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THE SURFACE TRANSPORTATION SECTOR IN A COMPETITIVE ERA: EFFICIENCY AND INNOVATION IN PRICING AND OPERATIONS

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INTRODUCTION

The past four years have marked the most dramatic change in federal regulatory policies since the New Deal. Government controls over pricing and operations have been removed or substantially reduced in the crude oil, natural gas, banking, communications, trucking, airline, and railroad industries. As this roll call indicates, the transportation industries dominate the growing list of those freed from federal economic regulation. The states have also begun to curtail economic regulation, particularly in the transportation area. Florida, for example, has completely deregulated trucking; other states, among them California, New Jersey and Alaska, have sharply reduced their regulatory control over that industry.[1]

During the course of the debate over deregulation of the transportation industries, attention was often focused on various predictions concerning the likely effects of these changes. The speculation continues even now that many reforms are in place, but it has changed in a fundamental respect because passage of the reforms has driven home the importance of planning for change to the real actors in deregulation: the companies themselves.

There are two basic factors which will determine the outcome of the return to competition in the surface transportation industries. The first is the shape of the reforms themselves. Since the reform statutes do not totally deregulate these industries, the residual provisions and implementation policies of the Interstate Commerce Commission (ICC) may have a significant effect on the outcome of the move into an era of competition in these industries.[2] It may have different effects than the total elimination of regulation, as in the case of intrastate trucking in Florida. Residual ICC regulation, however, will be significant only in the short run. Governmental policy has been fundamentally redirected

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1. Hayward & Grindstaff, Internal Joint Memorandum, United States Department of Transportation and Interstate Commerce Commission, October 16, 1980. Many other states, including Texas, Maine, Michigan and Pennsylvania, are also considering removing or drastically reducing economic regulation of the trucking industry. Voters in Arizona recently voted two to one in favor of eliminating trucking regulation over the next two years.

2. The statutes referred to are the Motor Carrier Act of 1980, Pub. L. No. 96-196, 94 Stat. 793, the Staggers Rail Act of 1980, Pub. L. No. 96-448, 94 Stat. 1895, and the Household Goods Transportation Act of 1980, Pub. L. No. 96-454, 94 Stat. 2011.

toward pro-competitive ends, and enhanced competition will subject business decisions to the guiding influence of the marketplace.[3]

The most important factor affecting the impact of deregulation is the reaction of the industries themselves to competition and greater operating flexibility. Whether transportation interests succeed or fail in the demanding free marketplace, will depend on the decisions, skills and resources of individual executives.

This article will outline some of the choices which transportation industry executives will confront in the imminent competitive era. The discussion presents one view of the challenges which attend the rapid deregulation of transportation industries, and examines the policies individual firms may adopt to meet those challenges. Appropriately, individual executives will provide the answers to the questions this analysis raises as they bear the risks and rewards of the marketplace.

THE IMPORTANCE OF CORPORATE DECISION MAKING

One of the fundamental changes precipitated by deregulation is the dramatic increase in the importance of corporate decisionmaking. Under restrictive regulation the operational and marketing decisions of individual companies was severely constrained. For example, it was futile to consider a major alteration in the scope of the territory served if there was minimal chance of securing ICC approval. There was little incentive to consider basic changes in routings if one could not hope to receive ICC approval for abandoning unprofitable rail lines or altering trucking certificates mandating the use of specific highways, one-way movements, or prohibiting service to intermediate points. It was senseless to design new marketing strategies based on innovative ratemaking schemes when both the industry rate bureaus and the ICC frowned on any deviation from traditional uniform rates and ratesetting practices. Unfortunately, many companies never developed the ability to consider these types of fundamental business decisions on an ongoing basis because they spent their growing and maturing years under restrictive regulation that minimized managerial discretion and made strategic planning irrelevant.

By restoring managerial discretion to the transportation industries, deregulation makes consideration of these basic decisions necessary. The accompanying stimulus of new competition, both actual and potential, requires executives to reevaluate business alternatives and choose the correct ones in order to survive. Having received substantial control over the territorial scope of their service, each firm must now choose its market area based on operating costs and characteristics, the service requirements of its current and future customers, the level of competition expected, and its overall marketing strategy. Having received substantial freedom to set rates without governmental interference, individual firms must devise pricing strategies which meet the test of vigorous competition.

3. See Gaskins & Voytko, *Managing the Transition to Competition*, LAW & CONTEMP. PROB. (forthcoming spring 1981) (detailed discussion of the effect of various types of regulatory reforms on the transition from regulation to competition).

In short, the lifting of restrictive regulation has dramatically increased the fundamental choices open to each firm. Due to the passage and successful implementation of the various reforms, the corporate decisions of industry management have assumed much greater importance than the regulatory decisions of the ICC.

One of several clear illustrations of this point is the reaction of the railroad industry to the complete deregulation of fresh fruit and vegetable shipments. The percentage of total fresh fruit and vegetable traffic carried by the rails had declined so drastically, from 21 percent in 1975 to a mere 11 percent in 1978, that it was not an obvious target market for new business development by individual railroads.[4] Nonetheless, the consultant studying industry reaction to deregulation of this traffic concluded that the railroads, with some effort, could have exploited this market by aggressively marketing the innovative perishables transportation programs they developed under traditional regulation.[5] The railroads, however, made no effort to attack this market until total deregulation finally compelled rail management to act.[6]

Once deregulated, they responded by developing a comprehensive program specifically designed to exploit this market. They made deliberate choices regarding the specific level of service they were prepared to offer and the pricing strategy they intended to follow. Significantly, the railroads that developed and implemented these strategies were successful. The Santa Fe Railroad, for example, increased its fresh fruit and vegetable carriage by more than 78 percent in just eight months.[7]

Another example is the extension of Blue Label air-motor express package service to ten mid-western states by United Parcel Service (UPS) immediately after deregulation of express air freight movement. Again, deregulation offered carriers an opportunity to attack a market in practically any way they chose. Anticipating this change, UPS decided to offer this specifically designed service with a complementary pricing structure. The advance planning allowed them to put the program in place the very day deregulation became effective.[8]

UPS has also developed an unusual strategy for reducing empty mileage. Because there is a greater volume of parcels moving from the east to the west coast, UPS trailers often returned eastbound empty. Management decided to equip these trailers with refrigeration units and compete for eastbound fresh fruit and vegetable traffic which has the opposite traffic imbalance.

Although this strategy is hardly revolutionary, one must recall that UPS is an extraordinarily specialized carrier of small parcels. The deliberate shift to

4. Manalytics, Inc., Exempt Rail Transportation of Fresh Fruits and Vegetables: Initial Impacts, ICC 80-M-1159, (March 1980) (hereafter cited as Manalytics Report).

5. *Id.* at 7.

6. The consultant's report repeatedly stressed the change in the psychological climate brought about by deregulation of this traffic. *See id.* at 7-8, 88-90.

7. Office of Policy and Analysis, Section of Rail Policy, Interstate Commerce Commission. For additional information on the resurgence of rail transportation of perishables, see *Perishables: Hitting the Comeback Trail,* RAILWAY AGE, April 28, 1980, at 22-28.

8. *See UPS,* Press Release (July 1, 1980). UPS Blue Label Air Service is unique in that it offers low-quality air parcel service with guaranteed 2 day transit for less than 50% of the cost of overnight service.

perishables to fill an important gap in their system was a significant departure from their routine operating patterns. Moreover, UPS had operated for years only within the regulated freight sector. Its excursion into unregulated perishables transportation illustrates how innovativeness and flexibility can lead to competitive advantage.

These are examples of the kinds of corporate decisions which have become increasingly important under deregulation. Just as firms throughout the rest of our economy continually make decisions on product and service options and pricing strategies, successful transportation companies will begin to address these choices as a routine part of doing business.

Decisionmaking Within the Corporation

During the era of regulation, much of the control over operations and pricing resided with regulatory authorities in Washington. Lawyers serving the transportation company became extraordinarily important players in corporate decisionmaking. This was only natural as the ICC, traditionally run and staffed by lawyers, received information from the regulated industries primarily through lawyers in the form of legal briefs and submissions. More importantly, the deciding factor in a firm's proposed operating or pricing decision was usually the Commission's determination of its lawfulness, rather than its potential as a business tactic or strategy.

As deregulation returns the responsibility for decision to transportation companies themselves, the decisionmaking process of those companies will likely undergo a concomitant revision. Removing regulatory restrictions eliminates or dramatically reduces the importance of legal components in these decisions. The wider range of business discretion increases the importance of transportation managers, those personnel responsible for operations, pricing and marketing, who devise and implement transportation service.

The case of fresh fruit and vegetables again provides a clear illustration of this change. In taking advantage of the regulatory exemption, the railroads devised a transportation program made up of three basic elements: improved service, flexible rates, and aggressive marketing. This approach required a coordinated effort by those divisions of the corporation whose previous activities had often been subordinated to regulatory requirements.

Improved service, a crucial element in the transportation of perishables, was essential if railroads were to compete successfully with exempt trucking, long the industry leader in perishables traffic. Success required careful and continuing attention to routings and transit by the operations personnel. Improved transit times were established and apparently have been a major factor in the resurgence of the railroads in the transportation of perishables.[9]

Flexible pricing was also part of the railroad's successful entry into the perishables market. When this traffic was deregulated pricing and marketing groups, whose regulation era activities were largely confied to rubber stamping

9. For example, Southern Pacific reported a 30% improvement in turn around time for refrigerated cars, effectively increasing the supply of these cars available to shippers by an equal amount. Manalytics Report, *supra* note 4, at 87.

collective action on rates, came to the forefront with innovative pricing schemes. In order to compete with truck rates, two major rail carriers of perishables, the Southern Pacific and the Santa Fe, established rates which fluctuated daily to match the supply of rail cars to demand.[10] This represented a startling departure from the ratemaking system utilized by the rail industry under restrictive regulation.[11]

The exemption of perishables also spurred the marketing activities of the railroads for agricultural products in general. The effort to redevelop this market included the establishment of more frequent contacts with the perishables growers, special marketing units within the railroad for this traffic, and communication systems giving shippers up-to-date information on rates. These developments, along with the concomitant increase in the importance of marketing units within the railroads, have been an essential part of the coordinated program implemented to compete with the rates and services offered by truckers.

The obvious lesson in the fresh fruit and vegetable experience is that successful exploitation of new business opportunities under deregulation requires a deliberate and coordinated response. The need for this kind of response will increase the importance of competent and imaginative participation by the operations, pricing, and marketing arms of the firm. Already, at least two major trucking companies have set up separate marketing and pricing departments headed by personnel brought in from the recently deregulated air freight business.[12] Trucking companies and railroads who simply rely on collective or routine average rate increases to recoup escalating costs are unlikely to succeed in a vigorously competitive environment. There is every reason to believe that the advent of competition in surface transportation will strengthen a variety of key departments outside the corporate general counsel's office.

STRATEGIES AND TACTICS FOR DEREGULATION

Clearly, the elimination of restrictive regulation greatly enlarges the number of business options available to surface transportation industry managers. The decisions each firm makes in choosing among these options will determine success or failure under vigorous competition.

Since the first significant reforms in surface transportation regulation were introduced several years ago, firms have unveiled new business strategies and tactics at an accelerating pace. Some examples of these innovations are outlined below, with a discussion of their relation to specific reforms and their contribution to management objectives of operational efficiency and successful marketing. Although these tactics may be categorized according to the type of business activity affected, for example pricing, it is important to emphasize at the outset that successful business strategies most often involve a combination of coordinated tactics and changes. This coordination typified both the railroads'

10. *See id.* at 64-70.

11. The advent of flexible pricing in perishables traffic proved a boon to the railroads during the truckers strike in the summer of 1979. With the temporary drop in competition from truckers, the railroads not only gained additional traffic but were also able to raise rates to ration the available supply of rail cars.

12. Ryder Truck Lines and Pacific Intermountain Express,

experience with the fresh fruit and vegetable exemption and UPS' timely expansion of Blue Label air parcel service.

Increasing Price/Service Options

The success of UPS has shown that an inexpensive, highly reliable, but undifferentiated service can prove attractive to shippers. The success of this strategy, however, depends on tight cost controls, a determination to fully exploit all economies of scale, and a large potential market. Of the nation's approximately 950 general freight carriers, few are capable of duplicating this strategy. Yet practically all of them continue to offer a similar undifferentiated service to their customers. This has proved costly as over the past ten years major shippers have abandoned for-hire common carriers in favor of specialized contract carriers or private carriage. The common carriers now have an opportunity to regain this traffic, primarily by exploiting deregulation of the type and variety of price and service options they may offer.

One example is the ability of common carriers to write customized service contracts with individual shippers.[13] As recently as 1977, these so-called "dual operations" were expressly prohibited. When faced with the loss of a particular shipper's freight, a common carrier could offer a special rate. But the carrier was prohibited from tailoring a specific rate and service package and contractually binding the shipper. The ability to contract is crucial because a trucking company facing stiff competition would feel far more secure about setting rates much closer to costs if it could rely on sole or preferred access to the traffic.

A 1978 ICC ruling, later endorsed by Congress in the Motor Carrier Act of 1980,[14] removed the prohibition against dual operations. Subsequently, at least one major common carrier of general freight has contracted to provide general freight service to a nationwide retail chain.[15] The shipper in this case, having a high freight volume and widespread distribution requirements, resembles many firms which have recently considered abandoning common carriage for contract or private fleet service.

There is a strong likelihood that other general freight common carriers will take advantage of deregulation to engage in dual operations. It enables them to depart from the undifferentiated service offering and retain freight volume through expansion of price and service options. Dual operations also offers the potential for reduced costs where some or all of the contract service can be channeled through existing common carrier network operations.

Another area where the ability to offer an expanded range of price and service options may prove important is the transportation of household goods. In the past the ICC did not consistently support the few sporadic efforts by household goods carriers to provide different levels of service at different rates.

13. These carriers must first acquire a contract carrier permit from the ICC. Passage of the Motor Carrier Act has made this a relatively simple requirement. Motor Carrier Act of 1980, Pub. L. No. 96-296, §10(a), 94 Stat. 793.

14. *Id.* §10(b).

15. McLean Trucking with K-Mart, Inc.

Congress, however, in both the Motor Carrier Act and the Household Goods Transportation Act, required the ICC to encourage these options.[16]

At least one household goods carrier has already implemented an operation offering three different price and service options.[17] Experience in nearly every other sector of the economy suggests that exposure to competition will lead to widespread adoption of price and service options throughout the household goods movers industry. It is not clear, however, whether it will be more efficient from both operational and marketing perspectives for individual firms to offer a range of options or to specialize in a single price and service combination. The advantages and disadvantages of each strategy are relatively clear. A firm which chooses to offer a range of options has a much broader potential market. But such a firm may fail to establish a strong and differentiated corporate image that is easily recognized by consumers. Furthermore, offering multiple levels of service leads to higher average costs for each level. In contrast, a moving company which chooses to specialize, for example, in low cost, low quality service could establish a clear market image and perhaps achieve lower operating costs. But by specializing in one end of the price and service spectrum, the firm automatically reduces the size of its potential market.

The increase in rail service contracts clearly illustrates the trend away from undifferentiated transportation service offerings toward the development of flexible, specialized price and service options. Over the past six months, railroads have filed 66 new contracts with the ICC. The terms of the individual contracts vary enormously. Moreover, these new offerings differ radically from the price and service packages offered by these same shippers under traditional tariffs.[18]

Eliminating Operating Inefficiency: Routing

Restrictive regulation severely hindered surface transportation industry efforts to develop efficient and cost-effective routing practices. Though employing different methods, both the Motor Carrier Act and the Rail Act removed these restrictions. As these industries enter into an era of open competition, they have the opportunity to minimize the costs of providing a given service through revised routings.

The most comprehensive response is expected from the motor carriers, because routing regulation of that industry has been totally abolished. Nevertheless, the results of this shift toward more direct and less costly routings will probably have a limited impact on profits. Lower fuel and labor costs will be offset by improvements in average transit times, added competition from carriers now able to compete because of their access to less costly routes, and the resulting lower rates as competition forces companies to pass along the cost reductions.

16. *See* Household Goods Transportation Act of 1980, Pub. L. No. 96-454, §§2, 4, 94 Stat. 2011; Motor Carrier Act of 1980, Pub. L. No. 96-296, §4, 94 Stat. 793.

17. Interstate Van Lines.

18. For a more detailed review of these first contracts, see Contract Advisory Service, Interstate Commerce Commission, Summary of Initial Rail Contracts (July 17, 1980). *See also* Malone, *Contract Rates are Catching On*, RAILWAY AGE, September 29, 1980, at 32-34.

Railroad reaction to greater routing freedom is likely to differ greatly in some respects. It will proceed in a more deliberate fashion due to: the physical aspects of routing, i.e., the greater frequency of joint rather than single line operation; the railroads' current lack of information on the relative efficiency of alternative routings; and the method by which rail carriers must terminate some routings if others are to be favored. At the same time, reexamination of the relative efficiency of alternative rail routings may profoundly affect rate levels. Railroads will then have a better understanding of the cost-efficiency of particular traffic flows, and may, therefore, make the rate adjustments necessary to cover costs.

The Rail Act gives railroads greater freedom to readjust joint agreements on rates and routings with their interline partners. Already, the railroads are taking steps that will eventually shift traffic toward the most efficient routings. One railroad has developed a simple but effective means of identifying inefficient routes. By systematically analyzing the relationship of revenue and mileage in each of its various traffic flows, it discovered that routing circuitry was leading it to carry many carloads for which costs exceeded revenues by a substantial margin.[19] This unprecedented systematic examination has led not only to a review of this railroad's single line traffic, but also to a fundamental revision of its operational relationships with its interline partners.[20]

Eliminating Operating Inefficiency:

Private vs. For Hire Carriage

Those interested in the response of motor carriers to deregulation have focused most of their attention on changes within the fore-hire sector of that industry. This sector, however, represents less than one-half of the entire trucking industry. Private trucking operations constitute the largest single industry segment based on gross carrier tonnage. Those who own and direct these private fleets face an important descision following deregulation: whether to continue operating their private fleets utilizing deregulation reforms to increase efficiency, or to eliminate them and rely instead on the increasingly competitive for-hire carriage industry.

Over the past decade shippers have steadily increased their reliance on private fleets. Private fleets were not hampered by regulations restricting service areas and routings, as were for-hire carriers. Until the advent of the trucking reforms, however, these private fleets could only carry traffic generated by their particular corporate progenitor. This restriction caused many private fleets to run empty much of the time. Apparently, many shippers preferred even this

19. This preliminary analysis, conducted over the past two years by the Southern Railroad, suggests that revenue and cost relationship among carloads varies widely and includes net losses in many instances. *See* Armstrong, *Rate Structure Analysis: Plotting in Color Yields Valuable Insights*, RAILWAY AGE, May 26, 1980, at 45.

20. After years of dispute, the Southern and Conrail, its major interline partner for north-south traffic, recently announced a new agreement covering routings and rates on certain categories of interline traffic.

grossly inefficient mode of operation to the fragmented service and excessive rates of the regulated for-hire sector.[21]

Now that private trucking operations have been deregulated, their shipper/owners are presented with a dilemma. On the one hand, they could take advantage of the rights to haul the traffic of their wholly-owned subsidiaries for pay and operate as general for-hire carriers, thus increasing the efficiency of their existing private fleets. Conversely, they could abandon private carriage and employ transportation specialists in the for-hire sector, which will be more efficient and responsive in the post-regulation free market.[22] Some shippers with unique distribution requirements, especially those whose marketing strategy emphasizes transportation, may well take the first course of action: more efficient private carriage. Firms with extraordinarily balanced intercorporate traffic flows and tight control over fleet operations might do the same. Many others, however, are likely to find vigorously competitive for-hire transportation less expensive and less troublesome than private fleet management. Utilization of contract carriers offering specialized and individualized shipping service is particularly advantageous. In the long run, trucking reforms may lead to decreased shipper reliance on private carriage, as well as greater efficiency in those private fleets which remain.

Eliminating Operating Inefficiency: Tariffs, Insurance and Handling

Although UPS and general freight common carriers presently serve different markets, a comparison of their operational differences is instructive. The operations of general freight common carriers typically exhibit the following features: assumption of full liability for all freight tendered them, utilization of an extremely complicated tariff system based on numerous factors including the origin and destination of the freight, the type of commodity, and the weight, density and value of the commodity and generally unsuccessful attempts to introduce mechanized handling to reduce labor costs.

UPS employs dissimilar policies: strict limitation of liability for damaged or lost freight; employment of an extremely simple tariff based primarily on weight and distance, and successful introduction of mechanized handling to perform the bulk of freight sorting. This comparison gives rise to consideration of whether the UPS system is superior, and whether it is adaptable to the needs of the general freight common carrier.

Initially, it is commonly recognized both within and outside the trucking industry that UPS is an extraordinarily efficient carrier. The purpose of this discussion is not to tout UPS' operations, but rather to suggest that trucking deregulation provides traditional general freight carriers with the opportunity to adopt some of their operational techniques. Several reasons for UPS' efficiency are obvious.

21. *Cf.* Office of Policy and Analysis, Interstate Commerce Commission, An Analysis of Rates and Costs in the Motor Carrier Industry, (April 1980) (estimate of the cost of regulation in terms of excessive rate levels).

22. *See,* Phillips, *Private Trucking: Low Profile Giant,* DUNS REVIEW, October 1980, at 123-154 (extensive discussion of the issues facing corporations using private fleets).

First, UPS uses a very simple tariff which ignores the type of freight tendered. This dramatically reduces the labor needed to complete freight transactions for both UPS and its users. In contrast, the commodity base class rate system used by general freight carriers is extremely complicated. Small errors may lead to huge differences in transportation charges. Both carriers and shippers must employ large numbers of rate clerks to collect and verify the voluminous data necessary to determine the applicable rate. This system also impedes the use of modern, efficient electronic data processing techniques for estimating and applying freight rates.

The UPS tariff system also provides a marketing advantage. Its simplicity makes their service attractive to shippers of small parcels who are neither trained nor experienced in arranging transportation. In addition the ease of transaction tends to create goodwill.

The second economy in UPS' operations is its successful program for mechanized handling and sorting. Their success in mechanizing is primarily due to self-imposed restrictions on the size and weight of the individual packages they accept. Their limited liability rate scheme is also an important component of successful mechanization. It allows them to feed all parcels, regardless of contents, into massive sorting machines by minimizing losses if the freight turns out to be too fragile for mechanical handling.

A third economy of the UPS operating system is the diminished need for insurance coverage. UPS accepts only a limited amount of liability per shipment; accordingly, insurance requirements are reduced. A critical element of the liability scheme is the use of released rates. Released rates are transportation charges which include a specific limitation on the liability assumed by the carrier for loss or damage to the freight. A complicated tariff based on commodity characteristics is unnecessary if liability is strictly limited. When transportation is performed under released rates, the contents of the box, whether diamonds or pebbles, is irrelevant to the carrier.

The Motor Carrier Act of 1980 gives all truckers the right to use released rates.[23] Thus, general freight carriers can now dispense with complex, traditional class tariffs and substitute more simple released rates. They may eliminate the additional labor costs associated with complex tariff systems while simultaneously reducing insurance costs. This would mark a major departure from traditional operating methods and would necessitate an extensive marketing effort designed to explain the advantages of the system to shippers. Nevertheless, the UPS experience has shown that reduced rates made possible by such modifications are quite attractive to shippers. The capacity to allocate risk between shippers and carriers gives truckers yet another opportunity to tailor service offerings to the demands of their customers.

REDUCING UNCERTAINTY

For a shipper, transportation is crucial to the successful marketing of his product. Buyers want to know not only the product's characteristics and price,

23. Motor Carrier Act of 1980, Pub. L. No. 96-296, §12, 94 Stat. 793.

but also its availability. Regulation, however, needlessly impedes efforts to reduce the shippers' uncertainty over transportation arrangements.

The surface transportation reforms are already correcting this unfortunate situation. One example, previously noted, is the growth of contracts in both rail and motor carriage. These contractual agreements reduce uncertainty over future rate levels and also provide strong incentives for more dependable service. Many of the rail contracts filed with the ICC contain penalties for poor performance (usually in pickup response and transit time). Some also contain rate bonuses when the railroad consistently meets or exceeds these performance goals.[24]

Several reforms contained in the Households Goods Transportation Act will enable movers to offer service guarantees to consumers. Movers can now offer consumers automatic payments for each day the carrier is late in delivering the shipment.[25] One moving company has already filed a tariff providing for a penalty of $100 per day.[26] A second device through which movers provide consumers with greater certainty is the binding estimate.[27] A binding estimate is a contract which limits the maximum rate allowable for a given household move. Although no mover has yet offered a binding estimate, several companies have the program under consideration.[28]

ELIMINATING OPERATING INEFFICIENCY: LABOR AGREEMENTS

The advent of competition in the surface transportation industries will have a profound influence on the future course of labor and management relations. Similarly, the way in which both management and labor adapt to this changed environment could have equally profound effects on the makeup of these industries.

There is little doubt that restrictive economic regulation has influenced labor and management relations in the trucking and railroad industries. Entry and rate regulations have molded the general economic and political environment in which past labor agreements were reached. In some instances, particularly in the case of the railroads, the federal government actually specified details of these agreements. Many critics of regulation have attributed high industry wages, a leading cause of inflated rates, to the abnormally high profits of regulated trucking companies. Assuming that a significant portion of the excess profits generated by protective regulation were passed on to organized labor, the advent of competition strongly suggests some fundamental changes in future wage levels.

Accordingly, the growth rate of union wage levels in the trucking industry will have to conform to the average rates of return possible under competition. To the extent that current wage levels were artifically inflated by protective

24. See note 18 and accompanying text, *supra*.

25. *See* Household Goods Movers Act of 1980, Pub. L. No. 96-454, §4(b), 94 Stat. 2011.

26. Bekins Van Lines. *See Taking Some Bumps Out of Moving Day*, BUS. WEEK, October 20, 1980, at 45.

27. *See* Household Goods Movers Act of 1980, Pub. L. No. 96-454, §4(a), 94 Stat. 2011.

28. *Taking Some Bumps Out of Moving Day*, BUS. WEEK, Oct. 20, 1980, at 45.

regulation, the rate of increase in wages will actually lag behind the rate of inflation for some period of time. If, however, wage demands cannot be reconciled with industry earnings under competition, the inevitable result will be a substantial expansion of the non-union workforce.

The evidence to date suggests that wage levels for organized labor have been falling as competition within the industry has increased. While the industry's national labor agreement has not yet been renegotiated, renegotiations are becoming increasingly common at the local level.[29] Concurrently, many trucking companies that traditionally have conducted all their operations under either the national or a local labor agreement are creating subsidiaries employing non-union labor to handle specific types of service, particularly truck-load only operations.[30]

The effect of increased competition on labor and management relations in the rail industry will be equally dramatic. Deregulation poses labor problems for railroads which differ from those encountered by motor carriers. The decline in rail activity over the past five decades led to labor agreements which focused largely on job protection rather than dramatic increases in wage levels. These job protection measures have foreclosed many opportunities to improve labor productivity and have forced the railroads to cede many types of contested traffic to motor carriers.[31]

As a indirect result, the rail traffic base was narrowed to bulk commodities such as coal and chemicals. These are the only areas where the railroads maintain a clear competitive advantage despite the failure of labor and management to improve labor productivity. This narrowing of the rail traffic base has profound implications for the structure of the railroads, virtually dictating a much smaller and more specialized industry. This prospect, if realized, would be attributable to the failure of labor and management to reconcile permanent job protection with the exigencies of a competitive surface transportation market.

This outcome, however, is not inevitable. There are many indications that labor agreements are being tailored to the realities of a competitive transportation marketplace. For instance, there has been a revival in the fortunes of many shortline railroads which have managed to overturn the conventional wisdom that only large, long-haul railroads can make money. In every case,

29. Representatives of the trucking industry and the Teamsters met but failed to agree to renegotiate the national labor agreement. *See* BUS. WEEK, Sept. 8, 1980, at 110-112; Washington Post, Sept. 11, 1980, §B, at 3, col. 4. Nevertheless, many local revisions of the national agreement have been reported, including straight wage reductions, elimination or postponement of cost-of-living increases and less restrictive work rules. *See* Tamarkin, *The Skidding Teamsters*, FORBES, Oct. 27, 1980, at 33-34; *Teamster Local Shuns Master Pact*, J. Com., Sept. 30, 1980, at 2.

30. Office of Policy Analysis, Interstate Commerce Commission. *See also Deregulation Weakens the Teamsters' Clout*, BUS. WEEK, July 28, 1980, at 80-81.

31. The productivity record of American railroads under regulation has been dismal. A study comparing the experience of the American rail industry with the essentially dregulated Canadian railroads showed dramatically higher productivity gains among the Canadian lines. Caves, Christensen, & Swanson, Economic Performance in Regulated and Unregulated Environments: A Comparison of U.S. and Canadian Railroads (March 1980) (Social Systems Research Institute, University of Wisconsin).

they attribute a large measure of their success to reduced labor costs and increased labor productivity.[32] This not only preserves rail operations and jobs, it also promotes vigorous, intermodal competition and leads to more diverse and flexible rail systems. The real question, however, is whether labor and management throughout the bulk of the rail industry can resolve the conflict between job protection and the pressing need for increased productivity in an increasingly competitive environment.[33]

Surface Transportation Under Competition: A Conclusion

All of the innovative strategies and tactics outlined in this article are changes already underway in the transportation industry. They are likely to appear with increasing frequency as the level and intensity of competition inspired by deregulation increases. Some characteristics of those firms which will survive the transition are relatively clear. They will be dynamic, responding quickly to the changing needs of their customers. Competition will provide the stimulus to act; the lifting of restrictive regulation will remove operational impediments. Price and service options will multiply and flourish. Operating methods will be continually revised to promote efficiency. Labor agreements will be modified to conform closely to the economic reality of intense competition.

There is certainly no guarantee that these modifications will lead to a properous future. Conducting business in a competitive environment is an inherently uncertain venture. Changes in technology and the demands of shippers can make entire transportation modes obsolete. The era of competition, however, ensures that the rewards of the marketplace will be earned by those firms whose services are most highly valued by shippers, and who provide these services most efficiently. Business success will no longer depend on the skill of the attorney or the whim of the ICC. Whether surface transportation is dominated by truckers or railroads, by big carriers or small carriers, or by contract or common carriers is less important than that these industries have the freedom and the incentives to provide the highest quality transportation service at the best rates possible. The regulatory reforms in surface transportation over the past year and the competitive environment they are creating will make this vision a reality.

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32. *See, e.g.*, Kizzia, *The Delmarva Shortlines: A New Breed*, Railway Age, September 8, 1980, at 83-84; Holsendolph, *How to Survive On the Rails*, New York Times, Nov. 2, 1980, §D (Business), at 18.

33. One example of at least a partially successful renegotiation of job protection rules is the collection of separate agreements reached by individual railroads and organized labor on minimum train crew sizes. *See*, Welty, *Crew Consist: The New Pacts are Paying Off*, Railway Age, Mar. 31, 1980, at 48-50.