COMMENT: GOVERNMENTAL UNDERMINING OF THE COMMON CARRIER SYSTEM—A CONFLICT IN PHYSICAL DISTRIBUTION

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INTRODUCTION

This paper deals with controversy. Section 203(b)(5) of the *Interstate Commerce Act*[1] states that motor vehicles controlled and operated by a cooperative association as defined in the *Agricultural Marketing Act*[2] shall be relieved of economic regulation.[3]

Recent legislative and judicial events that have transpired during the last decade regarding the interpretation of this section of the ICA have raised numerous questions as to whether the strength of the common carrier system is being undermined.

THE PHILOSOPHY OF THE AGRICULTURAL MARKETING ACT OF 1929

The *AMA* is germane to this discussion because it is specifically referred to in Section 203(b)(5) of the ICA.

To fully understand the meaning of Section 203(b)(5) of the ICA[4] it is necessary to look briefly at the content and philosophy of the AMA. The first paragraph of the AMA declares the policy of Congress in this area to be:[5]

> . . . to promote the effective merchandising of agricultural commodities in interstate and foreign commerce so that the industry of agriculture will be placed on a basis of economic equality with other industries, and to that end to protect, control, and stabilize the currents of interstate and foreign commerce in the marketing of agricultural commodities and their food products, (2) by preventing inefficient and wasteful methods of distribution, (3) by *encouraging the organization of producers into effective associations* or corporations under their own control for greater unity of effort in marketing . . .

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1. 49 U.S.C. 303(b)(5). Hereafter referred to as the "ICA".
2. 12 U.S.C. 1141. Hereafter referred to as the "AMA".
3. See footnote 1.
4. *Ibid.*
5. 12 U.S.C. 1141(a).

As the above policy statement points out, Congressional intent was to encourage cooperatives among farmers and in fact to protect them if necessary.

Section 1141j of the AMA defines the term "cooperative association" as follows:[6]

> Any association in which farmers act together in processing, preparing for market, handling, and/or marketing the farm products of persons so engaged, and also means any association in which farmers act together in purchasing, testing, grading, processing, distributing, and/or furnishing farm supplies and/or farm business services: Provided, however, That such associations are operated for the mutual benefit of the members thereof . . . and in any case to the following: Third. That the association shall not deal in farm products, farm supplies, and farm business services with or for nonmembers in an amount greater in value than the total amount of such business transacted by it with or for members. All business transacted by any cooperative association for or on behalf of the United States or any agency or instrumentality thereof shall be disregarded in determining the volume of member and nonmember business transacted by such association.

In summary, a careful reading of the AMA brings out two basic points, *i.e.*, (1) cooperative associations are to be encouraged and that they will be protected if necessary and (2) that they will have the right to haul products for nonmembers of the cooperative, as long as these revenues are less than 50% of the total revenues for the cooperative.

The AMA states rather clearly that the hauling for nonmembers would be only in farm related products. However, this point, which appeared so patently clear when it was written in 1929, has become the focal point for a very controversial issue during the last decade.

CACHE VALLEY DAIRY ASSOCIATION: INVESTIGATION OF OPERATIONS

In *Cache Valley Dairy Association Investigation of Operations,*[7] Division 1 of the Commission stated specifically that the backhaul

6. 12 U.S.C. 1141(j).

7. 96 M.C.C. 616 (1964), aff'd. I.C.C. v. *Northwest Agricultural Cooperative Association, Inc.*, 234 F. Supp. 496 (D. Oreg. 1964), rev'd. 350 F2d 252 (9th Cir. 1965), *cert. den.*, 382 U.S. 1011 (1966), on reconsideration, 103 M.C.C. 798 (1967).

transportation services that cooperative associations are involved in *must* be limited to hauling farm related goods to be eligible for the exemption from regulation provided by Section 203(b)(5) of the ICA.[8]

Although it was found that Cache Valley Dairy Association was a bona fide cooperative association within the meaning of the AMA, the Commission found that ". . . it was never intended that a bona fide cooperative association under the marketing act might indiscriminately engage in the transportation of nonfarm commodities for nonmembers and use Section 203(b)(5) as a shield against our regulations pertinent to for-hire transportation of otherwise nonexempt commodities."[9]

It was also noted that if the Commission would allow the "co-ops" vehicles to haul nonexempt goods for nonmembers, the Commission would be in the awkward position of having this traffic not subject to the third part of Section 1141j of the AMA[10] while at the same time, the "co-ops" hauling farm-related products for nonmembers would be controlled by the restriction in Section 1141j. The effect of this is that the valuation amount of business would be restricted when hauling farm products for nonmembers, but would be *unrestricted* if the traffic was nonfarm related.

Because of the above, the Commission concluded that:[11]

> Thus, in considering the overall intent of the statute, we believe that the limitation of the third part of section 1141j implies an affirmative corollary; namely, that an association's dealings with nonmembers shall be limited to farm products, farm supplies, and farm business services.

The decision makes it clear that the Congressional intent of the AMA was not to sanction "co-ops" to engage in for-hire transportation in open competition with rail and motor common carriers.

Although the Association's revenue in the cases for nonmembers was only 2% of its total revenues the Commission rejected the percentage of revenues theory as not a valid test. This appeared to be a valid position for although only 2% of the Association's revenue was derived from nonmember traffic during a representative period, 35% of the tonnage hauled by the Association involved nonfarm items for nonmembers.[12] This constituted a considerable quantity of freight

8. 96 M.C.C. at 622.
9. 96 M.C.C. at 620.
10. 96 M.C.C. at 620-621.
11. 96 M.C.C. at 621.
12. 96 M.C.C. at 621.

that should have been carried by regulated common carriers.

As noted by the Commission there is little or no relationship between revenues and tonnage hauled.[13] In fact, the revenue of the nonfarm goods on backhauls can always be kept at less than 50% by merely lowering the rate to be charged.

Thus the decision of the Commission turned on the issue of whether the backhaul transportation by the Association of nonfarm-related commodities for nonmembers was a service, functionally related or unrelated to the Association's farming activities.[14]

NORTHWEST AGRICULTURAL COOPERATIVE CASE

In *I.C.C. v. Northwest Agricultural Cooperative Association, Inc.*,[15] the District Court concurred with the Commission's finding in *Cache Valley*. In a decision written by Chief Judge Solomon, it is stated:[16]

> The difficulty with the defendant's position is that it sanctions for-hire transportation in open competition with regulated common carriers without subjecting the Association's fleet to regulation. Though Congress intended to exempt agricultural cooperatives from regulation under the Act in the transportation of their goods to market and their necessary supplies and services on return, I do not read the statute as granting these associations an exemption to enter the general transportation business. Undoubtedly the Association's practice affords economies to its members, but these are economies not intended to be conferred by the Act.

On appeal, the Court of Appeals, reversing the District Court, held that an agricultural "co-op" whose primary activity was hauling for members did *not* lose its status as a cooperative association and therefore was not subject to the economic regulation of the Commission as long as its transportation of nonfarm products for nonmembers was *incidental* and *necessary* to the "co-op's" farm-related transportation both in character and amount.[17]

In its decision, the Court of Appeals specifically noted that the AMA did not state, nor did it imply, that a "co-op" could not deal

13. 96 M.C.C. at 621-622.
14. 96 M.C.C. at 622.
15. 234 F. Supp. 4961 (D Oreg. 1964)
16. 234 F. Supp. at 498.
17. *Northwest Agricultural Cooperative Ass'n. v. I.C.C.*, 350 F2d 252 (9th Cir. 1965), *cert. den.*, 382 U.S. 1011 (1966).

at all in nonfarm products for nonmembers. Furthermore, it was noted that the AMA specifically stated that its intention was to protect and encourage agricultural cooperatives and therefore the AMA should be *liberally* construed to effect that purpose.[18] Therefore, the Court of Appeals found that Northwest did not lose its identity of a cooperative when it engaged in activities other than its primary one, as long as the other activities were *incidental* to the primary one and *necessary* to its effective performance.[19]

This "incidental and necessary" test was an outgrowth of *I.C.C. v. Jamestown Farmers Union*[20] where it was stated:[21]

> . . . if such activities are merely incidental to, and necessary for the effectuation of the cooperative's principal activities as embraced within the Act, the status of the cooperative remains unimpaired.

In applying the "incidental and necessary" test, the Court of Appeals in the *Northwest* case noted that the cooperative's hauling was incidental because it was limited to otherwise empty trucks returning from hauling member farm products to the market and because the nonfarm revenue was very small compared to the total revenue of the cooperative. Likewise, the backhaul of nonmember traffic was necessary because it would not be economically feasible to operate the vehicles empty on the backhaul and without this traffic the "co-op" costs would be higher than common carriers and against the policy of the AMA.[22]

The prime argument of the Commission in the *Northwest* case was that nonfarm hauling for nonmembers may not be counted at all in computing the 50% limit because the limitation applies only to "farm" business for nonmembers. The Court, rejecting this argument noted that a cooperative will only retain its exemption as long as its essential character is that of a cooperative. In other words, the Court said that a cooperative would not be of this character if its nonfarm hauling exceeded that which was incidental and necessary to its farm-related hauling.[23]

If the Court of Appeals' approach prevails, it is difficult to imagine a situation where the nonfarm business could approach 50% of the

18. 350 F2d at 257.
19. 350 F2d at 257.
20. 57 F. Supp. 749 (D. Mn. 1944) affd., 151 F2d 403 (8th Cir. 1945).
21. 57 F. Supp. at 753.
22. 350 F2d at 255.
23. 350 F2d at 256.

total and still remain incidental and necessary to the farm-related business.

The Court in *Northwest* also found the cooperative was *not* engaged in the general trucking business:[24]

> Its trucking operation, viewed as a whole, is a farm service performed jointly by Northwest's members "for themselves." The return hauls enjoined are "connected with farm operations," for they are incidental and necessary to the effective performance of Northwest's farm-related operations. This return haul transportation therefore did not deprive Northwest of its essential character as a 'cooperative association' under the *Agricultural Marketing Act*. Since it retained this character it retained its right to exemption under Section 203(b)(5) of the *Interstate Commerce Act*.

I.C.C.'s FIRST REACTION TO COURT's DECISION

The Commission, through its Chairman, immediately recognized the gravity of the Court's decision and stated:[25]

> There goes business which regulated carriers have to be authorized to haul. If that isn't simply legalizing what the transportation industry, the Congress and the Commission has long fought as a type of 'gray area' operation, I don't know what it is.

It was also charged that the Court did not realize that its decision, in effect, had legalized a very dangerous threat to all regulated transportation and to the National Transportation Policy and was not justified because agricultural cooperatives were losing money.[26]

The position of the Commission, as expressed by the Chairman, was based on two prime considerations, *i.e.*, (1) every common and contract carrier has the problem of backhauls and the judicial decision would only compound the problem by taking away traffic that rightfully belongs to for-hire carriers, and (2) if the Court's decision was based on valid reasoning, it would appear that private carriers should have the same privilege of hauling nonexempt commodities when it has problems of empty backhauls.[27]

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24. 350 F2d at 257.
25. "I.C.C. Head Urges Definition of Co-op Clause by Congress," *Transport Topics* (Oct. 24, 1966), p. 1.
26. *Ibid.*, p. 66.
27. *Id.*

It was also noted that the Commission would press with increased vigor to amend Section 203(b)(5) of the ICA to overcome the existing judicial interpretation.[28]

D.O.D. POLICY STATEMENTS CONCERNING "CO-OPS"

The Department of Defense[29] shortly after the *Northwest* decision stated its position relative to the use of cooperatives:[30]

> Farm cooperative trucks will be used when they can meet military requirements of safety and reliability and when their use would result in the lowest overall cost to the government.

Prior to the Northwest decision, cooperative vehicles were only used by the D.O.D. when there was no other form of for-hire transport available.

The old cliche that "there is nothing like a war to unite the political parties of a country towards a common goal" became true of the transportation industry after the *Northwest* decision. Immediately after the D.O.D. policy statement, various segments of the regulated transportation industry sent the Secretary of Defense a joint communique urging "that the D.O.D. proposal be accepted only in the remote event that common carrier service is not available.[31]

The regulated segment of the industry pointed out that the regulated common carriers were a definite part of the logistical arsenal of the United States in a time of national emergency. On the other hand, the "co-op" trucks were engaged in transportation completely exempt from all economic regulation and they had absolutely no obligation to provide general transportation service on a nondiscriminatory basis to the general public. The "co-op" trucks could legally pick and choose traffic and receive just enough compensation to cover the cost of the otherwise empty backhaul. Furthermore, it was pointed out that the cooperatives can and will set rates that are just low enough to divert traffic from the regulated carriers and that utilizing cooperatives on such a basis was false economizing which would compromise the strength of the United States defense posture.[32]

The transportation industry's position was supported by the

28. *Id.*

29. Hereafter referred to as D.O.D.

30. "Defense Department to Use Farm 'Co-op' Trucks to Haul Military Cargo Within U.S.," *Traffic World*, (Nov. 12, 1966), p. 38.

31. *Id.*

32. *Id.*

United States Chamber of Commerce. Its President issued the following statement:[33]

> For the good of the nation's regulated transportation system and in the best interests of all those who depend upon it for service, I urge that you take no action which would lead to the continuation or growth of unregulated for-hire carriage by agricultural cooperative organizations.

CONGRESSIONAL REACTION TO THE CONTROVERSY

A number of bills subsequently were introduced into Congress to restrict the growth of "co-op" nonfarm, nonmember tonnage.[34] Section 203(b)(5) was ultimately amended[35] as a result of the enacted amendments. The new law provided that fifteen percent of the cooperative's total annual *tonnage* could be transported for nonmembers who are also nonfarmers. Also a maximum of 50% of the cooperative's total annual tonnage can involve carriage for farmer nonmembers. For purposes of computing the cooperative's total annual tonnage, any transportation service provided for an agency of the United States Government was to be included in the annual tonnage figure.[36]

RECENT "CO-OP" CONTROVERSIES

After the legislative amendments, it was merely a matter of time until cooperatives sought common carrier status. The first cooperative applicant was successful in its endeavor in *American Farm Lines Cooperative Common Carrier Application.*[37]

CONCLUSION

Section 203(b)(5) of the ICA[38] was enacted by floor amendment and there was little time to consider all the possible ramifications of the

33. *Id.*

34. See, for example: "Truckers, Co-ops 'Accept' Amended Bill on Co-op Backhaul Operations," *Traffic World,* (Nov. 12, 1966), p.38.

35. Public Law 90-433. For a thorough review of the various proposals, and the rationale behind the amendment see S. Rep. No. 1952, 90th Cong. 2d Sess. May 28, 1968, of the Senate Committee on Commerce, to Accompany S. 752. See also *Implementation of P.L. 90-433—Agric. Coop. Exemption,* 108 M.C.C. 799 (1969).

36. "I.C.C. Adopts, With Some Changes, Proposed Rules Governing 'Co-op' Transportation," *Traffic World* (May 24, 1969), pp. 62-63.

37. 114 M.C.C. 30 (1971).

38. 49 U.S.C. 303(b)(5).

exact words that were chosen. The Section adapted the provisions of the AMA and at the time seemed crystal clear in meaning. Although the AMA stated that "co-ops" could not earn more than half of their revenues from nonmember hauling of farm-related goods, it did not explicitly state that "co-ops" could not haul nonfarm-related goods for nonmembers. It was obviously assumed they would not. Because of the haste in which Section 203(b)(5) of the ICA was enacted, there appeared no reason to state explicitly what was obviously implied.

All was copacetic until the *Northwest* decision when the Court appeared to err. Specifically, the decision was diametrically opposed to the implied National Transportation Policy. Although, the preamble to the ICA does not specifically state the importance of common carriers, the implication is clear. In addition, various transportation messages of recent Presidents state unambiguously that the common carrier organization is the backbone of our transportation system.[39] Therefore, any action that will weaken the common carrier system should be vigorously opposed by both the Courts and the Commission.

However, the Court of Appeals in *Northwest* ignored this portion of the National Transportation Policy and allowed a type of carriage that could only have unfavorable results on the common carrier system. Furthermore, the Department of Defense then added to the problem by stating that it would use "co-op" vehicles to haul their freight. This is really ironic, for the D.O.D. more than any other government agency should know the value of having a strong common carrier system during a time of national emergency.

The author finds the D.O.D. policy of shipping military freight on "co-op" vehicles lamentable. Consider the *Doyle Report's* comment about the Government as a purchaser of unregulated transportation:[40]

> The indispensable nature of regulated for-hire carriers as the backbone of our transportation system has been emphasized elsewhere in this report. To the extent Government diverts traffic from regulated to unregulated for-hire carriers it is negating its own promotional and regulatory objectives which are established in the national interest. Such action on the part of

39. Kennedy, John F., *Message on Transportation,* (The White House, Washington, D.C., April 5, 1962), p. 3. Johnson, Lyndon B., *Message on Transportation,* (The White House, Washington, D.C., March 2, 1966), p. 3.

40. "Government As A Purchaser of Unregulated Transportation," *National Transportation Policy,* Report of the Committee on Commerce, (June 26, 1961), p. 492.

> a Government agency is far less reasonable than similar action on the part of a private shipper who, so long as his actions are within the law, can be excused for seeking thus to minimize his costs. It is not the individual responsibility of a shipper single-handedly to assure a healthy transportation system—it is a responsibility of Government.

The 1968 "15/50" amendment[41] was a political expedient which was totally devoid of logic concerning the preservation and strengthening of the common carrier system. There are approximately 9,300 agricultural cooperatives which in the aggregate have the potential and the ability to substantially weaken the common carrier system. The cooperatives' legalized traffic diversion is slowly but surely sapping the strength of the common carrier system today.

The present situation is deplorable and it is strongly urged that Congress repeal the "15/50" rule so that cooperatives will be precluded from transporting any nonfarm-related products for nonmembers.

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41. See footnote 35.