DEREGULATION AS A SELECTIVE PROCESS:
THE AGENDA FOR REFORM IN THE
U.S. BUS AND RAIL INDUSTRIES

by

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INTRODUCTION

For several years, the idea that U.S. industries are over-regulated has been taking hold among legislators and the general public. If outdated and burdensome red tape were to be eliminated, the thinking goes, industries would be rejuvenated. Long-buried market signals would begin to clean out dead wood and summon innovative services to life. Market discipline would replace both the caprice of any one generation of regulatory officials, and ossified, decades-old rulings.

This view of deregulation presupposes, however, that existing regulatory structures can be dismantled at once, and with considerable neutrality as to the outcome. If the market is to take effect -- blindly and without prejudice -- in industries where to date its influence has been curtailed, then deregulation must also be a blind process: a complete undoing of old rules without attention to the effects on specific firms, specific groups of industrial or household consumers, Congressmens' political status with their constituents, or any segment of the economy which might be adversely affected.

In frequent recent attempts by policy analysts, economists and other commentators to evaluate the early results of deregulation, insufficient attention has been paid to the reality of deregulation. Not only has it been far from complete and instantaneous in the affected industries, but of course it has not been neutral either. Factional pressures from affected industries, consumer groups, regional

interests, and above all, specific firms, have prevented the full exercise of the deregulation concept in one instance after another. The rhetoric of deregulation, however, continues to inspire participants in regulatory reform debates and to cloud the public view of what deregulation really means in any one case. "Greater efficiency," "lower costs," "heightened competition," "innovation" -- each supposed attribute has a heady sound and together these concepts continue, in a most abstract manner, to convince the wary that deregulation is, on principle, a sound development, and perhaps more importantly, that deregulation has in fact been taking place.

Without attempting to judge the concept of pure deregulation, or the merits of any specific regulatory reform proposal, this paper seeks to examine the selective nature of recent reforms as they have developed in two transportation industries, the intercity bus industry and the rail freight industry. In both cases, it appeared that deregulation would only partially strip away established patterns of government-backed privilege or government-enforced denial that have shaped both the behavior, and the composition, of the industries. In each case, the particular shade of deregulation was instead consciously chosen, as if from a palette of possible hues. And the shades have not been permanently fixed, but are subject to revision by the same set of artists now painting the initial designs.

Since deregulation in practice consists of careful adjustments, it would be useful to gain a better understanding of how those adjustments are shaped, or planned. This paper focuses on the agenda, or public dialogue, concerning regulatory reform in the bus and rail industries, and specifically, on the types of arguments bus and rail

industry officials use to promote certain reforms and block others. A detailed examination of the officials' motives, their publicly aired reasoning, and their use of popular concepts can help to explain the ultimate choice of reforms (or implementation procedures) which emerge from Congress and the regulatory agencies. While industry officials are not the sole participants in public discussion about deregulation, they are generally able to set the terms of discussion, and to greatly restrict the range of alternatives considered. Hence it is important to examine the way in which industry rhetoric conditions the planning of deregulation. This is not, however, a comprehensive political analysis; I have not kept score of the political actors who won and lost, although it is sometimes obvious. The legislation discussed here is relatively recent and subject to interpretation; and in the bus case, it is still being formulated. Therefore it would be premature to specify winners. Instead, I have focused on the arguments bus and rail officials use in their attempts to selectively influence the direction of regulatory reform: how and why were they chosen? What effects did they have on the proceedings, and with what apparent consequences for policy development?

Two types of arguments are particularly common, and both appear influential. In the first type, which I have called social utility or social policy arguments, the companies stress the public services they now perform, or could perform given favorable regulatory reforms, as justifications for their positions. Social utility statements are often, though not always, rhetorical facades, not well tied into the reform proposal. For instance, a rail firm may cite its energy efficiency record as a reason to block a merger that could put the

firm out of operation, when energy use is irrelevant to the matter at hand. In the second type of argument, which I call business fairness arguments, either individual firms, industry segments, or spokesmen for the industry as a whole justify their regulatory proposals with reference to what seems fair from their point of view. These arguments incorporate such notions as handicaps for underdogs; equal chances for success; favors deserved on account of harmful rules suffered in the past, or corporate bad luck; and seniority rights for veteran firms. On occasion, social utility arguments and business fairness arguments are linked. For instance, Greyhound Lines cited a long record of quality service in Ohio as a reason for regulatory concessions which would preserve the company's monopoly there.

Regulated firms use both types of arguments to narrow the terms of debate over regulatory reform. They may do this 1) by absorbing most of the time and attention available for discussion, which is possible for those firms with superior resources; 2) through superficial discussions based on catch-words, when detailed analysis and dialogue would be more appropriate; and 3) by limiting the range of issues considered through repetition of a few, powerful concepts.

The firms' dominance of the public agenda does not automatically mean that business interests will be served, or public or consumer interests abandoned, in the course of bus and rail deregulation. The firms frequently do not share a unified position on deregulation, and intra-industry conflicts are often so severe that the narrowing of the agenda comes about precisely because their conflicts take up all of a Congressional committee's attention. Still, business-oriented viewpoints and the vocabulary of business conflicts tend to emerge with

greater clarity than broader public or consumer issues.

Even with the discussions framed in terms that industry spokesmen select, one cannot simply assume that the ensuing legislation will do positive harm to bus passengers, rail using firms and workers, transportation employees, other firms, or the physical environment. A regional railroad may argue for permission to lower its rates, and thus be able to serve area farmers more inexpensively. Or a bus firm may seek to make deregulation contingent on capital funding to improve its stations, and thus provide greater comfort to passengers. But business representation of public needs is clearly a haphazard process, at best. Business domination of the regulatory reform agenda can result in an impressive recitation of social concerns, but a fairly shallow ability on the part of federal personnel to articulate or explore them. And while it may not be possible in the cases here to demonstrate positive harms, it is evident that little public scrutiny has accompanied the planning of deregulation. Congress has explored few alternatives to the status quo arrangement of benefits and restrictions in each industry. In the long run, business control over the vocabulary of policy-makers may be the most significant remnant of the original transport regulatory system for these two industries.

This project focuses on transportation industries because these were test cases, in a sense, for the concept of deregulation as it emerged in the 1970s. A movement to deregulate the intercity transportation service industries began to take shape during the Nixon administration, and has been gathering steam more recently. Congress passed legislation to deregulate airlines, trucking firms, railroads,

and intercity bus companies between 1978 and 1982. In addition to these legislative projects, federal administrators have made many changes in the way they implement earlier laws throughout the 1970s, which together can be characterized as a regulatory reform movement. Deregulation was not strictly a new concept: regulatory reform efforts have been proposed in the transportation industry for several decades, and the Transportation Act of 1958 attempted to reduce the scope of federal regulation. But the recent legislative changes constitute a more visible departure from past policy, and currently occupy the attention of many transportation policy analysts, lobbyists, and managers.

The bus and rail industries are, of course, quite different. The rail industry has a longer history, a much more prominent place in U.S. economic and political history, and is much more complex than the bus industry. But both industries have been regulated in a similar manner, by the same institutions. They offer some instructive comparisons, since they represent both passenger and freight transportation. Each has been considered a declining industry for a long period of time, yet has remained subject to a stable regulatory framework until very recently.

In exploring the deregulation agenda in each case, I reviewed hearings, trade journals, academic and government reports, and several conference transcripts. The rail case also makes use of testimony from Interstate Commerce Commission rate and merger dockets. Each case begins with a brief profile of the industry, current market trends, and a discussion of regulatory practices that form the historical background for the current policy debates. I then discuss de-

regulation in the context of overall policy towards the industry, and trace the rationales firms use to argue their positions. The bus case focuses primarily on a single piece of legislation now being considered in Congress, while the longer history of rail deregulation permits consideration of a sequence of reform efforts beginning in the early 1970s. This difference affords a more detailed look at intra-industry variation in the bus case, and a more dynamic perspective in the rail case.

The final chapter compares the two cases in order to make general conclusions and suggest situational factors that may account for several differences observed in the firms' lobbying strategies, their motives for favoring a particular form of deregulation, and for developing specific arguments. The comparison incorporates both economic and political factors, some relatively stable and others changing. The chapter also sketches out several questions that merit further thinking and research, including the role of external interest groups in shaping the public agenda for regulatory reform; potential comparisons with other industries; the influence of concurrent policy changes; and the connection between industry rationales and broader currents of thought.

CHAPTER ONE:

DEREGULATION OF THE U.S. INTERCITY BUS INDUSTRY

INTRODUCTION

A movement to deregulate the intercity bus industry began about 1976. In 1977, the Interstate Commerce Commission (ICC) started to grant route permits more liberally than it had in the past, spurred on by pro-regulatory reform personnel in the Carter administration. In the next few years a struggle developed over what form legislative deregulation would take. The U.S. House passed a deregulating measure in 1981, and deliberations are coming to a close in the Senate. Considering the rhetoric which has surrounded the concept of deregulation, the emerging legislation might be expected to overturn a full set of government-backed advantages and obligations, putting the industry in a pure market mold, and creating both significant new profits and a rash of bankruptcies. To all appearances, however, the changes will be modest, and new rules--carefully protective of the status quo--will replace many of those eliminated.

From the industry's point of view, the key issue at stake has been the prospect of alterations in the existing system of state and federal route franchises. This system has aided some firms (including Greyhound Lines) but hinders others (including small entrepreneurs). Discussions of bus industry deregulation in Congress have emphasized intra-industry conflicts over the route franchises, and a related regulatory superstructure. A range of consumer concerns, such as service quality,

safety, and fare levels, has also come up on Congress, but on a more limited basis than might be expected. Bus company managers tend to raise consumer issues when they mesh with the firms' political positions on the route franchise system. The firms, and several industry lobbies, also stress what each views as fair treatment vis a vis the other segments of the industry. Each wants a slightly different form of deregulation, and some firms do not really want deregulation at all.

Since Congressmen and regulators hear bus company viewpoints much more often than those of passengers or the general public, their perception of the issues is heavily influenced by industry presentations. Not only do they tend to consider franchise reform primarily a question of business impacts, but even when attending explicitly to broader policy issues--such as the place of intercity bus services in a hypothetical nationwide energy-conservation scheme, or in facilitating rural mobility--Congressmen and public officials readily borrow the concepts and symbols put forward by industry leaders. The narrowness of the resulting debates, often unsupported by critical investigation, makes it difficult to evaluate the proposed legislation from a broad public policy standpoint.

This discussion will explore the way bus firms have shaped the agenda for regulatory reform, using popular ideas as well as direct pressure, and their motivations for doing so. A profile of the industry is followed by a short history of bus regulation. The discussion then turns to the beginnings of deregulation and the role of industry rationales in shaping legislation. A concluding section sketches the social implications of defining bus deregulation as government and industry have together done, and suggests the type of consumer issues

that have been excluded from full consideration in this process.

BUS INDUSTRY PROFILE

Market

The approximately 1100 U.S. intercity bus carriers serve a small proportion of long distance travelers. By any criterion, the vast majority of intercity travel is by private auto. It is often said that auto travel is the bus services' chief competition, rather than airline or rail travel, but this depends on the particular location and route in question. Distance, of course, is a major factor and the airlines are increasingly able to win over former bus patrons for longer distance travel. In some cases, bus services compete with discretionary household activities, including local recreation, rather than other forms of transportation *per se*.

On a nationwide basis, the three carrier modes (bus, rail, and airlines) are not close substitutes. The rail system is much less extensive, covering under 500 lcations. Most rail service is concentrated in the Northeast. By contrast, in 1980 the bus system covered 14,600 locations and also served approximately 50,000 flag stops.[1] Intercity bus service is available in almost all metropolitan areas and in 96 percent of towns 2,500 to 5,000 in population.[2] Bus patronage tends to be concentrated on shorter trips than either rail or airline patronage (see Table 1).

Since the modes occupy different, though overlapping, markets, aggregate statistics on bus market share give only a crude indication of the bus industry's competitive ability. They do show, however, that the bus niche is small, and that auto travel has made major inroads into the bus market. Depending on the indicator chosen, the bus "share" of the intercity travel market lies somewhere between 1.8 and 6.0 per-

TABLE 1: Average Intercity Trip Length by Mode

Mode	One-way trip length*
Intercity bus	125 miles (198 km)
Rail	226 miles (359 km)
Air	714 miles (1133 km)

*excludes trips under 100 miles (159 km) one-way

Source: National Travel Survey 1977

cent, as Table 2 shows. The 1977 National Travel Survey, conducted by the U.S. Bureau of the Census, placed the bus market share at 2.5 percent.[3] On a revenue basis, the industry earns approximately twice the revenues of Amtrak and 6 percent of those earned by the airlines.

The bus market share has been falling steadily throughout the past few decades. For instance, in 1950, bus carriers served 4.5 percent of person-trips nationally; this has fallen to 1.8 percent today.[4] On a geographic basis, no region depends on the bus for more than 5 percent of its intercity person-trips. Busses account for 5 percent of person-trips in the Middle Atlantic region and under 3 percent in the West and South.[5]

Scheduled bus ridership levels are inversely related to auto ownership.[6] A significant portion of bus riders have no regular access to automobiles, are unable to drive, or underage.[7] Travelers with access to automobiles seldom choose to travel by bus. (Marketing studies consistently find that bus travel has a strongly negative public image.[8]) The scheduled bus services thus operate on the fringe of the other modes, especially autos. Hence, slight changes in auto ownership levels, gasoline availability, license-holding or demographic composition of a region can have major effects on bus industry revenues.

In addition to scheduled routes, many bus companies operate charter and tour services. The large firms also provide package express, mail delivery, and other incidental services. Most bus companies see charter service as an important revenue source. Charters typically involve longer trip distances and much fuller busses than scheduled route service. Consequently, profit margins are higher. Bus companies operating both scheduled and charter service can frequently

TABLE 2: Bus Share of Intercity Travel Market

Mode	Person-Miles[a]	Person-trips[b]	Passengers[c]	Revenues[d]
Bus	6.0%	1.8%	360,000	$1.4 billion
Auto	48.6%	95.9%	NA	NA
Rail	0.9%	0.2%	19,000	$0.7 billion
Air	44.5	2.1%	216,000	$22.8 billion

[a] Oak Ridge National Laboratories, 1978

[b,c] ICC, 1975

[d] Management Analysis Center, Inc., 1979

TABLE 3: Percent of intercity travelers female or low income, by mode, 1977

	Percent with household income under $10,000	Percent female
Bus passengers	60%	61%
Auto travelers	41%	46%
Rail passengers	38%	47%
Air passengers	22%	36%

Source: American Bus Association, 1977 Annual Report

use the same vehicles for either service, switching uncommitted busses from one service to the other, depending on relative demand. For instance, during the gasoline shortages in 1974 and 1979, major bus carriers added unused charter busses to their regular routes in order to expand their capacity.[9]

Passenger Characteristics

The bus-riding population differs significantly from the traveling population as a whole. Riders tend to be under 20 or over 50 years old. (Only one-third of bus passengers are between ages 18 and 55.[10]) Sixty-one percent of bus riders are females, compared to 36 percent of air travelers. Twenty percent are non-white.[11] More retirees and fewer professionals ride the bus than other intercity modes. Although experts disagree on the extent of car ownership among bus passengers, some estimate as many as 70 percent are unable to drive.[12] Many have low incomes or are unemployed, and approximately 30 percent are non-metropolitan residents.[13]

While business travel forms 20 percent of all intercity travel, only 12 percent of bus trips are business-related. The majority of bus travel consists of trips to visit friends or relatives. In the industry, this is known as "VFR travel."[14] Consequently, a small proportion of scheduled bus passengers visit tourist establishments or stay in hotels at their destination, in comparison to rail and air travelers.[15] Not surprisingly, the intercity bus patrons are not politically organized on a nationwide basis, in contrast to rail and airline passengers. According to former ICC Chairman Daniel O'Neil, bus passengers

> are not wealthy individuals by and large. They tend to be very young or...very old. They are the individuals who, probably more than any others in society require somebody else to intercede for them. They are not knowledgeable, and in the rate cases we have had before the Commission, I don't think we have ever seen anybody that has been a user of the system come forward...They would not know what to do if they could appear to protest the rates.[16]

Industry Structure

The industry is dominated by Greyhound Lines, Inc. and Trailways, Inc., with about 65 and 21 percent of the nationwide market, respectively.[17] The remaining 14 percent is controlled by approximately 1100 smaller firms, which range from family-owned independents to large-scale regional systems. The Interstate Commerce Commission (ICC) regulates 750 of these firms: those whose services cross state lines. State public utility commissions regulate the remaining (intrastate) carriers, as well as the intrastate routes that the 750 ICC-certified carriers serve. An unknown number of unauthorized ("gypsy") carriers escape regulators at both the state and federal levels. Industry regulation, which is described in more detail later on, includes control of fares, routes, schedules, insurance, speed limits, and equipment specifications. (The industry uses a basically standard sized vehicle nationwide, serving both rural and urban areas, and lower and higher volume routes. Highway conditions in all but a few rural areas permit use of full-sized Greyhound busses.[18])

The bus industry is highly concentrated. ICC regulations distinguish between bus firms with revenues over $3 million annually (Class I) and smaller firms (Class II and III). Class I carriers must submit more detailed financial data, for instance. In 1977, 46 bus

firms--4 percent of the firms in the industry--qualified as Class I carriers. As Table 4 shows, these firms controlled 70 percent of the route operating authority (franchises) on a mileage basis, and earned 74 percent of the revenues.

Smaller firms operate most of the charter service, while Class I firms concentrate on scheduled service and package express delivery.[19] Charter and tour services provide approximately 30 percent of the industry's overall revenue, and 16 percent of Class I revenues, but only 10 percent of Greyhound's revenue.[20]

In general, intercity bus companies do not engage in significant marketing or demand-forecasting activity. Industry expenditures for marketing rose significantly during the 1970's, but managers still emphasize day-to-day operations over long-range service planning. The industry sets fares through a single nationwide rate bureau, the National Bus Traffic Association.[21] There are two formal lobby associations, the American Bus Association and the National Bus Owners' Association, as well as several informal trade groups.

TABLE 4: Intercity Bus Industry Structure, 1977

	Class I	Class II and III
Number of firms	46	1104
Percent of firms in industry	4%	96%
Passengers	37%	63%
Passenger-miles	64%	36%
Bus fleet ownership	40%	60%
Route-miles of operating authority	70%	30%
Gross operating revenues	74%	26%

Source: American Bus Association, 1977 Annual Report

CHANGING CLIMATE

The bus industry has undergone a number of changes that affect bus firms' regulatory interests. These include the decline of older markets and the availability of new ones; the financial decline of the industry overall, with some exceptions; and relevant changes in the other intercity modes.

Decline of older markets

Demographic changes have restricted the size of the scheduled bus market. As noted earlier, the bus industry primarily serves persons with limited use of automobiles. The portion of U.S. households fitting this description continues to shrink, even in the lowest income brackets and among the students and retirees customarily forming a major part of the bus market. Drivers' license holding among the elderly, for instance, has significantly increased over the past two decades.[22] Population shifts to lower density parts of the country, and to suburban residences, have also removed a substantial part of the population from proximity to bus terminals. The companies are seldom permitted to move terminals to suburban locations to accommodate this shift.[23]

General economic decline also lowers demand for conventional bus services. Past recessions provide some evidence that bus travel is more sensitive to the state of the economy than travel by other intercity modes. This probably stems from the higher than average vulnerability of discretionary travel in low-income budgets. It may also be due to bus riders' greater susceptibility to unemployment, due in part to their unusual age distribution.[24]

Although demand for intercity passenger transportation has grown

by approximately 1.3 percent per year since 1970, the number of bus passengers has declined an average of 1.5 percent per year.[25] Bus industry revenues grew an average of 6.7 percent between 1970 and 1977 in current dollars, compared to 14.4 percent for the three carrier modes overall. Since 1970, the bus industry share of total carrier revenues has dropped from 9 percent down to 5 percent.[26] Industry statistics show that the year 1974, when gasoline was temporarily in short supply was

> The only point between 1970 and 1977 that ridership did not decline. By 1977 ridership had dropped 17 percent below the 1970 level.[27]

In addition to the growth in auto ownership levels, average intercity trip lengths have increased in recent years, tending to promote air travel.[28] Partial deregulation of air transportation in 1979 produced airline price wars in several regions, which have eroded some bus carriers' former price margins.[29] It is also possible that the federal speed limit reduction to 55 mph (87 kph), undertaken in 1974, resulted in some loss of bus patronage.

Availability of new markets

The charter and tour markets, as noted earlier, have been growing steadily, partially compensating for the decline of scheduled service on an aggregate industry basis. From 1950 to 1980, charter and tour revenues rose from 7 percent of industry revenues to constitute nearly half (48 percent) of industry revenues.[30] According to the ABA, between 1970 and 1977 charter revenues grew 177 percent.[31]

Demographic factors again help to explain the increase in demand

for charter services. The shift to lower density land-use patterns (both inter- and intra-regionally) promotes intermediate-distance organized travel in the range between comfortable driving distance and economical scheduled bus or airline services. Intercity charter operators have been taking over functions once served by local charter firms. For instance, in Texas, many high schools use intercity, rather than metropolitan, charter busses to transport their athletic teams. The same is true of church groups and other voluntary organizations throughout the Southwest.[32] Arizona and Texas have minimal patronage of public transportation services in comparison to the Northeast, but bus tours are growing very rapidly in those states.

Significant demographic developments are also transforming the tourism industry, with implications for tour service. According to one travel industry analyst, tourism is becoming more "wholesale" than retail in its orientation.[33] Organized tours have higher prestige than they once did, and a higher proportion of young people are subscribing. An influx of foreign tourists also stimulates demand for bus tours. (In 1980, for the first time, more foreigners came to the U.S. to visit than Americans went abroad.) Hotel profits have increased in many regions, creating an incentive for joint ventures between bus tour operators and resorts.[34]

Aggregate financial decline

The bus industry as a whole has experienced a financial decline since 1970. From 1970 to 1979, operating margins for Class I carriers declined from 11.5 to 4.8 percent. For the 600 members of the American Bus Association, operating margins fell from 9.9 percent to 5.4 per-

cent during the same period.[35] Revenue per passenger-mile increased 67 percent against a 98 percent increase in the Consumer Price Index for 1970-1979.

In addition to the decline in scheduled bus demand, cost increases have contributed to the reduced overall profits. The cost of new busses has risen significantly in real terms since the late 1960s.[36] Carriers claim they have not been able to replace equipment as rapidly as in the past. For instance, Trailways Vice President D.V. Taylor noted in a 1980 hearing that his company has been

> unable to replenish our bus supply satisfactorily. A continuation of this unsatisfactory situation will lead to deterioration in the quality and quantity of bus service available to the public.[37]

Varied implications for bus firms

Not all bus firms have experienced low profits in the past decade. Among Class I carriers, 1979 operating margins in 1979 ranged from -4.5 percent (for Lincoln Transit) to 22.8 percent (for Kerrville Bus). In the Southwestern region, operating margins averaged 10.5 percent in 1976, in contrast to 4.5 percent for the U.S. Greyhound Lines' profits are close to the industry average. (The low proportion of charter revenues probably explains why Greyhound Lines is no longer among the most profitable bus carriers. Greyhound has focused primarily on conventional scheduled routes.)

The climatic market trends discussed above affect bus firms in different ways. For instance, airline deregulation raised short-distance air fares on lower volume routes, relative to long-distance fares.[38] Bus firms serving those routes benefited from airline

deregulation, while those serving more competitive airline routes (where fare wars have taken place) have suffered. The shift in relative demand from scheduled service to charters has favored many small bus firms without significant scheduled route obligations, while threatening others with bankruptcy. These market variations are significant for understanding the firms' positions on deregulation and will be discussed further. Because of market differences, the industry cannot be said to have a single interest, or position, with respect to federal policy.

REGULATION: THE FRANCHISE SYSTEM

The initial regulation of the intercity bus industry took place in several waves from 1910 to 1935. Regulation began on the state level with certification programs. Early state regulation focused on safety standards and equipment specifications (for instance, bus weight limits). But fare and market regulations were quickly added: all but one state (Delaware) enacted bus market regulations between 1913 and 1930.[39]

Bus firms promoted market regulation, rather than resisting it.[40] They formed statewide organizations during the early 1920s, in part to advocate route restrictions which would prevent further crowding of the field.[41] State governments typically responded favorably to the demand for route regulation, in order to promote stable profits and protect consumers from unnecessary service disruptions. While the route regulations (or franchises) tended to serve the interests of well-established firms, they also created an instrument for protecting bus passengers from inordinate fare increases. Franchise rights could, for instance, be denied to firms with poor service records.

In many states, early market regulations were a form of reciprocity between government and bus firms. Firms took on less profitable routes, maintaining low fares in exchange for monopoly or franchise status within state borders. The magnitude of these tradoffs probably varied among states, and has not been established. State regulatory commissions tended to endorse bus company mergers, which further consolidated the hold of successful franchise operations within states. (Mergers increased the length of routes that a single carrier could serve with one ticketing system.) Throughout a long period of

consolidation, Greyhound Lines was in most states the firm most suc-cussful in acquiring other bus companies.[42]

By the 1930's, more bus passengers traveled between states, and interstate services proliferated. Interstate routes were still without protection. (In 1925, the Supreme Court ruled that states could not regulate interstate markets.[43]) The spectre of "destructive competition," or overcrowding, was now encountered in the interstate markets, and established investors experienced declining profits.[44] The bus industry began to put pressure on the federal government to create a franchise system for interstate routes as well. The trucking industry participated in this lobbying effort. (A parallel development had occurred in trucking.) The Motor Carrier Act of 1935, the first federal legislation to regulate these two industries, was the federal response to these pressures for route protection. The Act was only secondarily a consumer protection program.[45]

The Interstate Commerce Commission successfully implemented the Motor Carrier Act to protect existing interstate carriers from new entrants. Applicants for interstate route authority were now required to show that their services were "responsive to a public demand or need" and could be "served without endangering or impairing existing carriers contrary to the public interest." Generally, the ICC found impairment when applicants' proposed services would divert passengers from the original service--whether or not the diversion was likely to damage the company's standing.[46] Like entry regulations in many other industries, the Motor Carrier Act had a conservative effect, in this case literally "conserving" Greyhound Lines on many major routes.

Regulation and Greyhound

Since Greyhound is dominant among bus carriers, and a major lobbyist in the deregulation proceedings, the company's regulatory history deserves special mention. Greyhound began in 1925 as a holding company for several southern and midwestern firms. Within a few years, it began acquiring other bus companies. In 1933, it merged with two other holding companies to form a unit of 45 former bus companies in total.[47]

Favorable economic conditions and increasing trip distances contributed to the success of the corporation's acquisition program. Greyhound Lines established a comprehensive marketing strategy, with foreign sales offices and through-ticketing arrangements similar to those now used by airline companies:

> In 1932, Greyhound established sales offices abroad... (By) 1948, they had 600 sales agencies abroad. Foreign travel agencies were commissioned to sell Greyhound tickets to travelers so they would be ready to board the bus when they arrived in the United States. Greyhound also established the first national bus network which enabled through-ticketing arrangements. For the first time, passengers could purchase one ticket for a route that required riding several carrier lines.[48]

Greyhound's early success was in part the product of good timing: the Motor Carrier Act granted antitrust immunity to the industry when Greyhound was in the best position to benefit from it.

Greyhound Lines is now part of a $4 billion vertically-integrated holding company, Greyhound Corporation, which manufactures approximately 70 percent of the intercity busses sold and used in the United States. Greyhound Corporation also owns a majority of U.S. bus terminals, leasing space to other carriers. Bus service forms only a small part

of Greyhound Corporation revenues:

> As one of the top 100 of the nation's Fortune 500 corporations, (Greyhound Corporation's) biggest profit-making activity is its computer leasing. In addition, it owns Armour Hotdog, Apian Way Pizza, Burger King, and other food processors/retailers, as well as Dial and Tone Soaps and Traveller's Express Insurance.[49]

The ICC and state regulatory agencies did not actively discourage Greyhound's early acquisition movement, nor its subsequent diversification. At the state level, Greyhound has routinely testified that its mergers and purchases would reduce costs and result in lower fares to passengers.[50] Several state regulatory agencies have adopted Greyhound's argument themselves, using it to defend decisions favorable to Greyhound in state legislatures.[51]

Contrasts and similarities in state and federal posture

It is worth briefly considering the difference between state and federal regulation of the bus industry in order to appreciate the deregulation agenda to be discussed shortly. Although the state and federal regulatory agencies have created similar franchise systems for bus firms, each system advances a somewhat different set of interests. Statutes permit both the ICC and the state commissions some discretion, so that rules may be applied either for industry or consumer benefit, where the two conflict. The ICC tends to have a sympathetic posture towards the industry in general, and Greyhound in particular. State regulators, on the other hand, have frequently interpreted their statutes from what may be considered a consumer advocacy position.

With respect to fares, for instance, decades of relatively lax

oversight at the federal level and stricter, consumer-oriented rulings at the state level have produced a large difference between interstate and intrastate fares on a per-mile basis. One study found that in 1979 interstate fares were on average double those permitted on corresponding intrastate routes, on a per-mile basis, despite cost similarities between the two types of services.[52]

Most state governments have required bus companies to make internal cross-subsidies from more lucrative routes and services to less profitable, or in some cases unprofitable, services. Charter and tour permits are granted conditional on the applicant's willingness to undertake "public service" routes as well. Similarly, states often withhold permission to operate more lucrative scheduled routes in urban areas unless companies agree to serve rural areas as well. These provisions are similar to those of the Rural Electrification Program. In contrast to state regulators, the ICC does not need to impose many cross-subsidies of this type. Few interstate routes are completely unprofitable.[53] The ICC also looks more favorably on service abandonments and new charter applications than do the states.[54]

Despite these general tendencies the labels "pro-business" and "pro-consumer" are reductive and do not accurately describe state and federal regulation. Since the ICC's decisions (particularly on entry and exit) affect the relative position of bus firms as much as the industry's overall welfare, the agency inescapably damages some business interests as it upholds others. And a decision in favor of the bus industry, or its most powerful firm, Greyhound, is not necessarily damaging to consumers, or potential consumers. The states' ability to facilitate transport or tourism through bus policy is, however, circum-

scribed by the adversary regulatory system. The only forms of consumer protection authorized by statute are denials of industry initiatives: fare increases, schedule changes, and service abandonments. States are not generally involved in positive planning or funding of bus services. Only past arrangements--and hence those consumer needs which have remained constant--can be protected. For instance, state commissioners cannot ensure adequate bus service between suburbs in two adjacent cities. They must wait for petitions to come in, from firms that believe the services would be profitable. It is difficult for states to force new cross-subsidies on the industry: maintaining the status quo is the norm in many states. And as bus company managers are fond of pointing out, preserving low fares--mandating fare decreases in real terms--can ultimately lead to service degradation.[55] State regulations thus have an uncertain consumer impact.

Another reason why the "pro-consumer" appellation often given state policymakers is unsatisfactory is that the state governments do provide indirect services to bus operators. And although the federal government subsidizes the bus industry only indirectly, nine states have created modest subsidy programs for intrastate services. The assistance includes bus purchasing and financing, public terminal construction, and terminal improvement funding.[56] Most states also continue to protect established firms against new entrants, including new charter firms, preserving the long-standing bargains described above. Thus both federal and state regulation aid segments of the bus industry against external and internal threats. And both are more favorable to the status quo arrangement of privileges than to alternative conceptions of either consumer or business welfare.

DEREGULATION: THE REFORM AGENDA

The Interstate Commerce Commission developed a strong interest in deregulating the bus industry in 1976, when it began to grant entry and exit permits on a more relaxed basis. In a 1978 policy statement, the agency announced that it would disregard a key protective requirement imposed in 1935. As mentioned earlier, the protection stipulated that route applicants had to prove proposed services could not be performed by existing carriers. In its announcement, the ICC claimed that this "adequacy test...has outlived its usefulness, and it will no longer be applied."[57]

Both the Carter and Reagan administrations have supported the concept of federal legislation to further deregulate the industry. Several pieces of legislation have been introduced in Congress that would preempt state power over intrastate routes and fares. Since the state regulations form the most significant controls on the industry, full deregulation cannot be accomplished without preemption. Congress has given most active attention to a bill the ICC introduced in 1980. The U.S. House passed a modified version of the bill in 1981. The Senate is still considering the bill. The Reagan administration has not taken a formal position on the House bill, and is reportedly interested in working with Congressmen for a more sweeping measure.[58]

The ICC bill reduces entry and exit requirements and preempts state authority to do so. It also establishes greater fare flexibility, and removes anti-trust immunity from joint fare setting. (Joint fares are the fares quoted on trips involving a transfer between carriers.) It would also triple minimum insurance coverage from its current level of $500,000 to $2,000,000, with provisions for the Secretary of Trans-

portation to grant exceptions.[59]

Most state governments are against the federal legislation, as would be expected since it reduces their powers. Some states, such as Arizona and Florida, however, have taken their own initiative in deregulating the bus services under their jurisdiction. Florida deregulated bus services in 1980, in part to promote service to resorts that were suffering reduced patronage as a result of high fuel costs.[60]

During the past few years, as deregulation has become a popular issue, bus companies have taken different sides on the matter. When the ICC first began to relax entry standards, many bus firms objected, fearing that their routes would be confiscated. Greyhound was among the firms protesting what it called "arbitrary administrative deregulation." The company called for total legislative deregulation, to ensure uniform treatment of cases. (Uniform treatment of <u>cases</u>, would of course be different from uniform treatment of <u>companies</u>, since Greyhound dominates the market.) Although the American Bus Association has come out in favor of the House compromise, it initially opposed deregulation. The lobby introduced a limited reform proposal which would not have preempted state route authority.[61] But once the strength of deregulation as a political concept, which of course extended beyond the transportation industries, became apparent to all parties, the bus carriers' tactics shifted. They concerned themselves with shaping the course of deregulation to fit their needs, rather than simply opposing it.

The struggle to shape the specific provisions under which government would "return the bus industry to the free market" suggests that deregulation does not always, nor perhaps generally, signify a cessation of government involvement in the industry. Instead, deregulation

created an opportunity for joint public and private re-planning of the market. It appears that secular changes in demand or costs--market signals--form a backdrop for the joint planning that is called deregulation. Government is sensitive to market cues, such as declining demand and profits, in the industries it regulates. Because the federal government cannot easily stimulate demand, these exogenous conditions do form a boundary of economic feasibility for regulation. But within the boundary, a great variety of solutions can be developed. In the process, other governmental objectives enter in, such as the desire to update service; to satisfy powerful lobby groups; or to conform to a general precept that regulation is unnecessary. The outcome of deregulation is managed to a significant degree by this joint political process.

A key element in the bus deregulation process is the industry's use of political rationales. Bus industry representatives have largely managed to control the terms of dialogue on deregulation as a public policy, using two different kinds of rationales. The first set draw upon an ethic of business fairness. The second set includes public service rationales. Some of them are nearly as old as the industry itself, and have been used in numerous policy debates in the past. For instance,

- "The U.S. has the best bus system in the world."[62]
- "We provide for vital transportation needs not served by any other mode."[63]

Others were invented expressly for use in the deregulation hearings. The industry's repertoire of rationales ranges from its record of ser-

vice to the poor and handicapped* to, more recently, energy conservation. By coupling these themes of service to its business ends, the bus industry has significantly shaped public perception of bus policy issues. The industry also bases many of its policy arguments on demands for equal treatment (whether in regulation, taxation, or subsidy) with Amtrak and the airlines. Equal treatment also forms an important theme for intraindustry disputes, as each firm sets forth what it deserves from deregulation.

Within the general pattern of fairness and service rationales, each element of the industry advances slightly different arguments. Each emphasizes different public missions and standards for equitable treatment. This is because each group seeks to use governmental authority in a different way. Taken together, their arguments have given the Congressional agenda a narrow and business-oriented cast, since public concerns mainly enter it in a rhetorical manner.

The wider social significance of bus services is not lost on bus executives. For instance, when George Snyder of Greyhound Lines testified before the Senate Governmental Affairs Committee on Tourism and Energy in 1979, he pointed out that busses were the most energy efficient form of intercity transportation, and that the rate of return on equipment was falling. This threatened to increase the average age of fleet, which he claimed was a key determinant of passengers' willingness to try the bus. Finally, he indicated that travel and tourism

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*Several carriers have a policy of permitting handicapped passengers to bring an assisting person on the trip at no extra cost. The offer is seldom utilized,[64] and therefore costs the companies little, while being publicly well-received.

support 5 million jobs in the U.S., that tourism is "one of the top three industries in almost all 50 states," and "contributes over $20 billion to the economy."[65] Snyder implied that special favors to the bus industry would capture additional passengers, helping the industry serve a tourism function and preserving jobs vulnerable to energy prices as well.

Congressmen often adopt similar conceptual links between firms profits and their ability or willingness to serve social functions. Senator Russell Long testified in 1977 that:

> "Today's hearing on the financial condition of the intercity motor bus industry assumes added importance in light of our Nation's energy situation. In order to begin achieving meaningful reductions in the amount of oil we consume, we should be searching for ways to get people out of private automobiles...Intercity motor buses are ideally suited for passenger transportation because they serve 16,000 cities, towns, and communities. They are convenient and accessible and they are fuel efficient...Unfortunately, during the past few years, we have seen a deterioration in the earnings pictures for the bus industry. Six years ago the industry earned about 11 cents per bus mile operated, but last year the figure dropped to a little over 5 cents per mile."[66]

Analogous links between bus firms' financial and political status, their managers' desires for specific forms of deregulation, and the social functions the industry serves have been made throughout the hearings. The social arguments bus executives use are shaped by their relative market positions.

The smallest carriers, concerned about liberalized entry provisions, stress their safety record. The largest, Greyhound and Trailways, note their long history of comprehensive coverage. Medium-sized firms focus on more general bus attributes, such as the ability to

save energy or serve poorer households. Charter-oriented firms interested in dumping nonremunerative scheduled routes stress the link between their profits and their potential service to the tourism industry. The arguments overlap, but are chosen to match the concession sought. A brief review of the major positions in the deregulation process will illustrate this point further.

Greyhound's position

Greyhound Lines supported the ICC bill in its original form. (The bill would have allowed Greyhound to abandon less profitable services and to take over many "small fry" routes now protected against Greyhound.[67]) The company's support for the bill was a quick turnaround in its relationship with the ICC which had deteriorated during the Carter administration. As noted above, the ICC's unilateral effort to reform its own entry regulation drew fire from Greyhound. The company issued an angry policy statement in 1979, saying that the ICC had abandoned a long-established trust:

> For forty years the interpretation...of the...Motor Carrier Act...was consistent with the Congressional objective... "to promote safe, adequate, economical, and efficient transportation" and "to encourage sound economic conditions in transportation..." The result was a mutually beneficial partnership of the regulator and the carrier (which) existed in proper and fruitful balance from 1935 until the mid-1970's. At that time and to this date, the regulator...has nullified that partnership by embracing a policy of uneven and ill-considered administrative deregulation. The result is that carriers today are shouldering many of the burdens of deregulation but realizing few of the benefits...The ICC has embarked upon an ill-advised philosophy of re-regulation which is hastily resulting in the dismemberment of meaningful and productive regulation while also contributing to the substantial deterioration of the financial strength of the industry.[68]

The company statement faulted the ICC for reducing the entry process

> to a meaningless series of ministerial steps...The carefully constructed tests for the balancing of the interests of existing carriers against the proposals of new applicants, while weighing the public interest, are no more. In two short years the Commission has buried the criteria developed over forty years for judging the application of prospective entrants.[69]

But Greyhound was also beginning to realize that the carefully constructed tests were on their way out. Seeing the handwriting on the ICC wall, company executives recognized that a far-reaching form of deregulation could be of help to the company because of its already established market power. A company paper states:

> Although we firmly believe that the regulatory balance achieved between 1935 and 1975 is a principal reason for the development of the world's best intercity bus transportation system, we are realistic and recognize that there will not be a return to that form of regulation in the foreseeable future. At the same time, we sincerely believe that the piecemeal deregulation are presently experiencing is producing the worse form of deregulation from the standpoint of both the consumer and the carrier.[70]

By 1981, when legislative deregulation was imminent, Greyhound no longer advocated the careful tests. The company's new line was to favor "efficiency":

> The bottom line of deregulation is simple...the reform of an archaic regulatory structure that thwarts efficiency.[71]

Greyhound's strategy thus entails a mixture of different public service claims, depending on the time and place. In the example above, the firm shifted from a "careful balance" rationale to one of "effi-

ciency." Another contrast shows up in Greyhound's state and federal lobbying efforts. In Ohio, where a state deregulation bill has been proposed, the company is lobbying in favor of continued regulation.[72] Greyhound holds a virtual monopoly on Ohio intercity service.* Across-the-board deregulation would likely result in parts of Greyhound's Ohio "route property" being confiscated by other firms.

A Greyhound executive defends the seeming contradiction between its position in Ohio and in Washington, D.C., by claiming that Ohio is a special case--in Ohio, Greyhound performs unusual public services:

> "Greyhound has a covenant with the state of Ohio to provide service on certain money-losing routes in exchange for protection from destructive competition. We provide competent personnel, modern terminals, reliable equipment...We serve hundreds of Ohio towns and hamlets where there are few travelers--certainly not enough to justify the kind of service they receive--and we lose money providing this service. In return, we are permitted to have limited franchises on some routes."[73]

Of course, Greyhound has a similar covenant in many other states, but this does not prevent use of the argument. And despite the company's protests, the ICC's relaxed entry provisions also applied to Greyhound. (During 1975-1977 the ICC approved 14 new routes for the company.[74])

Trailway's position

Trailways also uses contradictory arguments to suit its varied lobbying environments. The company wants continued regulation in Colorado, where it has an advantage over Greyhound. But on the interstate level, Trailways advocates a staged deregulation process with a built in handi-

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*Trailways, however, obtained one small route there in 1980.

cap for Greyhound. In House hearings on deregulation a company executive argued:

> "Trailways wants deregulation for itself and other bus companies, but believes Greyhound should continue to remain subject to regulation for a transition period if there is to be any real competition on inter- and intrastate routes.
>
> "During the transition period, Trailways could set up competition along Greyhound's routes but would be protected from retaliation by the larger bus company. Greyhound is so much larger and stronger that Trailways might not survive the onslaught that could result from immediate freedom of entry and exit for Greyhound. We are playing with a stacked deck, and Greyhound has already been dealt the winning hand."[75]

In these remarks, the Trailways spokesman refrained from linking the company's profitability to social functions such as rural transport service, energy savings, or employment, which presumably Greyhound could equally well provide. The argument instead hinged on the business virtue of fair play. Trailways advocated, in a sense, rules of war. But on other occasions, Trailways' strategy is to combine the fairness argument with one of passenger comfort. Trailways has been pressuring for a federal program of bus terminal construction, arguing justifiably that ridership has dropped due to unattractive and inconveniently located bus stations.

Trailways wants to see deregulation linked to subsidies useful to its own operations.[76] In addition to the marketing benefits of better stations, Trailways is concerned about the market power Greyhound holds through its ownership of most bus terminals Trailways uses.[77] Greyhound recently attempted to deny competitors the right to renew leases in some of its stations. Although a federal court order prohibited

Greyhound from carrying out this threat, continued terminal rights for Trailways and smaller carriers are not secure.[78] Unless Congress mandates continuation of status quo leasing arrangements in the deregulation bill, it is possible Greyhound competitors will lose some station space.[79] Equitable terminal rights formed a significant issue in one recent seminar the ICC conducted with the industry.[80] Trailways hopes for a satisfactory resolution, either in the form of permanent leasing rights or assistance in constructing its own terminals.

American Bus Association position

The main industry lobby, the ABA, also mixes social arguments with business fairness in its testimony. (The organization has been instrumental in developing compromise positions on bus policy issues in the past. It represents a broad spectrum of firms, including the two dominant carriers and approximately 600 others.) In the present case, the ABA opposes total deregulation, claiming it would disrupt the industry and "could leave thousands of communities with no public transportation."[81] The organization argues for "re-establishment of meaningful controls on entry," and supports continued collective fare-setting. The ABA also advocates freer exit from services found inessential, and those which cannot be locally subsidized. (Undoubtedly, many of these are the same dependent communities hauled in for the disruption argument above.) The ABA, like Trailways, is also campaigning for further federal subsidies to the bus industry, including a relaxation of highway toll requirements.[82]

The ABA has offered its own plan for more limited regulatory reform.

An important element in its proposal is an increase in the minimum insurance coverage from the current level of $500,000 to $2,000,000.[83] This provision appears to be a concession to small carriers, who are concerned that a flood of new entrants might take over some of their established routes upon deregulation of entry. The new firms could potentially set up operation along the most lucrative routes. By using non-union labor and other economies of business youth, they could conceivably engage in "cream-skimming" (taking the most lucrative service only), which could be harmful to established small firms. By increasing financial barriers to entry, the insurance provision would mitigate the threat of relaxed administrative behavior.

Small companies' positions

Like stability, passenger convenience is a recognized concern in the deregulation proceedings, but it comes under the rubric of fair competition as well. The smaller bus companies insist on the preservation of joint fare-setting (through-ticketing and baggage handling) and terminal leasing rights.[84] Without antitrust immunity for joint rates, they fear passengers will desert them, due to the inconvenience of having to purchase separate tickets and transfer their own luggage at each leg of the journey.

The charter-oriented small companies combine the fairness rhetoric with the public service problem of illegal bus operations. They want deregulation laws to include stricter inspection and enforcement standards than the ICC has developed in the past. These carriers have focused their lobbying on this issue for business reasons. But the ICC and state inspectors consider gypsy bus firms a social nuisance as well

as a business threat. (The firms are prevalent on routes to and from gaming resorts in Nevada and elsewhere.)[85]

Greyhound has similar concerns about illegal competition on the intrastate portion of some routes. Attacking the ICC's indifference to the problem in a 1979 statement, the company claimed:

> One major responsibility that the ICC has, but which it virtually ignores, remains. Carriers not meeting the statutory standards must not be permitted to operate if the travelling public is to be protected against uninsured, unsafe operators. The Commission has the authority today to stop such carriers, of which there are many, but refuses to act in a meaningful manner. With deregulation, this responsibility should be given to an agency with the dedication necessary to achieve compliance with the law. The travelling public is deserving of this protection.[86]

Charter firms that are currently required to cross-subsidize unprofitable scheduled routes (or who at least claim they are) have stressed that freedom of exit provisions should go into effect before free entry is allowed to new, all-charter applicants. This would give established charter operators the first opportunity to expand into new markets. A phased-in deregulation of this sort would form a public reward for past service to these firms, in a sense. Their request seems fair, or honorable, by the same standards that might apply to senior employees in a firm. They have already "paid their dues" and should not be thrown out on the street.

These arguments are compelling, and indeed difficult for Congressmen to resist. The firms may sense that Congress will place the ethic of fair competition ahead of both the lawless market--represented here by the unscrupulous outfits--and the potential advantages of creamskimming to new consumer groups. Serious federal attention to their

concerns in the context of this legislation illustrates the grip that business fairness arguments hold on the whole debate. Small bus firms have been accusing the ICC of overlooking illegal operations for years.[87] But now that bus regulation is receiving renewed attention, the safety and fitness arguments seem to take on more importance.

The small tour-oriented carriers also seek more liberal tour regulation. In this they have formed alliances with related industries. Hotel, resort, and other tourism lobby organizations have joined forces with bus industry groups to demand freer entry for bus tour brokers. (Tour brokers provide bus transportation under contract by assigning vehicles according to tour demand.) In the past, the ICC has viewed them with suspicion since they can jeopardize cross-subsidized operations.[88]

<u>Other uses of rationales</u>

Bus carriers have used social need arguments as ballast in other policy debates besides deregulation. In the 1979 gasoline shortage, for instance, Greyhound, Trailways, and 16 other carriers petitioned the ICC for temporary relaxed entry standards so that they could supplement excess demand along each others' routes. Although Greyhound objected to Trailways' entry onto some of its routes, the ICC granted this permission to both of the large carriers. Greyhound operated on several routes previously controlled by Trailways for three months.[90] The carriers were able to make hay out of the energy crisis, using uncommitted charter vehicles on scheduled routes. The ICC's actions demonstrated both a concern for a short-term social need, and careful

attention to the ethic of business equity, since temporary authority was distributed among the firms.

The bus industry as a whole uses a business fairness argument in lobbying for better treatment vis a vis other modes. Once the industry's potential contribution to the goal of energy conservation was recognized, during the fuel shortage of 1974, the industry began to request special consideration. Congress and the Department of Transportation had generally ignored the bus industry, focusing far more legislation and administrative resources on Amtrak and the airlines.* In 1981, the Department of Transportation had no staff group to attend to bus industry issues, for instance.[91] Since the industry was beginning to experience declining profits, it is likely that industry leaders saw the late 1970s as a timely opportunity to win some new concessions. In 1978,

> In recognition of the fuel efficiency of the intercity bus industry, Congress reduced the excise tax on intercity bus carriers.[92]

In 1979, the Department of Transportation funded a cooperative research program with Greyhound to develop an especially fuel-efficient gas turbine engine.[93] And in 1979, the industry received special exemptions from diesel fuel taxes.[94]

Business fairness makes a powerful argument for increased bus industry subsidies in addition to increased attempts at evenness--however interpreted--in regulatory reform. Greyhound and the ABA launched

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*In part, this was due to the perception that the busses were self-sufficient private firms, while Amtrak was a quasi-public operation and the airlines received heavy federal subsidies.

a campaign during the late 1970s against "unfair government subsidies" to Amtrak. (For instance, Greyhound sued Amtrak for arbitrarily low fares.[95]) Although Amtrak does cut into potential bus revenues on some routes such as the Northeast Corridor, the threat to bus profits was not the main motivation for this campaign. The ICC had already granted bus firms permission to reduce fares on short notice in corridors where Amtrak presented significant competition. (The agency has since extended this short-notice provision to routes where air fares fall below corresponding bus fares.) Instead, when the bus industry argues for equal treatment, as the ABA did in its 1980 annual report, the main concern is not actually unfair competition in the transportation market, but government favoritism. Bus industry lobbyists repeatedly stress that their competitors use federally funded terminals, while they must provide their own. During the late 1970s, the government began to redress the so-called imbalance, albeit modestly, by funding several mixed-mode transportation terminals under the Urban Development Action Grants (UDAG) program.[96] While the future of the new bus programs is uncertain, it is likely that the federal government will continue to pay more attention to the bus industry--as an industry--even after deregulation.

CONCLUSIONS

The variety of rationales, and the central influence of business equity among them, make a compromise deregulation solution likely. But what problem will this "solution" address? It is unlikely to solve the problem of declining demand in the scheduled portion of the industry (if indeed that is a problem of any concern to the public). Exit freedoms may boost operating margins for Greyhound, and entry relaxation is likely to result in more lucrative charter operations. Deregulation may thus postpone the next occasion for a hearing on the bus industry's financial position. But the main problem it addresses is that of satisfying a general clamor for regulatory reform, without unduly disrupting established privileges. Some market-oriented improvements in service patterns may be forthcoming, and the industry may improve its position marginally. Ironically, both pro-business and pro-consumer positions in the debate reduce to the maintenance of status quo elements in the original bargain between industry and the regulators.

Although the Congressional verdict is not out yet, the House bill provides evidence that government's mediating role will not end with the passage of a deregulation law. The law would not provide a uniform preemption of state route authority, but would leave substantial discretion to the ICC. State exit restrictions would be subject to ICC oversight. Carriers wishing to enter or abandon markets could go over state regulators to the ICC by showing that states had denied or refused to act on their petitions.[96] The ICC must make a finding, or else the permission is automatic. The ICC thus would serve as a court of appeals.

The bill defines national bus policy as the

> promotion of a competitive and efficient bus service and the development of a cooperative approach to federal and state regulation of intercity buses.[97]

The bill directs the ICC to grant permits unless it finds a proposal "inconsistent with the public interest." The definition of the public interest is broadened from "necessity and convenience" to include the effects on "small communities" and energy use. But policy would continue to be defined on a caseload, adversarial basis.

The burden of proof as to whether proposals meet the public interest is shifted to the protesting party. This would perpetuate the adversarial definition of public interest--in contrast to either a planning or market concept of it. The shift seems likely to make it harder for consumers outside of "small communities" to successfully appeal their cases. New entrants are also likely to be swamped with litigation when they challenge established carriers' franchises. (However, the bill does provide expedited procedures for carriers wishing to enter markets where no other bus services exist.)[98]

The House bill contains a provision designed to help

> prevent efficient companies from being crippled by new carriers' attempting to skim off the most lucrative business.[99]

This clause prohibits the ICC from granting either charter or scheduled route permits if the new service would "damage the ability of other bus companies to provide a substantial portion of their regular-route service."[100] The ICC would have to define criteria for these findings.

Bus firms' arguments for fair treatment crowd the public roster, generally excluding consumer concerns that are not immediately compatible with some strong position carriers take. Industry-minded consultants and outside analysts have tried in vain to introduce alternative formulations of the consumer side of deregulation, which they seem to believe will help influence Congressmen. For instance, one consultant suggests that if states are concerned about losing needed rural bus routes, they should consider creating their own low-cost transportation programs for those areas. (These might, for instance, use smaller vehicles and local labor and repair services, providing an additional local benefit.)[101] One study points out that exit prohibitions on rural routes may have discouraged formation of innovative private sector services in those locations.[102]

Congress has never investigated alternative means for providing the consumer benefits which bus industry regulation is supposed to uphold. It has not even attempted to document those benefits. Congress has not, for instance, sponsored any major analytical research on the transportation needs of bus riders, as it has for airline and Amtrak passengers. State governments do not generally make forecasts of bus demand or user needs. Hearings at both the state and federal levels reveal a limited understanding of the functions bus services provide. For instance, repeated emphasis on the number of locations served--a favorite industry statistic--obscures the issue of whether the services' schedules and destinations actually correspond to the trips rural residents would like to make.

In the House bill, the shift in the burden of proof to protesting parties is troubling, since preparing cases against service cutbacks is

an expensive process. But more troubling, perhaps, is the very narrow equation of consumer interests with insurance requirements and the established bus services of rural communities. The bus industry and the ICC seem to have decided that bus insurance coverage is a more important social concern than entry flexibility. Discussions of the "gypsy bus problem" rarely raise the possible consumer advantages of a much less regulated service which could potentially prove innovative and useful.

The same uncertainty arises with respect to "cream-skimming." Cream-skimming is the sort of result envisioned by advocates of total deregulation, when they use the less pejorative terms "highest use" or "most efficient investment." But in actual practice, this free-market vocabulary is generally set aside for <u>fair</u>-market rationales. What in theory is most efficient becomes most unfair. Whether cream-skimming in the bus industry constitutes a threat or a boon to consumers is uncertain. It hasn't been actively discussed, and relevant data on the cross-subsidies involved have not been collected. As noted in the earlier discussion of Greyhound's position, the only terms used to discuss the consumer impacts of free entry, are the abstract virtues, "efficiency" and "carrier fitness." For discussion of the merits and dangers of cream-skimming to pass beyond these simple ideologies probably requires a more active role for consumers in the proceedings, and a more thorough assessment of their needs.

The prognosis is equally uncertain for realizing the other consumer virtues--and avoiding the consumer dangers--that industry's political categories have created. The business fairness issue may be relevant to consumer welfare, but it is hard to interpret it from a consumer viewpoint. For instance, the dominant firms, Greyhound and Trailways,

that argue for continued "seniority rights" may in fact be able to provide better interconnecting bus service on a nationwide basis than other firms. This advantage could outweigh the problem their duopoly poses for other firms in the industry. But in order to investigate the question, it would be necessary to establish whether or not interconnecting nationwide service is a prominent consumer concern, more central for example than frequent regional service, which could demand different scheduling priorities. And from a business viewpoint, recent evidence suggests Greyhound and Trailways may have made strategic errors by focusing for too long on long-distance service when regional short-distance markets could have been more profitable.[104] As airlines improved and average auto trip distances increased, the bus mode's relative advantage has shifted towards intermediate or regional markets. One economist suggests Greyhound would have done better to compete for intraregional auto travelers than interregional air travelers.[105] If fuel prices and driving distances continue to rise in future years, upgraded regional bus service might find significant markets among moderate-income auto-owning households, for instance.

Bus companies might benefit more from government-assisted market research than from some of the provisions in the House bill. They could attempt to expand service among new demographic segments, with relatively minor changes in route regulation. If terminal locations were liberalized, for instance, they might attempt to serve the growing number of low and moderate-income households now living in suburban areas, who do not consider taking the bus because of poor connections to downtown terminal locations. Current regulations make this type of adjustment difficult. But the deregulation process has not picked up

on these alternatives, nor have Congress or the Department of Transportation actively studied them.

The bus industry has valued route regulation from a very narrow, company perspective which does not necessarily coincide with the overall interests of either the industry or the public. The heritage of regulation is a relatively static set of business benefits, and a narrow perspective from which it is difficult to isolate business and consumer concerns. To the extent that these mesh, the continued oversight of the ICC and Congress make a favorable outcome possible. The emerging reform legislation does not, however, represent a departure from the narrow conceptual framework for considering intercity bus services, any more than it overthrows historic patterns of business privilege and denial. The existing view of the industry does not rest, however, on a single piece of ideology. Bus company officials choose their arguments--and hence fashion those of the public--from a variety of ideological themes without consistency over time or by place, according to interests of the moment. Any improvement in our ability to judge regulatory reform proposals will require a capacity to get behind the industry manipulation of themes, and redress the lack of basic knowledge about who the industry serves, and how well.

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CHAPTER TWO:

DEREGULATION OF THE U.S. FREIGHT RAILROAD INDUSTRY

INTRODUCTION

Railroad deregulation, like bus deregulation, has not been a unilinear rollback of past regulations. Instead, despite the sweeping implications of the term deregulation, the regulatory reforms undertaken have been highly selective. In a series of reforms since the late 1960s, Congress, the ICC, and the Department of Transportation have removed some former obligations and legal rights from railroad managers, while leaving others intact.

The selective reforms have, furthermore, been only partially cumulative in their effect. Reforms initiated during one administration have on occasion been repealed, either by subsequent legislation, or by modifications in the way the reforms are implemented. For instance, Congress voted in 1976 to permit railroads to set seasonally-variable rates. The rates accomodated fluctuations in rail demand, as at harvest time, and when new model automobiles leave Detroit.[1] But in 1980, when Congress passed the most comprehensive rate deregulation bill to date (the Staggers Act), it removed the authority for seasonal rates.[2] In an administrative example, the Carter administration, which promoted a particularly radical form of deregulation, interpreted the Stagger's Act liberally for the railroads, allowing a variety of rate innovations to go into effect. The Reagan administration, by contrast, is reversing the direction taken by the Staggers Act.[3] (Several

business leaders recently criticized Reagan ICC Chairman Reese Taylor, Jr., for "regulating the rail industry again," as a favor to the Teamsters.[4]) Thus rail deregulation, in addition to being selective, has a forward and backward motion: it takes place in a fluid economic and political environment, and can be reshaped at numerous points.

Over the past ten years, the rail industry's own lobbying frequently determined when reductions in railroads' legal obligations would be contemplated, and how the reforms would be discussed. Through a series of administrative and legislative actions which have altered a long, stable tradition of government involvement, the industry maintained its own perspective on what specific changes were desirable. Railroads lobbied the ICC and Congress through their chief trade group, the Association of American Railroads (AAR), as well as individually when firms' interests diverged. Both the AAR and individual railroads, especially large ones, were successful in positioning issues on the regulatory agenda, playing on popular views of the industry. Rail managers selectively promoted several key themes, notably the theme of financial crisis, to advance their positions, and they often persuaded the ICC, the DOT, and Congress to adopt their own construction of the problems that policies should address.

The rail policy reforms that have emerged over the decade are difficult to evaluate, both individually and in sum. Whether each reform constitutes good public policy is, of course, partly a matter of definition. For instance, one criterion of good rail policies might be that they produce low transportation costs; another would be efficient pricing, to avoid unnecessary and fuel-wasting movement of goods. A third common definition, often implicit although infrequently articula-

ted, is maximum preservation of the rail network. According to this view, rail-dependent firms and their employees deserve continued service according to status quo location patterns, since the firms have made investments in the faith that adequate rail service was a permanent fixture of the landscape. Another frequent definition of the public welfare in railroad regulation is expressed as the need for some minimum level of profits, usually unspecified. In addition to the mixture of criteria one might adopt, the complex nature of the railroad industry has made it particularly difficult to predict and evaluate policy outcomes, in comparison with many other regulated industries. Policies undertaken at one time or with respect to specific railroads were certain to interact with regulatory changes made subsequently, so that the sume effect could not always be anticipated.

The variety of criteria and predictive difficulties in evaluating rail policy are not, however, necessarily the most important problems confronting policy analysts who attempt to assess rail deregulation. Equally or more important are the conceptual limitations imposed on those who would analyze and act on the issues by railroad managers and lobbyists. While the public merit of rail deregulation in its current form is ambiguous, it is clear that the terms for public debate over deregulation were largely set by railroad companies with the greatest lobbying resources and the most at stake. These firms typically managed to color the public view of the issues to suit their own interests.

This discussion will explore the industry's success in getting the government to see railroads' obligations and opportunities in the industry's own terms, throughout the past decade. A brief profile of the industry and an overview of the regulatory tradition will establish

the context for discussing the reform agenda.

RAIL INDUSTRY PROFILE

Markets

Railroads transport five principal commodities: coal, grain, bulk metals and minerals, and chemicals.[5] In 1980, coal accounted for 35 percent of rail traffic on a tonnage basis. Also important are forest products, paper pulp, cement, motor vehicles, and auto parts.[6] Railroads transported 37 percent of freight traffic (in ton-miles) in 1980. The modes' shares of traffic for selected years are shown in Table 5.

Industry structure

In 1980, of approximately 500 railroad companies, 40 had revenues of over $50 million each. These companies transported 98 percent of total railroad traffic, operated 94 percent of rail mileage, and accounted for 92 percent of the workers employed by all railroad companies.[7] Table 6 shows the revenues of the 13 largest railroads in 1980 and 1981.

Financial performance

The railroad industry's financial performance is varied. In general, railroads in the coal, grain, and paper pulp markets have experienced higher profits in the last few years than those transporting manufactured goods. Midwestern railroads with traffic tied to automobile manufacturing have suffered the largest recent decline.

In 1980, the industry's estimate of its rate of return on net investment was 4.25 percent for the 40 railroads that dominate the industry. This was the highest level reached in 25 years. The increase

Table 5: Mode shares of freight ton-miles, historic and recent

Mode	1929	1950	1970	1974	1980
Railroads	74.9	56.2	39.8	38.6	37.3
Trucks	3.3	16.3	21.3	22.3	22.6
Waterways	17.4	15.4	16.4	16.1	16.9
Oil pipelines	4.4	12.1	22.3	22.8	23.0
Air cargo	--	--	0.2	0.2	0.2
Total ton-miles (billions)	607	1,063	1,936	2,215	2,497

Source: Association of American Railroads, *Yearbook of Railroad Facts*, 1981

Table 6: Railroad revenue, 1980 and 1981 (millions)

Railroad	1980	1981
Union Pacific	$4,872	$6,381
Missouri Pacific	2,237	2,524
Southern	1,637	1,790
Norfolk & Western	1,576	1,801
Burlington Northern	3,954	4,936
CSX	4,841	5,432
Southern Pacific	2,860	3,272
Santa Fe	3,215	3,366
Kansas City Southern	323	386
Chicago & North Western	936	982
Illinois Central Gulf	4,142	4,195
Denver & Rio Grande	350	388
Conrail	3,358	--

Source: Barron's, April 19, 1982, and Moody's Transportation Manual, 1981

was due to record volumes of coal and grain traffic.[8] Since 1975, the industry's rate of return indicator has been low and erratic, as shown in Table 7. Railroads in the Eastern District, which encompasses much of the Midwest as well, lost money throughout the period.

Table 7: Rate of return on rail investment*
1975-1980, by rail district

Year	United States	Eastern**	Western	Southern
1975	1.20%	deficit	3.98%	2.65%
1976	1.60	deficit	4.63	3.57
1977	1.24	deficit	5.23	3.71
1978	1.52	deficit	5.17	4.22
1979	2.87	deficit	5.38	4.38
1980	4.25	0.07%	6.33	5.43

Source: AAR *Yearbook of Railroad Facts*, 1981

*net railway operating income as a percent of net investment in transportation property, less interest, plus working capital

**includes Conrail; does not include Amtrak

CHANGING CLIMATE

The railroad industry has experienced two major context changes since the 1960s, both of which affected the outlook for regulatory reform. The first was a series of major bankruptcies in the Northeast and Midwest, and the second was expansion in the markets for coal and grain transportation. These events took place against a backdrop of overall decline in the industry's market position, relative to trucks, and a loss of traffic in regions where service industries have replaced transport-intensive raw materials, agriculture, or manufacturing as the predominant economic activity. Commonting on the decline of Northeastern railroads, U.S. Representative James Florio aptly stated that in

> "New Jersey, now our number one industry is drugs and number two is tourism. Research and development is a major industry, and you don't ship that."[9]

The decline of the railroad industry is not a recent development. Railroads have been considered a declining industry since the 1930s. (The system peaked in size in the 1920s at 250,000 miles, and is currently operating over approximately 200,000 miles.[10]) The industry is heavily tied to the commodities business cycle, so attempts to quantify the decline with time-series data can be misleading. But one rough indicator, employment, has shrunk by two-thirds during the post-war period.[11] Despite the shrinkage, the industry is regarded as having an overcapacity of both track and personnel.[12]

As Table 5 showed, the railroads' share of domestic intercity freight ton-miles fell from 74.9 percent in 1929 to 37.3 percent in 1980.[13] The trucking industry made up most of the difference. Absolute

rail tonnage has been fairly stable since World War II, but its composition has shifted towards denser commodities, that move only at relatively low rates. Hence, the decline would be greater if stated in terms of revenue market shares.

Besides improvements in trucking service and the reduced significance of heavy manufacturing in the U.S., other destabilizing trends have included the development of synthetic materials that require less transportation, and the regional decentralization of the U.S. economy. Decentralization makes it harder for railroads to balance large volumes of two-way traffic over their fixed routes.[14]

The Eastern railroads' position grew relatively worse as railroads lost their market in general manufactures and became more dependent on raw materials and export grains located elsewhere. Demographic shifts may also have contributed to the relative position of the region's railroads.[15] A series of railroad bankruptcies, beginning with the Penn Central Railroad in 1970, prompted public recognition of the relative decline of Northeastern and Midwestern railroads. Railroad bankruptcies have been common since the industry's early years, but the Penn Central was the largest bankruptcy case in U.S. history.[16] Other major bankruptcies in the region included the Boston and Maine in 1970, the Reading Railroad in 1971, the Erie Lackawanna in 1972, and the Rock Island Railroad in 1979.[17]

Although the overall impression is still one of a declining industry, individual railroads have maintained, and increased, their profits throughout the past two decades. The Southern Railway, for instance, continued to invest in new technology and acquired high-volume markets for grain and other products while Northeastern and

Midwestern railroads were disinvesting. More recently, the industry has experienced significant increases in demand for coal transportation. (Over 60 percent of U.S. coal is hauled by rail.[18]) The federal government helped to establish an increased domestic market for utility coal in 1978 legislation requiring conversion of oil-and gas-fired electric plants. The coal export market has also grown significantly (see Table 8).

Short-term changes in rail finances also shape the policy-making context, in conjunction with the longer-term events discussed above. Long-run decline typically produces its most visible signals, such as near-bankruptcies, during off-years (either recessions, or years with major strikes or embargoes). Short-term traffic increases (often one-time occurrences), conversely, produce hopeful signals to policy-makers concerned about rail profitability. For instance, the year of the Soviet grain deal and the termination of the United Mine Worker's strike--which added much of one year's expected coal shipment to the next--were heralded as "growth years" for railroads.[19] Since it is difficult for policy-makers to sort out foreground and background trends, especially on a firm-by-firm basis, the industry has little trouble arguing that it needs regulatory or legislative relief, whenever any dip in volume or revenues arises. In addition to regional bankruptcies and new bulk commodities markets, inflation represents another climatic change which has affected the railroad industry's regulatory agenda. The development of chronic inflation, beginning in 1967, altered the context for rail rate-making, which in the absence of inflation was a very conservative process.

Table 8: U.S. Coal Consumption, 1977-1980 (million tons)

Domestic	1977	1978*	1979	1980
Electric utilities	476	480	526	565
Coking Coal	77	71	77	73
General Industry & Retail	67	70	74	77
Exports				
Canada	17	15	19	19
Overseas	37	25	46	65
Total Domestic & Export	691	654	776	825

Source: Connie Holmes, Coal Exporters Association and National Coal Association, December 1980

*In 1978, both supply and demand were depressed due to coal and rail strikes.

REGULATION: HISTORIC PRACTICES

The rail industry and the federal government challenged three main areas of regulatory practice in the reforms of the 1970s and 1980s: service abandonment (or exit) regulations, rate regulation, and merger guidelines. Not all aspects of railroad regulation went through an upheaval, however. In addition to these three regulatory elements, the ICC has also traditionally monitored railroad operations in considerable detail. Operating requirements include, for example, technological standards to facilitate interchange of equipment among railroads, and detailed provision for the movement of freight cars around the rail network.[20] The ICC also provides railroad accounting standards.

Most of the rail regulations derive from the Interstate Commerce Act, and from ICC precedent in implementing the Act. Many rules predate the 20th century. The full set of rail regulations supports what is called the "common carrier" system of rail transport. The term common carrier designates the regulatory principle that railroad service should be available to all potential users at a standard price. Although this principle has never been fully realized, over time the ICC developed an extremely elaborate set of rules, intended to approximate this condition. The nature and origin of the common carrier requirements are too complex to develop here, but a thumbnail sketch is necessary to understand the railroads' motives for eliminating some of them and preserving others. In essence, the rules require that railroads operate in an interdependent, rather than autonomous, manner, and that status quo services and traffic handling arrangements be maintained unless specific proposals are made to change them.

Service regulation

Service regulation consists of two main guarantees, each supported by a battery of detailed, technical rules. The first is a guarantee of service to shippers, and the second is a guarantee of mutual cooperation among railroads where coordination is required, or supposedly required, to back up the first guarantee. Under the common carrier principle, railroads cannot refuse to carry goods if a customer can pay the rate. Railroads are not permitted to abandon service on any line without first petitioning for ICC approval.* Even in bankruptcy, a railroad is not permitted to cease operations or abandon low-volume lines without ICC approval. Exist or abandonment cases have often entailed protracted hearings.[21]

In the common carrier tradition, railroads are not only required to serve all customers until further notice, but to cooperate with each other in order to do so. They must, for instance, haul each others' traffic without discrimination when specified by the ICC, and in some cases, they must make special trips to pick up and return another line's freight cars which would otherwise be stranded at their destination.[22] Much rail traffic moves over several firms' lines, often creating conflicts over what routing pattern will be followed (for example, when two of the companies have duplicate facilities over a segment of the route). Another very frequent kind of conflict involves the share of revenues to each participating railroad, known as the "divisions." The ICC has devoted considerable attention throughout its history to adjudicating divisions conflicts, and continues to do so today. Al-

*Of course, by setting rates high, or failing to make freight cars available on a timely basis, railroads can occasionally refuse unprofitable traffic.

most any type of rail case has the potential to turn into a divisions dispute, since any changes in service or rates potentially affect railroads' relative portion of jointly-handled traffic. Divisions adjustments are sometimes used to compensate a railroad that expects to lose traffic after the change.[23] The ICC also specifies which parties--railroads, shippers, or receivers of goods--have authority over routing decisions.

Merger guidelines

In the merger area, the ICC developed a set of guidelines based on precedent, and codified in 1950, which provide that weaker and/or smaller lines be incorporated in the merged system, to ensure their continued operation after the merger. In some cases, parties wishing to merge were required to purchase smaller, low-profit lines. In others, the ICC imposed protective conditions, requiring merging railroads to guarantee previous routing arrangements, or to allow weaker lines the right to use their track. Two standard protective conditions, for instance, are as follows:

- The present traffic and operating relationships...shall be continued whenever possible.
- The promptness and frequency of handling of all cars shall be without discrimination.[24]

The conditions ostensibly protect shippers located on vulnerable lines. This usually occurs, however, only as a by-product of the railroads' internal negotiation. A railroad with a costly or circuitous route, for instance, may fear that its now more efficient, merged competitor will take over its former share of traffic. By requesting a guaranteed traffic share after the merger, the vulnerable railroad may be in a

good position to continue service to local points on the line. But the conditions are specified, and applied, from the point of view of fair treatment of railroad companies.[25] The ICC has imposed the 1950 conditions in numerous merger cases since then. Because negotiating a satisfactory resolution of railroads' requests for conditions is a delicate process, until recently the ICC often took years to weigh the evidence of competing parties in merger cases.[26]

Rate Regulation

The ICC does not set rail rates, but may approve or deny proposed changes over a base structure. The basic rate structure has a very long tradition, since its main outlines evolved prior to the ICC's inception in 1887.[27] In its regulation of rail rates, the ICC has been described as a "monitoring system supervising a cartel."[28] Railroads have had a major hand in regulating their own rates, working through a hierarchical network of rate bureaus (legal price-setting boards). The bureaus publish official tariff (rate) books, and perform both administrative and lobbying services for their members. Congress held the rate bureaus exempt from anti-trust law, on the grounds that the ICC was better equipped than the Department of Justice to correct any problems of monopoly power.[29] The AAR presides at the top of the rate bureau pyramid. The AAR maintains contact with all of the bureaus, compiles their government paperwork, and testifies for the railroads in a variety of rate cases involving more than one company.

Rate regulation originated on the state level, and was gradually introduced at the federal level during the early years of the ICC.[30] Early state regulation (as in the case of intercity busses) tended to

be more exacting than federal regulation. States were concerned with protecting local shippers against high railroad rates. But as railroads found state regulations increasingly burdensome in the early 1900s, they successfully pressured the federal government to preempt much of the states' power over rates. State preemption took place gradually during the Theodore Roosevelt and Wilson administrations.[31]

During this period, the ICC became a forum for routine rate and divisions conflicts between railroads. The ICC's role as arbiter was later extended to intermodal disputes, when Congress passed the Motor Carrier Act of 1935. The Act provided standards for "fair competition" between railroads and trucking firms. After its passage, the rail common carrier system had to coexist with similar systems in the other regulated modes. The increasingly complex ICC roster ultimately guaranteed a fuller hearing to industry viewpoints than to those of the general public.[32] As early as Theodore Roosevelt's presidency, Gabriel Kolko states that the ICC had

> "broken into a routinized pattern of adjudicating the problems of the railroad industry without concern for the larger interest of a public not immediately involved in the day-to-day issues preoccupying the railroads, Commission, and wealthier shippers."[33]

Both in the early period of rate regulation and more recently, many rail rates have been established outside the regulatory process; they are worked out informally between railroads and their customers. The ICC only becomes involved if someone protests a rate change. The ICC criteria for judging rate cases are complex and contradictory. According to the Interstate Commerce Act, rail rates were historically prohibited from giving undue preference to

> any particular person, company, firm, corporation, association, locality, port, port district, gateway, transit point, region, district, or territory.[34]

The original purpose of the law was to prevent railroads from developing selective relationships with individual shippers, that could lead them away from the common carrier principle of availability.[35] For this reason, the ICC also prohibited railroads from offering contract rates or discounts to shippers. In actual practice, it is virtually impossible for any change in a rail rate to live up to these requirements. The ICC therefore has had significant discretion, sometimes following its own precedent, and often justifying its decisions with a *post hoc* selection from the repertoire of possible prohibitions mentioned above.

The rate picture is complicated further by detailed ICC case-law concerning the relationship of rail and truck rates. Rail rates are required to cover marginal costs, although determination of marginal costs is often another matter for protracted ICC hearings. Until recently, the ICC was required to consider whether or not a proposed rate would undercut truck traffic.[36]

The traditional system of rate-making has produced two main forms of cross-subsidy: 1) between railroads (when traffic is handled jointly), and 2) between competing shippers, who may for historic reasons pay different rates for similar services. The extent and magnitude of either form of cross-subsidy throughout the industry has not been determined.[37]

The ambiguous public value of the regulatory system

The three components of common carrier regulation that were partially dismantled in the 1970s--service requirements, rates, and merger conditions--have an important common feature. Because of railroads' widespread interdependence and the keen competition between rail users, regulations of each type typically protect one set of shippers' and railroads' interests, while threatening others. Service requirements, for instance, protect shippers located on existing rail lines, and they also ensure that customary connections for jointly-handled freight movements are maintained. (The latter benefit accrues primarily to the connecting railroad, and the major lines dependent on it.) And as mentioned earlier, a rail merger fashioned under the ICC's conventional guidelines may protect status quo service competition, by keeping traditional choices available to shippers. However, the conditions are framed in such a way as to protect existing traffic patterns, and benefit individual railroads.

Deregulation in any form is likely to alter the balance between competing or mutually dependent railroads, and between competing shippers. As in any routine rate case, a change in the guidelines for rate-making may result in some shippers losing their markets, if the price or service differential between them and their competitors increases. Hence, if a railroad wishes to propose a change--a merger, a rate increase or reduction, or a change in revenue divisions--it is always possible to bill the change as one which will "aid shippers by creating more competition," or "promote efficiency," or enhance some other generic attribute of a good railroad system. Yet the same change may reduce competition or efficiency elsewhere in the transpor-

tation system. Hence, most departures from regulatory tradition--both routine and structural--have an ambiguous outcome for rail-using firms, competing railroads, and the general public. Further, because of this ambiguity, there is in the history of rail regulation a pronounced tendency for railroads, and the ICC as well , to use the terms competition, efficiency, and service without analysis, and without admitting that their definitions are narrowly applied to one set of firms and not another. Both sides in almost any rail dispute can utilize one or more of these catch-words to advance either a change, or maintenance of the status quo. The same unspecified terms that appeared in traditional rate, merger, and abandonment cases have occupied key intellectual positions in recent debates over deregulation.

DEREGULATION: THE REFORM AGENDA

The following sections examine a series of regulatory changes which have taken place in the railroad industry since 1970. In some instances, the railroad industry (or specific firms) initiated regulatory changes, in response to a changing external context. In other cases, the ICC or Congress first proposed a reform, intended to benefit a broader segment of the population such as industrial or household consumers. The railroads then sought influence over its development, to promote what they considered a favorable outcome.

The timing of the railroads' participation in selective deregulation initiatives suggests that in addition to the secular economic developments described earlier (including bankruptcy and bulk transport opportunities), the political climate was also an important motive for reform attempts. Both economic and political changes contributed to make the reforms--some of them long-desired--more necessary or more feasible than previously.

As each of the reforms came under discussion, railroad companies significantly shaped the terms of discussion, and often the policy outcome as well.* The industry's success in steering policy formation stemmed from the use of lobbying arguments compatible with the public opinion at the time. Some of the railroad managers' arguments are similar to those that bus industry spokesmen made in order to promote favorable provisions in the bus reform package. These include arguments about business equity, energy conservation, and the industry's

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*Whether or not the outcome would be favorable to the industry in the long run is another question.

"underdog" status vis a vis other modes. Other rail rationales are distinct. For example, the railroads frequently couched their positions in the rhetoric of imminent financial disaster.

The merit of the resulting policies for consumers, workers, and the general public is uncertain. As noted at the start of this chapter, a variety of useful criteria could be developed to evaluate the reforms, given accurate impact predictions. Some of the regulatory changes might result in more efficient prices, promote regional employment, or create long-term investment capital, three frequently mentioned policy goals. But Congress, the Department of Transportation, and the ICC seldom undertook formal impact assessments of the reforms described here, or their likely interactions. They seldom evaluated the policies against broad social criteria of any sort, relying instead on an adversarial definition of the public welfare, largely couched in industry terms.

The regulatory reforms considered include 1) the legislative formation of Conrail in 1973; 2) selective relaxation of rate regulations during the period 1970-1976; 3) partial liberalization of merger conditions in the late 1970s, and 4) legislative reform of rail rates in 1980. It should be noted that some of these reforms fall outside the conventional meaning of the term deregulation, which often refers to a formal, comprehensive legislative package, adopted "once and for all." But on each occasion, railroads pressed for a selective alteration in government obligations, creating and drawing on unexamined popular arguments to bolster their position.

Legislative formation of Conrail

One of the most important instances in which railroads promoted selective deregulation, using popular themes, was the formation of Conrail in 1973. The legislation establishing Conrail as a quasi-private Northeastern railroad was not a regulatory reform measure, as such. Rather, the Regional Rail Reorganization Act (or 3R Act) removed most of the rail mileage in the Northeast, and much in the Midwest, from the traditional exit and bankruptcy regulations in the Interstate Commerce Act.

The 3R Act was formulated by general counsel to the Union Pacific Railroad, in response to actions of the Penn Central trustees. The trustees, concerned about their ability to repay creditors and extricate themselves from railroad operations, proposed to abandon half of the railroads' lines. They claimed that the bankrupt railroad would "revive by itself" if the mileage were cut. The trustees claimed the ICC was at fault for

> forcing the railroad to keep these branch lines after their usefulness had ended.[38]

It is true that some of the branch lines had virtually no traffic at the time of bankruptcy. Yet, as Richard Saunders points out, if half of its system was useless, the Penn Central must have had an indication of this before 1973. The Penn Central had not petitioned to abandon many of the lines previously, despite opportunities to do so. The company had even encouraged shippers to build or expand facilities along some of the lines.[39] And some lines were still valuable feeders to the mainlines.[40] It appears that the Penn Central, a diversified conglomerate with major real-estate holdings, had decided to disinvest

in its railroad operation, and saw an opportune occasion in 1973. Public attention was at a high level due to the bankruptcy, and the prospects for an ordinary income reorganization seemed limited.[41]

Since it would not have been possible for the trustees to put the 10,000 miles of lines through the ICC abandonment process all at once, their goal was to deregulate the abandonments. This required legislative removal of the ICC's authority to block them. In 1973, the Penn Central secured the cooperation of Judge Fulham, the bankruptcy court judge responsible for the Penn Central case. Fulham declared a time limit of 45 days during which a "Congressional solution to the Penn Central crisis" must be found.[42] If a solution was not forthcoming, Fulham announced that he would order immediate liquidation of the entire Penn Central property.

The Union Pacific came forth with a plan to create a national corporation which would purchase and operate the Penn Central system, and have the authority to cut out little-utilized mileage through planning (rather than regulation). The Union Pacific had a direct interest in a federal subsidy to the lines:

> The Union Pacific didn't want to lose the 25 percent of its traffic that it sent to or received from the Northeast. It didn't want a free-for-all of southern and western roads grabbing for pieces of the northeastern network in case there should be a liquidation.[43]

The Nixon administration responded favorably to the Union Pacific plan, despite concern that it might appear to be a precedent for nationalization. The Department of Transportation adopted the trustees' notion that by slashing railroad mileage, profits could be restored. Although

the ICC contended that the plan was a piece of "wishful thinking,"

> The DOT made no attempt to analyze if this were the correct solution...Instead, the statement was simply repeated, over and over, in the reports, in hearings and to the press that students of transportation agreed that slashing mileage was the proper solution.[44]

John T. Fishwick, president of the Norfolk and Western Railway, agreed with the ICC that the bankrupt railroads could not be revitalized without massive financial aid. He was "particularly critical of the suggestions in the original Conrail plan," estimating that federal expenditure on the Contrail system "would be about double what the DOT projected."[45] Fishwick's criticisms were not purely methodological. They reflected his concern that the federally subsidized railroad would provide unfair advantages to Norfolk and Western's competitors.[46] But the forecasts, and the threat of cutting mileage, prevailed, and the legislation was passed in time to avoid liquidation.*

While the trustees stressed the need for special government action to bring the railroad out of its financial emergency, the Union Pacific (now the most profitable U.S. railroad) claimed that government purchase was essential to the economy of the northeast.[48] Union Pacific appeared interested in having the government absorb losses on the Penn Central branch lines which it might otherwise have had to purchase, or subsidize through revenue divisions. Both railroads as-

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*The DOT projections assumed a reversal, rather than further decline, in the northeastern railroads' traffic base. And the 3R Act budgeted only $250 million to cover the guaranteed lifetime incomes awarded to the bill's labor supporters. DOT estimated that the $250 million would last "until the last protected employee retired," but it was gone in four years.[47]

serted the need for immediate government action. Little thought was given to alternative forms of intervention, in part because the railroads had created an artificial urgency via the bankruptcy court.

The 3R Act's selective deregulation did preserve some rail services that might otherwise have been abandoned. The public value of these services, as a group, was not scrutinized, however. The 3R Act was probably not the most cost-effective manner for preserving the lines, yet potentially more economical alternatives, such as cooperative ownership or nationalization, were not debated. As a job preservation program, the 3R Act was not assessed on a long-term basis. Supporters cited the need to "save rail-dependent jobs," but Congress did not investigate whether the branch lines would be preserved indefinitely, or only on a stop-gap basis to justify a one-time subsidy.

The 3R Act is generally considered to have been a broad social welfare measure, aimed at protecting rail-dependent Northeast employment, and the performance of the U.S. industrial economy. But its success on both of these terms was uncertain. The railroads with the greatest interest in partial deregulation of abandonment, and the greatest ability to advocate that interest, shaped the agenda to their own liking, by manipulating the themes of financial crisis, optimism, and regional economic need.

<u>Selective rate reform, 1970-1976</u>

In addition to the 3R Act, rate regulation was another important area of reform during the early 1970s. During this period, the federal government and the AAR each attempted to reform different aspects of rail rate regulation. The AAR's reforms generally succeeded, while

most of Congress' reforms were perceived as failures. The ability of the AAR to construe the issues to its members' advantage accounted, at least in part, for the discrepancy. The AAR's target for change was the historic rate structure, or the relative prices charged for hauling different commodities. Congress, the DOT, and later the ICC itself, focused instead on the railroads' continued collective rate-making practices via their rate bureaus.

Although the rate bureaus still enjoyed anti-trust immunity, they were increasingly perceived as illegitimate and outmoded. The ICC made few investigations to determine the extent of the rate bureaus' collusive powers or stabilizing function, so their continued existence was of ambiguous merit from a national policy standpoint. The commodity rate structure, likewise, had seldom been alayzed as a whole.[49] But the railroads' successful lobbying initiatives helped to prevent the development of an appropriate methodology and research expertise, which might have addressed the impacts of selective deregulation from a broad public standpoint.

The AAR used a single rationale--financial crisis--both to promote its rate structure reform and to resist reform of collective rate-making practice. Thus, where rate regulation was concerned, financial crisis was an all-purpose justification for implementing one form of deregulation and avoiding another. In asserting the industry's own view of what constituted appropriate deregulation, the AAR made use of the same public concern over the Northeastern railroad bankruptcies discussed in the previous section. However, unlike the Union Pacific or Penn Central's lobbying for the Conrail program, the AAR sought to extend the public impression of crisis to the whole industry.

The external change motivating both government and industry initiatives was the onset of chronic inflation. Congress had criticized collective rail rate-making in the past. But inflation made collective rate-making much more visible to Congress. Beginning in 1967, the industry had petitioned the ICC on a yearly basis for nationwide percentage rate increases. These general increases were designed to cover the effects of cost inflation quickly, without the need for separate actions on each rate. (Use of the general increases had been rare before 1967.) While in retrospect, the use of percentage increases to adjust for inflation seems above controversy, in the late 1960s and early 1970s, when inflation was not yet viewed as a normal state of affairs, it often appeared to Congressmen that the general increases were an illegitimate use of ICC authority. Each general increase case drew angry constituent mail. (A typical complaint from local shippers was that the railroads "should not have another general increase because they just had one last year.") Congressmen were also concerned about the inflationary effect of sudden nationwide rate increases.[50]

Congress put pressure on the ICC to de-emphasize the general rate increase process, beginning in 1971. The ICC began to suggest that railroads make up cost inflation on an individual basis, or at least through local rate bureaus, rather than enmasse through the AAR.[51] The ICC's printed decisions on general rate increases, for instance, exhorted the railroads to provide more detailed supporting data, so that varying levels of need could be determined for different segments of the industry. Railroads were instructed to

> stop depending on the general increase process and make more use of selectively tailored rates.

In 1973, Congress formally required the ICC to collect a detailed schedule of financial data by individual railroad before approving any more general rate increases. The measure was intended as a disincentive, to discourage collective percentage increases. Although the ICC threatened to enforce the reform, the industry resisted it, and the ICC continued to grant increase petitions with the schedule left blank.[52] In refusing to give up the collective practice, railroads claimed that the delays involved in adjusting rates on an individual basis would "cripple the industry."[53] From a procedural point of view, it would require continuous manual updating of the tariff books, and "confuse shippers." Similarly, the AAR and a number of individual railroads claimed that filing the more detailed financial and cost data that the ICC sought in support of general increases "would present an untenable financial hardship" in itself.[54]

The AAR used the same argument successfully in another setting. State-level regulatory authorities still had some power over general rate increases on intrastate rail traffic. The state commissioners typically took much longer to approve inflation-related rate increases than the ICC.[55] The AAR turned "intrastate rate lag" into a major issue in 1974, again claiming an urgent need for revenues. Congress responded with legislation to preempt most of the remaining state autonomy. States would now have to decide general increase cases within two months after the ICC announced each nationwide increase. The reform posed an ironic contrast to Congress' other actions on general increases, since it pegged the intrastate rates to the very

structure Congress was trying to dismantle. But a fact the railroads seldom mentioned throughout the intrastate lag campaign was that intrastate traffic contributed less than one percent of total railroad revenues.[56] In a true revenue emergency, this insignificant amount would have made little difference to the railroads' standing.

Since the ICC would not act to command managerial reform through paperwork rules, in 1976 Congress passed a more comprehensive piece of legislation, again designed to wean railroads away from the nationwide collective increases. In contrast to earlier efforts, this bill, the Railroad Revitalization and Regulatory Reform Act (4R Act), offered a carrot rather than a stick. The Act provided several modest rate-making freedoms, "to encourage more long-run cost sensitivity and marketing" among the railroads. For instance, the ICC would approve individual rate increases of up to 7 percent per year without petition, and higher increases would be permitted, as long as the railroad did not dominate the particular market. The bill also offered the railroads a first opportunity to establish seasonal and peak-volume rates.[57] But the railroads utilized these innovations very sparingly, with the exception of the seasonal rates, and continued to rely on general increases to offset inflation.

In order to create the impression that financial hardship required nationwide rate increases, the AAR exclusively submitted aggregate cost and financial data in rate cases throughout the 1970s. This led one critic to comment that the ICC was

> rewarding railroad inefficiencies, creating a symbiotic relationship between the needy East and greedy South... The crux of the carriers' revenue case hinges upon the demise of the Penn Central.[58]

Whether the general increases created more inefficiencies than independent pricing would have done is not clear. But the Penn Central bankruptcy did figure heavily in the AAR's rate testimony and the ICC's printed decisions during the period. In 1971, for instance, the ICC permitted an increase approximately 20 percent greater than any but the Eastern railroads could justify with their cost submissions. The ICC announced that all the carriers could use the increase

> since the industry's financial condition is desperate... One has only to look at the flow of red ink to see the need for additonal revenue.[59]

Although there is no question that the industry's rate of return (as calculated by the AAR) was low throughout the country in 1971, financial conditions varied. The evidence suggests that many Southern railroads, including the Chessie and the Southern Railway, did not need the increases and may have been using them to overcharge grain and paper shippers.[60] By focusing attention on an aggregate, generalized view of the industry's financial hardship, the AAR successfully clung to its regulatory prerogatives.

Just as inflation made reform of collective rates a more urgent issue for Congress, it provided a natural opportunity for the AAR to win routine exceptions from rate structure regulation. Many railroads had long been interested in raising their rates on coal traffic, which is primarily tied to the rail mode, and lowering them, further than normally permitted, on commodities which could move by truck. The former action was difficult in the absence of a strong argument for rate relief, and the latter ran counter to the ICC's practice of protecting truck traffic from predatory rail rates. However, the superior

financial performance of the trucking industry (again, on an aggregate basis) during the period somewhat weakened the ICC's hand in trucking protection as well.

In the new inflationary environment, and with the mood of urgency described above, the AAR had an unprecedented opportunity to gradually skew the rate structure, allowing rates on some commodities to rise faster than others. A loophole in the general rate increase process, known as the "hold-down," permitted the percentages to vary slightly on specific commodities. The AAR used this loophole to instill variation in what were still considered uniform increases. By winning permission for a higher overall increase than could be cost-justified, it was possible for the railroads to raise less competitive rates by the maximum percentage authorized, but hold others down below it, citing the need to retain traffic on the competitive commodities. The hold-down procedure was an old device, but in the context of rapid inflation, the railroads could hope to increse the spread geometrically.

By 1972, along with each petition for a general increase, the AAR filed a battery of exceptions or hold-downs to be applied to different commodities. The American Trucking Association and the coal lobby protested the practice and claimed it was an extension of rail cartel power.[61] But the allegations were not scrutinized. In the interest of expediting the rate cases, to meet the carriers' "urgent revenue need," the ICC began to cut short the period for shipper and trucking testimony normally built into each rate case.[62] (Testimony in rail rate hearings was of two general types, each provided for by a separate section in the Interstate Commerce Act. In the first type, shippers and other parties were permitted to protest unfair or prejudicial

rate impacts on their particular traffic. In the second type of testimony, they could only address the railroads' financial needs, without reference to their own situation.) In two consecutive rate cases, the AAR convinced the ICC that the need for rate relief was too great to permit the customary rounds of testimony on prejudicial industrial impacts. Issues of rate discrimination against particular commodities and regions were thus excluded from the proceedings altogether.[63]

The hold-down method of deregulating the rate structure did not work as well in subsequent years. After 1974, the railroads were more often denied the full increases they sought, which were now--at 12 or 15 percent annually--even more visible to Congress than in earlier years. The AAR then began to petition openly for one base increase, and a special, higher increase on coal. The ICC generally adjusted the latter figure downwards, but allowed it to remain above the base request.[64] When utilities and coal interest protested the new arrangement, the ICC again echoed the railroads' statements that the industry's revenue needs were great, and the coal industry could stand the increase. The AAR often spoke of the need for a higher contribution from coal, to defray the costs of repairing railbeds in coal-hauling regions. The AAR's position may have had merit, but the ICC failed to investigate the claim.

Ultimately, the AAR won a legislative concession which institutionalized the derugulated coal rates. The concession came in the 4R Act. In addition to its modest selective rate provisions, the 4R Act allowed the ICC

> for the first time to include as part of its rate-making criteria whether a rate will assure a railroads' repayment of debt, cover the effects of inflation and assure raising of sufficient equity capital and a reasonable or economic profit.[65]

This new provision appeared to be aimed at coal rates, and the ICC used the criteria when coal rates were under consideration. According to a coal industry publication, some members of the House Commerce Subcommittee on Oversight and Investigation criticized this provision as a license to overcharge coal shippers:

> Subcommittee sources say some members see this as a profit enhancement measure, and wonder why the ICC has applied adequacy of revenue criteria to coal rates only. The staffers also admit they are hampered because the ICC has apparently undertaken no verification of the cost figures the railroads have given the agency to justify their rate requests.[66]

The AAR was able to win gradual deregulation of the rate structure, while retaining the privilege of using rate bureaus. In each case, the AAR successfully cultivated the impression that the industry's financial status required selective deregulation. The first few years of chronic inflation coincided with the wave of large bankruptcies, creating an environment in which the AAR could claim the need for special exceptions. By the time the novelty of inflation had worn off, and the sense of financial urgency had faded into one of chronic, predictable revenue shortage, the railroads' selective deregulation had become the new status quo.

The results of selective rate deregulation are difficult to evaluate from a public policy or comsumer viewpoint, as suggested in the quote above. Few commentators or analysts have advocated in-

definite retention of the archaic rate structure, and the AAR's changes may have brought rates on some commodities closer to costs. Likewise, the ability of rate bureaus and their nationwide conduit to act as a cartel may now be more circumscribed than critics imply. But the AAR's ability to dominate the process of choosing which regulations to keep, and which to remove, has excluded full consideration of these issues.

Implementation of liberalized mergers, 1978-1980

In 1976, the Carter administration's ICC Chairman, Daniel O'Neal, offered to streamline the rail merger cases the agency had handled on an adversarial regulatory basis since the 1940s. A 31-month time limit was set for ICC merger proceedings. And the ICC said it would no longer insist on the inclusion of weaker lines in merged companies.[67] The rail industry had pressured for freer mergers for a long period, claiming that excessive delays and restrictive conditions prevented the industry from consolidating to achieve cost reductions.[68] But O'Neal's announcement was not only a response to industry pressure: it also formed part of a larger Carter-era regulatory reform movement, which included the 4R Act discussed in the previous section. The AAR applauded O'Neal's decision, and several large railroads began to prepare merger proposals.

The four main proposals were for what are called "end-to-end" mergers, where two cooperating railroads merge lengthwise to extend their distance coverage. (End-to-end mergers are distinct from "parallel" mergers, in which former competitors combine to eliminate duplicate track or yards.) The proposed mergers were as follows:

- The Burlington Northern and the Frisco, to run from the Pacific Northwest to Florida
- The Chessie System and Seaboard Industries, to form CSX, a 27,000-mile network in the East
- The Norfolk and Western and the Southern Railway, to be called Norfolk Western
- The Union Pacific, Missouri Pacific, and Western Pacific, to be called PacRail

(The first two mergers took effect in 1980, the third in 1982. The PacRail merger is still before the ICC. Industry analysts expect the ICC to approve it soon.[69] The mergers are likely to create a system of 6 or 8 transnational railroads.)

In addition to the liberal environment for mergers, the railroads involved found the prospect of large-scale mergers especially attractive at this time because of the growth of coal markets. The mergers would allow capital pooling for high-risk investments in coal-hauling facilities and other specialized equipment.[70] They could also increase coal marketing opportunities by providing direct links between the mines and their markets. For instance, Burlington Northern viewed its merger as an opportunity to sell more of the utility coal it owns in the Wyoming Powder River Basin. Mergers also would reduce the costs involved in interchanging freight cars between the merging lines. (Interchange costs have become more significant as a result of longer average distances on rail movements.) And the large railroads' accelerating specialization in high-volume movements of bulk commodities meant that mergers could help to balance increasingly lopsided traffic:

> Mergers can help to stabilize the traffic and earnings base for a railroad company with a limited number of commodities subject to seasonal variations or unidirectional movements.[71]

The mergers offered potential benefits to rail customers and consumers, in the form of time-savings on long shipments. Long-distance traffic, formerly shared among competitors over a segment of the proposed merger corridor, could now be withdrawn from all but the one railroad entering into the merger.[72] (Without a merger, this traffic had to be parceled out among competitors through reciprocal guarantees, backed by the ICC.) The resulting decline in traffic on the duplicative roads could present a problem to local shippers and their employees, however. Withdrawal of more lucrative long-distance traffic could result in service abandonments, reducing these shippers' transportation options, with the possibility that remaining lines would gain monopoly power and reduce service quality. Thus, one policy choice made in each merger case, although not always consciously, was where to keep local service available on a dispersed basis, and where to end the traffic dilution for greater efficiency in the long-distance bulk markets.

A second policy issue also not actively considered, was whether the mergers would encourage duplicative investment in coal facilities on competing merged systems (for instance the Burlington Northern and PacRail). By allowing mergers to eliminate one form of redundant investment, the ICC might be promoting another. The expedited merger hearings did not focus on national transportation, employment, or energy goals, however, but were instead used as a forum for negotiating inter-company conflicts of interest. Since the ICC had relinquished its authority to force the inclusion of weaker roads, it might have been expected to take a broader view of each merger, as an increment of national and regional transportation policy, ruling on the

cases as a whole rather than becoming absorbed in parochial disputes. However, as one consumer-advocate participant commented, each merger had "a life ot its own," and only industry arguments were actively considered.[73] A Congressionally-established public interest organization, the Rail Public Counsel, hired a team of economists to analyze the CSX merger from the standpoint of nationwide cost savings and overall rail service quality, but the group's testimony was largely ignored.[74]

The expedited process meant that larger railroads' internal disputes could crowd out those of smaller companies, with fewer legal resources. Although the four giant systems proposed would serve distinct regions, there are points at which they overlap and would compete against each other. The prospect of one merger approval reducing another large system's traffic resulted in an ironic mix of testimony, further demonstrating the railroads' ability to steer the public perception of events. For instance, in the CSX case in 1980, the Norfolk and Western demanded a battery of protective conditions for its own traffic.[75] N&W petitioned for a ruling that CSX be prohibited from making any changes in the schedule or service standards of the former Chessie or Seaboard lines. And if CSX were to develop joint routings between the Southeast and West with other railroads, N&W wanted a protective condition that would require CSX to offer N&W similar joint routings on the same terms. N&W asked the ICC for a promise of access to the VEPCO plant at Wheelright, Virginia, in order to "provide VEPCO an alternative carrier" and "compensate for the merger's anti-competitive effects."[76]

When it came time for N&W's own merger case a year later, however,

the themes of competition and equal treatment gave way to one of efficiency. N&W Vice President John Turbyfill applauded the unusually quick handling of the Norfolk Southern merger case, saying that the government

> "has finally realized bigger railroads are more efficient. We do what we do best, that is, haul bulk. We're like the Bell System. You don't need 50 telephone companies to make a call."[77]

Thus, efficiency and competition only entered the cases as rhetorical weapons. The same was true of energy concerns. N&W submitted three volumes of energy and environmental impact studies in the CSX case, to support its requests for protection. And the Boston & Maine Railroad claimed that the CSX merger would result in "circuitous routing that will waste energy."[78] (The B&M wanted a promise of a direct connection with CSX to "neutralize incentive for CSX to route only over its own system.")

The logic of the industry's internal struggle, and the weight of precedent for ICC adjudication, precluded any but a token representation or analysis of national policy issues. The industry continued to absorb the agency's attention in its own affairs. The implementation of railroad mergers shows once again that railroad policy is often shaped around business fairness issues. The resulting mergers may produce a more rational rail system, with better service on the railroads' major commodities. But if so, it will only be as a by-product of industry negotiation, backed as before by the regulations that remain.

Legislative rate deregulation: the Staggers Act, 1980

In 1979, after Congress had passed legislation to deregulate airlines, there was a strong momentum to develop similar comprehensive deregulation packages for other transportation modes, including trucks and railroads. The 4R Act, as noted earlier, had allowed only a modest degree of rate flexibility, although sanctioning freer rates on coal. The AAR had criticized the ICC for what it considered tentative implementation of the 4R reforms.[79]

Most railroads still wanted to preserve anti-trust immunity, but to reduce restrictions still in force on the use of contract rates and discounts. Contract rates, or rates offered to individual shippers, were only authorized in special circumstances (as in the case of piggyback traffic). All other rates had to be posted in general tariffs, and discounts, even those offered at large, were prohibited.

The industry was generally united on the desirability of contract and discount rates. The railroads were divided, however, over another prospective reform: the deregulation of joint rates.[80] Joint rate deregulation would have permitted railroads to post their own independent rates for their respective portions of jointly-handled traffic. Thus independent pricing decisions would have replaced the established practice of collecting a single shipping payment, and splitting it among the railroads according to the divisions formulas. Small railroads, particularly in the East, tended to receive internal cross-subsidies from this arrangement, and did not want joint rates deregulated. They pressured for continued ICC authority over divisions.[81] Many larger railroads, including Conrail, were interested in posting independent rates, in part for marketing image.[82]

The Carter administration proposed a bill in 1979 to deregulate railroad rates, as well as the abandonment process, more radically than any preceeding legislation. A milder form of the bill, known as the Staggers Act, was passed in 1980.[83] The Carter bill would have prohibited the use of general rate increases, eliminated the industry's anti-trust immunity, and deregulated joint rates. Railroads successfully pressed for a modfication of the bill, in order to retain these privileges in part.

The industry argued for continued exemption from anti-trust law by stressing its special status. Jerry Conlon, Vice President of the Chicago and North Western, stated that since

> "the railroad industry is a fragile, interdependent network, it deserves to have the oversight and staffing of people conversant with transportation decisions and transportation ramifications,"[84]

in short, the ICC. The railroads also continued to use the theme of financial decline promoted earlier in the decade, though on a modified basis. This time, they emphasized the need for investment capital to pursue their new opportunities in the coal and grain export markets. Thus the tone was more optimistic, or upbeat, than in the early 1970s. Imperative need was now, simply, need.

Congress adopted the railroads' reasoning in the Staggers Act. The bill's legislative intent section states:

> Earnings by the railroad industry are the lowest of any transportation mode, and are insufficient to generate funds necessary for capital improvement.[85]

The aggregate view of the industry's status lingered on from previous

lobbying efforts, so that the general public tended to equate deregulation with railroads' financial difficulties. The difficulties, in turn, were linked to the industry's vital role in the economy, another association from the past. For instance, the Northeast-Midwest Congressional Coalition wrote in support of deregulation that

> The railroad freight industry today is in a struggle for survival...Tracks are in desperate need of repair and equipment is crumbling with age. Yet the vital need for railroads to play a continuing role in our nation's transportation sector is unquestioned. Railroads transport more than one-third of the nation's intercity freight and serve as the principal carriers of coal, grain, pulp and paper products, agricultural products, chemical products, and other commodities.[86]

Of course, the "desperate" and "vital" railroads were not necessarily the same set. Rate deregulation was also likely to strengthen the railraods with fewer financial problems, that had already improved their facilities and could offer large-quantity discounts, more than the unstable ones. But the AAR's history of aggregate presentations continued to make the conceptual association between financial stability and national importance nearly automatic for many Congressmen.

Similarly, the idea that rate regulation still stood in the way of investment was questionable. The principal investment railroads now contemplated was in the coal market, which had already been largely deregulated. In fact, capital outlays for roadways and structures had begun to climb significantly two years earlier, in 1977. Between 1977 and 1981, the railroad industry's capital budgets doubled.[87] But as the Staggers Act preamble cited above demonstrates, the overriding impression was still one of insufficient funds.

Further, despite implications to the contrary, rail profitability

was increasing, according to some indicators. In 1979, of the 14 largest railroads, excluding Conrail, only one had failed to make a profit, and all but three had shown earnings growth since 1969 (see Table 9). Thus, through a combination of old and new arguments, the industry maintained a carefully balanced and aggregate image, with growth prospects on one side and deterioration on the other.

The railroads also promoted a new business fairness theme, in keeping with the spirit of deregulation. Instead of fairness between railroads or between modes, they stressed equal treatment with other industries. Assisted, perhaps, by growing public recognition that the railroad industry was no longer a quasi-utility, but was becoming a specialized business with a limited niche, railroad spokesmen were able to argue that they deserved the privileges of any other business, such as contract pricing. Although on the anti-trust front, as noted above, the industry used the opposite argument--the need for special treatment--where discount rates were concerned, rail spokesmen grew more proletarian. After the Staggers Act was implemented, for instance, Barry Combs of the Union Pacific praised the ordinary:

> "We've been having a ball! We've been having sales! You know, like K-mart--hire four boxcars, get one free. That sort of stuff was impossible before."[88]

The smaller railroads, that stood to lose out if joint rates were deregulated, also mixed financial optimism with business fairness arguments. For instance, Alan Dustin, chief executive officer of the Boston and Main Railroad argued against joint rate deregulation as follows:

Table 9: Largest 15 U.S. Railroad Companies, 1979*

Company	Operating revenues ($ millions)	Net income ($ millions)	Net income as % of oper. revenues	Earnings growth 1969-1979**
Burlington Northern	3,250	176	5.4%	42.5%
Southern Pacific	2,626	180	6.8	5.1
Santa Fe Industries	2,556	228	8.9	12.8
Seaboard Coast Line Industries	2,174	133	6.1	10.2
Missouri Pacific Corporation	2,008	180	9.0	26.7
Chessie System	1,860	120	6.5	10.8
Union Pacific	1,712	149	NA	NA
Southern Railway	1,467	161	10.9	13.8
Norfolk & Western Railway	1,449	199	13.7	9.2
Illinois Central Gulf Railroad	895	132	14.7	--
Chicago & North Western Transportation	747	4	0.5	--
Chicago, Milwaukee, St. Paul & Pacific Railroad	471	(69)	def.	--

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Table 9: Largest 15 U.S. Railroad Companies, 1979 (continued)

Company	Operating revenues ($ millions)	Net income ($ millions)	Net income as % of oper. revenues	Earnings growth 1969-1979
St. Louis-San Francisco Railway	447	20	4.4	3.5
Rio Grande Industries	324	35	10.9	17.0
Soo Line Railroad	291	28	9.5	17.7

Sources: *Fortune*, "The 50 Largest Transportation Companies," July 14, 1980 and *Moody's Transportation Manual*, 1981

** (Earnings growth is growth in earnings per share where both years show positive earnings)

* Note: excludes Conrail. This table reflects slightly different corporate entities than Table 6.

> "The Boston and Maine Railroad is presently the oldest bankrupt railroad in the United States. Deregulation of joint rates would make the Boston and Maine...and perhaps all of the New England carriers, captive railroads, which would otherwise be totally destructive. The Boston and Maine will be the first railroad in modern times to effect an income base reorganization within the confines of Section 77 of the Bankruptcy Act. I would hate to see our hopes dashed by ill-conceived and ill-implemented deregulation of the joint rate issue."[89]

In this case, the firm sought fair recognition, not for public service, but for its own corporate struggle, and did not want the rules changed before a dramatic announcement of solvency could be made.

The railroads' systematic arguments helped them modify the bill proposed by the Carter administration, to achieve a more limited deregulation. The resulting Staggers Act authorized liberal use of contract and discount rates. It did call for a phase-out of general rate increases by 1984, but in vague language by comparison with the Carter bill. The Act allows the ICC,

> if necessary, to establish a formula to compensate for inflation that may be applied to more than one carrier.[90]

This provides an indefinite loophole for the practice. And the Staggers Act partially retains the anti-trust immunity of the rate bureaus.[91] Permission was granted for independent rate-setting on joint traffic, but the bill does not prohibit joint rates. The bill authorizes the ICC to set guidelines on the matter, and continue to regulate disputes on a case-by-case basis.

The policy impacts of the Staggers Act are uncertain, in part because the Act leaves considerable room for varied implementation.*

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*That implementation is difficult to predict, since the ICC's make-up is presently mixed. Of 11 authorized seats, only four are filled, with one commissioner each from the Nixon, Ford, Carter, and Reagan administrations.[92]

Some industry analysts believe small shippers will gain more influence over rates than in the past, but lose authority over service availability and quality.[93] The discounts present an opportunity for lower consumer costs on some products (including agricultural products and paper), but service contracting may draw railroads out of less profitable grain-producing regions, with consequent economic dislocation. The development of the Staggers Act proceeded with only limited attempts to weigh these potential impacts. The railroads' careful selection and systematic presentation of popular arguments ensured that the bill would reflect the industry's narrower perception of the issues involved.

CONCLUSIONS

Despite a public impression to the contrary, deregulation of the freight railroad industry has not been a general removal of regulations, but an alteration of them. The changes were selective in several ways. Some forms of deregulation applied only to specific firms, as in the deregulation of abandonment for Penn Central. Railroads also obtained regulatory changes for specific markets, such as coal, and for large-scale traffic movements rather than rail service in general. The industry did not win every concession it sought, but it significantly shaped the terms of discussion, so that social policy concerns were seldom articulated beyond the level of catch-words. Consequently, the ICC and Congress did not make a thorough effort to predict policy impacts, nor fully consider alternative policies.

The railroads systematically chose arguments compatible with changing public opinion, to advance the form of deregulation they preferred. When united, they used an aggregate picture of the industry to present their views. Where firms differed, two tendencies can be noted. The more powerful railroads, with the most at stake, often dominated the agenda. When this was not possible, they arranged compromises that continued to implicate the ICC in the more typical internal disputes.

The firms chose both business and social arguments appropriate to 1) the particular form of deregulation they sought, 2) their relative positions within the industry, and 3) the political environment. For instance, while the central argument for higher aggregate revenues persisted throughout the decade, it shifted in form. As the early bankruptcies lost their initial political impact, the AAR was less able

to create a sense of crisis, and its arguments focused on chronic revenue shortfall. Ultimately, a note of optimism crept into the argument, and this too corresponded with the growing view that railroads should be made into profitable enterprises.

Social policy concerns such as regional employment, service efficiency, adequate market discipline, and energy use were not omitted from the regulatory agenda, but they entered it primarily on a rhetorical basis, coupled to arguments for business equity. Business fairness arguments took a variety of forms, including fair traffic shares, fair competition, fair profits, and fair treatment for the railroad industry within the wider business community. Both forms of argument, social policy and business fairness, were influential in setting the tone of Congressional hearings and ICC proceedings. But business fairness received most of the attention.

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CHAPTER THREE:
CONCLUSIONS

COMPARING DEREGULATION IN THE BUS AND RAIL INDUSTRIES

The public agenda for deregulation has taken shape somewhat differently in the rail and bus industries. In each case, the industry's structure and economic environment set boundaries on the firms' motives for entering the regulatory change process. Each industry's economic situation gave rise to a different mix of political motives and arguments. Relatively stable economic features, such as industry structure and operating practices, established the backdrop of industry concerns. Some of these had little to do directly with deregulation, but broke in much as they might have in any other federal hearing on the industry. For instance, Greyhound Lines had long sought better enforcement against unlicensed carriers, and chose deregulation hearings as an opportunity to bring the issue up again. Other longstanding concerns were more specifically tied to regulatory reform. For example, several large railroads had been interested in reform of the merger process for many years, and the industry had often sought freedom for discount rates.

In addition to the firms' longstanding interests, recent economic developments created incentives for selective deregulation in both industries. The traditional markets, scheduled bus service and rail general cargo, were declining. This, in combination with growing

markets for specialized bulk commodities and charter services, created new motives for regulatory change. Smaller bus firms were interested in extricating themselves from low profit scheduled routes, in order to concentrate more of their resources on the charter market, for which they also required entry permission. Large railroads in major agricultural and coal mining locations wanted new rate and merger freedoms. But each industry could also point to a long-term, overall decline in profitability as a justification for selective deregulation.

In addition to its economic structure and climate, each industry operates in a distinct political context, which influences its firms' ability to tune the policy-making process to their goals. The prospect of deregulation, with its promise of universal application, formed a substantial point of overlap. But the form and scope of government attention to the two industries, and the public view of their social utility, were different, and had separate implications for the way firms positioned the regulatory issues.

In each case, the firms chose their reform arguments from a range of popular themes over which they had little control. However, they chose from the available repertoire systematically, manipulating policy dialogues to suit their goals. The set of themes evolved somewhat differently between industries, since arguments were gauged directly to perceptions of what each industry (or industry segment) could provide to the public. But in each case, the arguments helped to structure the evolution of new regulatory policies with a minimum of close scrutiny to broad public and consumer concerns.

In both industries, the firms and their lobby associations used

rationales for regulatory change without much regard for consistency. The Norfolk & Western, for instance, claimed that its own streamlined merger would improve efficiency, while in the CSX merger hearings (where N&W was a vulnerable party), the firm called for a full set of traditional protections. In the bus case, Greyhound and Trailways each developed one set of arguments for state lobbying, and another for Congress. The arguments also showed little consistency over time. Greyhound first praised traditional ICC regulations for their "careful balance" of interests, then called them "archaic" impediments to efficiency when the political context changed. Another form of inconsistency appeared across lobbying objectives. When railroads wanted to preserve anti-trust immunity, they argued that special attention was appropriate; but when they sought discount rates, they claimed they should be "treated like any other industry."

The set of arguments in each industry varied with the firms' divergent motives. For instance, on the issue of forming Conrail, the Union Pacific urged Congress to intervene and save the distressed Northeastern region, while Norfolk & Western cautioned against wasting government money in this manner. When the issue of subsidies for construction of new bus stations arose in the House of Representatives, Greyhound officials contended that their own terminals provided thorough, and indeed, ubiquitous coverage, while Trailways stressed the inconvenience to passengers of existing station locations.

In each case, firms used different labels for the same policy, depending on their viewpoints. In the bus case, the terms "cream-skimming" and "route flexibility" were used alternately to designate the outcome of a freer entry policy, the first in a pejorative and

the second in a laudatory sense. The House bill refers to the need to avoid cream-skimming; the ICC bill (which Greyhound supported) mentions flexibility instead. The same discrepancy is seen in the rail case, where the terms "predatory rates" and "innovative marketing" were interchanged, depending on point of view. The Staggers Act, less conservative than the bus bill, describes the advantage of lower rate floors as the opportunity for innovative marketing.

Through the selective use of social arguments, both bus and rail firms were able to promote concepts that ultimately colored the policy dialogue, and often stood in place of genuine analysis or attention to public needs. The American Bus Association emphasized the number of locations the industry served as a justification for preserving status quo franchises. The number of locations does not measure the value of the service, and it does not address the issue of whether needs for alternative scheduled services remain unmet. But the statistic appears repeatedly in government reports and Congressmen's testimony, indicating the importance it assumed in the debates. In the formation of Conrail, the Penn Central and the Union Pacific were able to convince the general public to focus on the concept of excess lines. Their lobbying eclipsed other possible diagnoses of the Penn Central situation, such as responsibility for a fixed work force; the firm's apparently intentional disinvestment; and the possible interpretation that the bankruptcy was not even a public problem. Another example of the firms' control over the dialogue is seen in the emphasis on minimum insurance requirements in the bus hearings. Although the industry repeatedly promoted the theme of passenger safety and that of carrier fitness, Congress gave little attention to whether unlicensed

operations actually posed a significant problem for passenger safety, or for the financial health of marginal firms.

The following sections compare the two cases to see what differences may be responsible for particular features of their regulatory reform dialogues. The characteristics, or variables, considered are loosely classified as belonging to either the "economic environment" or the "political environment." While in this exploratory discussion, it would be premature to suggest a model structurally relating these economic and political variables, they undoubtedly interact, together conditioning the regulatory reform agenda in each industry. Table 10 provides an overview of potentially relevant differences in the industries' economic and political environments.

ECONOMIC ENVIRONMENT

Business motives and political rhetoric differed between the two industries in part because of their respective capital and operating characteristics; their industrial organization; and their place in the larger transportation market. Two major operating differences shaped the way firms in each industry sought, through selective deregulation, greater control over their markets. These are 1) the degree of cooperation required to handle traffic and passengers, and 2) the capital requirements of providing service.

Operating characteristics

The rail industry has been much more interdependent than the bus industry, because it is less concentrated and transportation distances are longer. Long distance shipments typically require traffic to be interchanged between rail lines at several points, with alternative

TABLE 10: Principal Industry Differences

Characteristic	Bus	Rail
Economic environment		
• industry size	• small	• large
• industrial organization	• more concentrated	• less concentrated
	• national-level firms	• no national-level firms
• operating characteristics	• relatively independent	• relatively interdependent
• markets	• passenger	• freight
	• most powerful firms occupy shrinking market	• most powerful firms occupy growing markets
• cost structure	• low capital (when government provides roadways)	• high capital (when industry provides roadways)
Political environment		
• public image	• low visibility	• higher visibility
• external organized interests	• lack of politically active consumers	• politically active consumers
• jurisdictional division of regulatory practice	• relatively strong state boards	• relatively weak state boards
• regulatory history	• shorter, more straightforward	• longer, more complex
• technologies	• relatively new technology; always had external competition	• relatively old technology; developed without much external competition

possibilities for routing the shipments onto competing lines. The complex system of rules that the industry and the ICC have negotiated for handling, and pricing, joint traffic created vested interests both against and in favor of any reforms. These interests are sometimes regionally aligned, as they tend to be on the issue of joint rates. But the alignments are generally situational and transient, which precludes the formation of coherent factions. The divisions rules and merger protective conditions are often specific to firms and locations. Each firm, including the more dominant, is vulnerable to traffic loss if the joint traffic rules are changed (or eliminated) in such a way as to remove the firm's historic advantage.

In the bus industry, the mechanism for protecting market shares is much simpler. Although the same issues of joint fares and schedule coordination occasionally produce disputes, the route franchises allow relatively independent operations without the same degree of competition on routes. (Unit costs per mile are also more uniform in the bus than the rail industry, so that joint fares can be handled on a straight per-mile formula basis.) The conflicts that arise over bus franchises are more predictable than those over joint traffic agreements in the rail case. In many areas, franchise conflicts are just between Greyhound and Trailways, or between Greyhound and a regional operator. The division of interests this situation produces with respect to deregulation is relatively clear-cut, with recognizable factions: Greyhound, Trailways, charter operators, etc. In the rail industry, the parochial nature of market disputes, and the larger number of firms involved, means that the same railroad more often emerges on both sides of a reform issue, since it may lose out in one

application of a new rule, but win in another. Thus is is harder for Congress to accomodate disputes in advance through formulaic legislative solutions.

One result of the difference in levels of coordination is that the railroad industry as a whole has pressed for greater retention of ICC authority. Few railroads have advocated the elimination of anti-trust immunity, while several bus interests did. In the rail case, also, issues of inter-company equity came up more frequently in administrative than in legislative proceedings. Bus lobbyists may have been more optimistic about successfully explaining inter-company differences to Congressmen, and winning sympathy for their positions, than rail lobbyists, who were also more familiar with the ICC's supervision than were the state-regulated bus companies.

Capital requirements

A related difference is found in the industries' capital requirements. The railroads have a much greater fixed investment in their track and facilities. For railroads, entering a new market generally means investing in improved or specialized equipment to offer qualitatively new services. Few firms contemplate constructing new rail lines, and their investment in new markets (via equipment purchase or track repair) is not directly subject to regulatory control. But the fixed nature of the investment means that each firm is concerned about protecting its existing traffic, including traffic dependent on the investment decisions of other railroads. Small firms with only a few lines are frequently concerned about losing their traffic due to the disinvestment or exit decisions of other railroads. Thus, market entry

is a minor issue, while exit liberalization poses threats (and opportunities) which, as in the case of joint rates and traffic agreements, can more easily be accommodated on a case basis.

In the bus industry, entry deregulation would inevitably change some firms' market shares, if only slightly. In the absence of entry controls, more resourceful firms could easily cut into other firms' markets, using existing equipment and publicly provided roads. And with small amounts of capital, new firms can began serving established markets. Without route controls and insurance barriers, the industry could become more internally competitive, especially on high-volume routes. Hence, each segment of the industry has taken a position on what constitutes equitable reordering of franchise rights, and adequate guarantees of fitness and safety. But the industry could agree on exit liberalization with little difficulty.

Division of markets

In both industries, the declining markets -- small-scale rail service and scheduled bus service -- are what might be termed retail markets. The relatively ascendant markets -- for specialized bulk hauling and bus tours -- are package or wholesale operations, in contrast. In each case, the established pattern of regulation had evolved to suit the retail operations, while deregulation had to take account of the different type of operation involved in volume sales. However, in the bus industry, the most powerful company, Greyhound, occupied the traditional market, while in the rail case, the most powerful firms occupy the new markets. This difference may help to explain the greater emphasis on the theme of service flexibility (as

an advantage of deregulation) in the bus industry, where the dominant firm sought freedom to shed peripheral services. In the rail case, more attention was granted to the idea that deregulation would open innovative markets. The theme of innovation was somewhat muted in the bus industry discussion, perhaps because small entrepreneurs and operations not yet formed -- who would be the natural voice for market innovation -- did not have the wherewithal to participate meaningfully in the dialogue. The large bus carriers often mentioned the possibility that new operations would spring up to take over routes that they dropped or cut back. But the possibility of altogether different types of bus services being developed was not granted much discussion, in contrast to the rail case.

Industrial concentration

In addition to market differences, the industries' relative concentration may also have affected the reform dialogues. Both the rail and bus industry are concentrated, but the bus industry is more so, and has been for a long period. Since Greyhound has a nationwide market more extensive than any railroad's, and it has unusually significant lobbying resources among bus firms, it could hope to benefit from total deregulation, and the withdrawal of anti-trust exemption. Once regulatory reform legislation became a likelihood, Greyhound advocated total deregulation. In the rail industry, no firm advocated total deregulation at any point. Thus, in the bus case, there was more use of the rhetoric of deregulation itself. Railroad spokesmen commented more modestly on the need for change, but placed more emphasis on financial arguments not specifically centered on the problem of

"stifling regulation."

The bus industry's greater concentration distinguishes the bus and rail agendas in another way. The obvious dominance of Greyhound in the public mind permits the firm to make public service claims (such as the claim of support for the U.S. tourist industry) on behalf of the whole industry. In the railroad case, despite considerable economic concentration, no one or two firms have such prominence on a nationwide level. Greyhound has an advantage that larger railroads lack, since they must rely on the merits of their own policy positions, which of course are more restrictive than the public services of the whole industry. This difference appears to have given the AAR a more central role in deregulation than the American Bus Association. On the other hand, Greyhound's dominance makes smaller firms' complaints about the problem of Greyhound monopoly power more immediately credible than similar complaints in the rail industry. With industry control more dispersed, it is difficult for the weaker rail firms to win Congressional sympathy by pointing to the specific firms they regard as aggressors. In the rail industry, to be successful, this type of claim must generally be made in a setting attuned to the complexity of the more fragmented rail market. Therefore, in the rail case, it was in individual merger and rate hearings, as opposed to legislative debates, that the smaller firms could cultivate the greatest concern for equitable treatment.

POLITICAL ENVIRONMENT

The political environment also helped determine both bus and rail firms' motives and agenda arguments. The political environment can be

said to include the common (public) view of the industry's status and public mission, the relative disposition of agencies (and jurisdictions) to see policies in a manner consistent with industry views, the external interests, and the nature of Congressional attention to the industry's concerns.

Public Image

One similarity between the bus and rail industries' political milieu was the public perception that each was the underdog among its competitors, in the intercity passenger and freight markets, respectively. The idea that scheduled bus service or general cargo rail transportation form essential public utilities lost some of its force as their market shares declined. Hence it was not difficult for the lobbyists to argue that the firms should be treated like any other businesses, rather than being relegated to stand-by service in the shrinking markets. The declining significance of each industry made their arguments for greater efficiency relatively promising. Had the industries appeared widely important (for instance, as the airline industry does), proposals for increased efficiency might have aroused more concern about possible service cutbacks. But in the rail and bus industries, more remote from everyday consciousness, one is perhaps less likely to think of service cutbacks when hearing the word "efficiency." Freight transportation has lost its reputation as the backbone of the economy, and intercity bus services have a much lower political profile than Amtrak. If the industries were to continue to function profitably, it seemed appropriate to many people that they do so by scaling down to more limited niches.

The public's view of the two industries was quite different,

however. The rail industry had long been considered an important piece of U.S. economic infrastructure, and it had major symbolic associations that militated against radical shrinkage of the system. The bus industry, by comparison, was never part of the economic mainstream. It was always a secondary mode of travel, first while rail passenger travel dominated the market, and later overshadowed by auto and air travel. This difference may partially explain the bus industry's greater reliance on a theme of service to dependent populations, which contrasts with the rail lobby's emphasis on financial decline. The bus industry evidently hopes to win recognition by focusing attention on its <u>customers</u>' needs, whereas rail firms more often focus attention on their own needs. Of course, social dependency themes are more easily brought to the forefront where services are intended for household rather than industrial consumers, so part of this distinction may be due to the different images passenger and freight service project. The bus industry also had few visible bankruptcies to point to in making its claims. (Bankruptcies are common among the independent operators, but attract only local attention.) But vulnerable railroads, seeking traffic guarantees, have also used social dependency arguments on occasion, referring to small farmers, lumberyards, or rural towns that appear to depend on rail service for survival. The fact that such arguments are infrequent, in contrast to the bus firms' social dependency arguments, still needs explanation.

Another possible reason for the bus industry's greater use of humanitarian appeals is its lower public visibility. For bus industry needs to be taken seriously from a national perspective, the bus lobby had to form an association between the industry's financial con-

dition and the social services it performs. The rail lobby has not had to actively cultivate conceptual associations between the industry's financial status and broader public needs, such as regional employment, the overall condition of the economy, or service to export markets. These associations tend to be automatic, and seldom critically evaluated, so the rail lobby is free to work on reinforcing them. Hence the industry has relied in its lobbying efforts on the overall premise that the industry must be financially sound, and the related assertions 1) that it is not sound now, but 2) it could become so. The threat to the public of a weak railroad system was often implied, in the nature of a warning, rather than spelled out directly, in rail executives' testimony. To the extent the rail lobby has taken up new themes such as energy and environmental conservation, these are icing on the cake of financial necessity. Since the bus industry is so much less prominent, even its broad economic rationales (such as service to tourism-dependent regions) had to be specifically constructed for the debates on regulatory reform. Also, since scheduled service passengers form a minority group, the industry can appeal to its customers' special situation, when this suits the policy position taken. This is more difficult for railroads, since even the more vulnerable groups of shippers tend to have organized lobbies known to the ICC and Congress, and capable of making their own presentations.

Regulatory history

The rail industry's more prominent status within the transportation market also accounts for the more complex, evolutionary nature of the rail regulatory reform process. Congressional attention to the

bus industry is embryonic, since bus legislation is undertaken infrequently. The deregulation bill was a novelty both to Congress and the industry. Rail deregulation has had a longer history, both as a concept and a policy. The ICC had liberalized service abandonments and special rates on piggyback service in the 1960s, for instance. And the rate structure reforms of the early 1970s preceded the emergence of deregulation as a popular concept. By contrast, deregulation of the bus industry is a recent development, beginning with administrative liberalization of interstate entry controls during the late 1970s.

Deregulation of the bus industry has been described as an afterthought. Legislation deregulating the airline, trucking, and rail industries created a precedent for changes in bus regulation, as the last regulated transportation industry to be discovered for application of a general principle. Bus deregulation was also in part a direct response to airline deregulation, which threatened some bus firms' revenues, and to the creation of Amtrak. Bus industry lobbyists acted with the awareness that the industry would seldom arrive on the national agenda. Many firms appeared to view it as their one opportunity to achieve, or block, reforms. The railroad industry, in contrast, experiences new legislation each year, and is able to rely on greater recourse to the ICC if unfavorable legislative reforms pose a problem.

Interjurisdictional divisions

Another difference in the course of deregulation stems from the historic discrepancy in federal and state regulation of the two industries. In each case, state regulation initially formed the more significant controls. In the rail case, however, state supremacy was large-

ly eliminated through preemptive legislation in the early 1900s. During the period of rapid inflation beginning in the late 1960s, railroads successfully pressed for the elimination of vestigial state control over intrastate rates, and Congress established that these rates would be pegged to ICC decisions on nationwide rates. The current bus legislation represents the first instance in which the bus industry has been able to achieve public attention for similar measures. So while each legislative reform prospect in the rail case drew out classic arguments often used in other rail policy-making contexts (e.g., the competitive or anti-competitive effects of specific rate changes), in the bus case, the potential for a novel legislative compromise made room for new arguments.

Table 11 summarizes the differences in the regulatory reform agendas of the two industries. Some of the differences observed can be attributed to distinctions in both the economic and political environments. For instance, federal bus legislation was more of a novelty, and arguments were developed specifically for legislative lobbying, probably both because the industry has a history of state regulation and because it serves a small market not integrated into the industrial economy. And the rail industry pressed for greater retention of ICC case discretion, not only because the ICC has an established tradition for resolving rail intra-industry conflicts, but also because the rail industry's interdependent operations and high capital obligations create continual, parochial conflicts in which firms cannot easily agree to abide by a general formula.

The difference in industry environments accounts, also, for the rail industry's greater use of financial themes and the bus industry's

TABLE 11: Industry Differences in the Regulatory Reform Agenda

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Differences in lobbying

- relatively stable bus factions form predictable coalitions; contrasts with situational, transient rail factions
- administrative emphasis in rail case; legislative emphasis in bus case
- total deregulation only considered in bus case
- greater agreement on liberalized abandonments in bus case
- federal legislation common in rail industry, novel in bus case
- reliance on classic federal-level arguments in rail case contrasts with newer bus arguments
- bus industry attempts to speak for its own consumers, and unlike rail industry, can emphasize social usefulness in a vacuum

Difference in nature of arguments

- bus spokesmen use social dependency themes more extensively
- rail officials emphasize financial breakdown rather than social needs arguments
- in rail case, inter-company equity arguments predominate in administrative rather than legislative setting; bus officials more readily employ fairness arguments in both settings
- rail industry can play on major symbolic associations
- in rail case, more attention given to prospect of innovative marketing; in bus case, more attention to service flexibility

greater reliance on social utility themes, although the precise source of this difference is hard to pinpoint. It could be attributed to the distinction between passenger and freight services; to the absence of organized bus consumers; or to the bus industry's lower visibility and frequently negative image. The rail industry seemed to benefit from public assumptions that railroad profitability is a legitimate public policy goal in itself. And the composition of the industries may account for the greater emphasis on service flexibility and exit freedom in the bus case, and marketing innovations in the rail case.

AGENDA-SETTING: ADDITIONAL CONSIDERATIONS

Other interest groups

The bus and rail cases show that transportation firms have had a major influence on the deregulation agenda in Congress and in other agencies. However, their influence does not exist in a vacuum. For a more sophisticated understanding of the regulatory reform process in transportation, it would be necessary to consider the political influence of other business interests beyond transportation firms, such as the oil companies. One critic of the Conrail plan, for instance, charges that it was a "deliberate blueprint for the destruction of the northeastern railroads," perhaps engineered by the "highway, oil and aerospace interests that financed and otherwise dominated the Nixon administration."[1] It is not necessary to find active conspiracy, however, to appreciate the possibility that business groups more prominent than the transportation companies themselves may have played a subtle role in the deregulation debates, not captured in this discussion. A fuller understanding of rail rate deregulation, for instance, could require detailed research on the grain export industry's participation, not only in the Staggers Act, but in rail policy-making generally.

Labor groups and public officials bring their own set of arguments to the debates over bus and rail regulatory reform. The major intercity bus unions opposed deregulation, since they were concerned that liberal exit policies would scale down the size of the industry. The rail unions took a variety of stands on the reform measures discussed earlier, and were influential in obtaining the labor protection provisions in the 3R Act. For a complete account of the reform agenda

in each case, it would be necessary to compare the arguments of labor and political leaders (including state-level officials) with those used by firms and industry spokesmen. In some cases they are similar. For instance, the United Transportation Union leaders often commented on the energy efficiency of railroads when arguing for policies favorable to their own companies' business volume.[2] And governors have testified against unfair treatment of their states' industries by the rail rate structure. But it would obviously be useful to consider the interplay of the industries' own rationales with those of other participants. In this connection, the degree of inter-regional conflict over federal policies toward the industry could also be important. For instance, since on average railroads serve wider geographic markets than bus companies (excepting Greyhound), rail regulation is more likely to be a divisive issue regionally. (In Congress, inter-regional conflict over rail policy has been considerable, while there tends to be less of it in the case of trucking.)

The role of organized transportation customers in setting the reform agenda also deserves greater consideration than was possible here. In the rail case, large shipping interests could benefit from contract and variable rate authority, while smaller rail-dependent firms organized against the service disruptions and rate increases they feared would result from the rate freedoms. The compromises worked out in the formation of Conrail and in the Staggers Act reflect the additional complexity of customer involvement, lacking in the bus case. The agreements railroads work out with large shippers, outside of the regulatory process, also undoubtedly figure in the development of the rail policy debates. (In the bus case, the only external in-

dustry significantly dependent on policy outcomes is the packaged tour industry, which has generally sided with bus lobbyists' requests for reduced tour certification requirements.) The lack of politically active groups external to the bus industry, in contrast to the rail case, may have implications for implementation of the reforms. It may be politically less expensive to experiment with bold reforms -- and thus bolster the appearance of satisfying an ideological clamor for deregulation -- when the regulated industry is not enmeshed in a tangle of related business interests. Bus deregulation would thus be easier for an administration to contemplate than rail, truck, or airline deregulation. And in fact, while the Reagan administration claims to favor complete deregulation of the bus industry, and has not endorsed the compromise bill passed by the House, the administration is implementing rail and truck deregulation quite conservatively.

Another question to consider is to what extent the industries' lobbying efforts represented long-run political strategy, and to what extent they were purely reactive to externally determined events. For instance, Greyhound simply reacted to the propsect of bus deregulation, but the Union Pacific may have prepared a strategy in advance of the Penn Central's threatened abandonments. The task of isolating firms' motives for regulatory reform, and ascertaining the degree of corporate planning involved, sometimes requires consideration of a larger conglomerate of which the transportation firm may form only a small part. In the case of railroads, complex stock ownership patterns and interlocking directorates can make determination of any given rail manager's ultimate motivations very difficult: ownership mysteries of this sort generally pose a problem for more thorough research on the

topics outlined in this paper. Some comparison with other industries could be useful in distinguishing strategy from reaction.

Comparison with other industries

An extended comparison, incorporating the airline and trucking deregulation processes, could provide more insight into the way regulatory reform arguments develop. The bus and rail cases may differ in some respects from the airline case, since they involved the ICC, a unique institution and the oldest federal regulatory agency. The ICC has an unusually large body of regulatory case law, and is geared up to consider business fairness arguments in every conceivable permutation. Industries regulated by a less formal, adversary procedure may be less likely to construe their policy arguments in equity terms. Comparison with non-transportation industries would also reveal a different use of strategy and rhetoric in the regulatory reform process, and suggest which of the features of industrial organization touched on here are most promising clues to understanding the reform process. The nature of the bus and rail industries as systems of "rivals and joint venturers," particularly noticeable in the rail case, may be atypical for regulated American industry. In cases where regulated firms are competitors without a high degree of mutual dependence -- as in the pharmaceutical or broadcasting industries, for instance -- the deregulation process is perhaps less likely to give rise to a coordinated, compromise strategy among firms.

Within the transportation field, airline deregulation might provide the most instructive comparisons to the bus and rail cases. Similar issues arose in the legislative agenda for airline regulatory

reform. For instance, Congress gave considerable attention to what was considered the "problem of small communities." As in the cases here, the firms were split on the form of legislation they supported. Five of the large airlines advocated complete deregulation (American, Continental, Delta, Trans World, and United), while the others wanted joint tariff powers and antitrust immunity.[3] And the chief industry trade group, the Air Transport Association, presented an extensive array of industry-wide social arguments for more favorable regulation.

Concurrent policy changes

To fully understand the selective nature of regulatory reform it would also be desirable not only to make cross-industry comparisons, but to consider concurrent policy changes that may escape detection in the course of reform discussions but still be significant, either in tracing firms' motives for reform, or evaluating the outcome of deregulation accurately. Many rail firms, for instance, will realize large cash flow improvements as a result of changes in accounting methods for track and other fixed assets, owing to the National Recovery Tax Act of 1981.[4] It would of course be spurious to attribute the resulting profits to rate deregulation, yet industry spokesmen are likely to attempt to do so, in order to preserve or extend their gains from regulatory reform (by showing that deregulation "is working"). In addition to the tax code, two other policy areas that deserve consideration in tandem with regulatory reform of each industry include the bankruptcy laws, and government regulation of labor relations.

Secular ideological changes

In order to fully understand the formation of regulatory policy in these industries, it would be necessary to look beyond businessmen's statements at more global changes in public opinion. The rationales that business groups use emerge from a complex mixture of conceptual habits and ideologies, cultural as well as political in origin. For instance, the railroads' introduction of efficiency arguments in the late 1970s was probably due to the resurgence of efficiency as a popular concept in the U.S., rather than simply to the railroads' renewed interest in acquiring high-yield equipment. The difficulty of distinguishing the firms' own ideological creations from broader undercurrents of public opinion makes it hard to trace the effect on policy of a switch from one argument to another.

To understand the conceptual power of business fairness principles, for example, requires identifying their ideological origin. The theme of business fairness seems particularly enduring in American politics, while others (such as the resource conservation theme) emerge only periodically. Business equity as a controlling idea may be derived from early American culture; yet the quasi-judicial procedures of the ICC no doubt helped endow this theme with the high regard it now enjoys in transportation policy. Whether the concept made its appearance on the regulatory reform agendas through habit, or whether the specific uses devised by bus and rail firms were themselves critical policy determinants, is a question beyond the scope of this discussion. Yet more exploration might help to distinguish universal from idiosyncratic features in the cases examined here. It might turn out, for instance, that the threat of business failure always has a major role

in shaping the course of regulatory reform. Business failure, and public intolerance of it, may serve as a major catalyst for significant restructuring of government involvement in other regulated industries. Every bankruptcy in a regulated industry can potentially be pinned on the unfairness of regulators, as well as on poor management or exogenous market conditions. The threat of bankruptcy may serve to discipline regulators not only because of direct pressure from the concern involved, but because to allow the firm to fail, even if the reasons lie elsewhere, appears unfair.

A final puzzle that a study of regulatory reform cannot in itself solve is the nature of the mechanism by which firms' social arguments actually exert their influence in policy making. I have implied that industry rationales are powerful because they genuinely convince their listeners. Yet one may raise the objection that Congressmen or ICC personnel are in a position to spot the posturing in the lobbyists' policy statements: after all, they hear them every day. They may respond favorably because of direct pressure, while remaining indifferent to the intellectual arguments the firms advance. The arguments, or window dressing, may be so transparent in many cases as to provoke impatience with the speaker; or they may simply serve as a polite ritual. Why, then, bother to examine their conceptual origins and the instances in which they are used?

Clearly, conceptual and ideological tools do not do all the political work by themselves, and they vary in their forcefulness. However, the power of window dressing should not be underestimated on the grounds that some actors _realize_ it is window dressing. Indus-

try rationales or postures may still do much to influence not only the choice of a general policy direction, but also the details, which often come to have their own importance. And if the general public does not recognize window-dressing, Congressmen and administrators may use the same suspect arguments to justify unwarranted decisions to their constituencies. At this point, of course, the politeness ends. For instance, in recent testimony before the Joint Economic Committee, ICC Chairman Reese Taylor defended his retreat from truck regulatory reform by saying:

> "The Commission is beginning to receive a number of rate tariffs that appear to be predatory. The ICC has the responsibility to ensure that rates are not anti-competitive."[5]

It would not be surprising to hear this phrase used ten years from now, and after two more deregulation bills were passed. One may regard it skeptically, but it must be credited with some power of its own, apart from that of its users.

In another instructive example, one can see the same kind of independent power in the business fairness principle, despite the complete transparency of its use. Pressed by the Water Transport Association, Representative John Dingell of Michigan has proposed that the ICC reopen an old grievance and review the amount of land grant assistance given to the rail industry during the nineteenth century, as part of a pending rail merger case. The Water Transport Association recently charged that the rail industry received unfair subsidies at that time, and has hired a consultant to prove it.[6] Bennett Whitlock, president of the American Trucking Association, has jumped on the land grants issue as well:

> The railroad industry to this day continues to be the beneficiary of what must be the biggest government give-away program in history -- the land grant program of 1850. The railroads nuzzled up to the public trough then, and they are still there today. [7]

In this statement, the ATA obviously wanted to create the impression that the federal government has been unfair to truckers (in this case, not to any particular firm, but to the whole industry). The argument is unabashedly aimed at preventing Congress from imposing new highway user charges on trucking firms. One may easily dissect the statement, and reject the equity contention as a simple facade for industry factional interests. The statement even seems absurd: the government is to compensate truckers for damage done to them before the invention of the truck! Yet whether or not this statement directly convinces any Congressmen, or helps truckers to stall the imposition of new highway charges, the unfair land grants argument must be effective on its own merits, since the railroads' competitors have been using it for at least forty years. Perhaps it creates a lingering impression of an injustice done, even as it gives away the ulterior motive it cannot actually hide. By absorbing attention from genuine public concerns, business fairness arguments of this kind, and spurious social utility arguments, reduce the prospects for developing reasonable policies. More attention should be given to the specific ways that they influence the policy-making process.

CHAPTER THREE REFERENCES

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