of the separately operated companies to consolidate. Another approach is the removal of restriction on ownership of competing forms. This change has the most significance for railroads, for the other types are hardly in a position to institute railroad carriage. There is some indication that if transportation companies are ever formed they will evolve in this manner. The rail carriers are campaigning vigorously for the privilege of pursuing this course, although it is quite possible they waited 30 years too late. One last suggested possibility is the acceleration of consolidation of similar forms of transport, such as has been taking place in the mergers of motor carriers and those of air carriers. Once sufficient size is achieved, these firms might be more easily merged with rail and water carriers to form transportation companies.

If transportation companies are to be formed, what is the proper climate for their operation—controlled competition or exclusive territorial operating rights? If the first condition prevails, some of the conflict between competitors which currently exists would continue, but effective regulation should be more easily achieved than at the present time because of the structural homogeneity of the firms involved.

It always requires a great deal of soul searching for an economist of orthodox training to advocate monopoly, even controlled monopoly. Still, this appears to be the inevitable solution to the formation of an economic and coordinated transportation system, and the author proposes that the transportation companies operate under these conditions. They would, in effect, be treated as a public utility. The change is not as marked as it might appear at first glance. Common costs would continue to be allocated on a demand basis and rates would still be related to the value of the service as long as such value was above out-of-pocket cost. Earning control would keep the general rate level within reasonable bounds, and the commission power over individual rates would care for specific instances of unreasonable or discriminatory charges. The only thing missing under the regional monopoly would be the fiction of allocation of resources by interagency competition.

If some reliance on competition is insisted upon, then the transportation companies could be granted overlapping territories as were the rail carriers. The activities in these competitive areas would have to be regulated, but the regulation could be uniform and consistent.

It is evident that existing regulation is unsatisfactory in many respects. It is also apparent that the transportation system is not achieving its maximum economic potential. Expressions from industry and congressional leaders indicate that the need for remedial action is recognized. This action will probably manifest itself in revision of the Interstate Commerce

Act. As a minimum, some patching of the most obviously inadequate or outmoded provisions, such as those relating to the long and short haul clause, private and exempt motor carriage, and rate suspension powers of the Commission can be expected. As a maximum, greater reliance may be placed upon interagency competition, with a change in regulatory policy to effect it. Neither policy will provide a completely workable answer because of the nature of the transportation industry. The industry's characteristics will not permit more than a minimum amount of competition without undesirable after-effects. On the other hand, regulatory control is made difficult by the heterogeneity of the carriers subject to Commission jurisdiction.

The ultimate solution may lie in a change in the economic structure of the firms offering transportation service, which will eliminate interagency competition and provide a base for uniformity of regulation.

A change of the sort proposed in this paper would be most difficult to effect. Still, the transportation company has much to offer from a regulatory and economic standpoint. Further thought might well be given to the transportation company as a long-run solution to the transportation problem.

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