MARKET DOMINANCE

The Evolution and Implications of the Market Dominance Concept in Railroad Ratemaking

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I. INTRODUCTION

A. BACKGROUND

Control of market and shipper abuse through the Interstate Commerce Commission (Commission) has been the cornerstone of railroad regulation in the United States. Pervasive monopoly power in some rail markets coexistent with severe intramodal (i.e., rail versus rail) competition in other markets seemed to warrant some form of economic regulation to protect the interests of both shippers and carriers. Although often interpreted and implemented to protect either shippers or carriers, the tenets of regulation as guardian of shipper and carrier remained unchanged for nearly ninety years despite vastly changing market conditions.

Academicians perceived the need for regulatory reforms from increasingly apparent trends in the post-war years.[1] Between World War II and 1980, the railroad share of intercity ton-mileage dipped from 68.6% to 37%.[2] Over the same period, the rail industry experienced a precipitous decline in their share of intercity freight revenue, from 76% to 38%. For 1980, the estimated return on investment (net investment basis) was 4.25% for Class I railroads. Although a twenty-five year high for the industry, this return is still far below that in other industries, and far below the 11% the railroads must have to attract the private capital necessary to maintain service at an adequate level. The effect of declining freight revenue has been anemic returns to owners, jeopardizing the very existence of the rail industry.

The initial justification for regulation of the railroads, monopolization,

1. J. MEYER, M. PECK, J. STENASON, & C. ZWICK, THE ECONOMICS OF COMPETITION IN THE TRANSPORTATION INDUSTRIES 273 (1959).
2. ASSOCIATION OF AMERICAN RAILROADS, YEARBOOK OF RAILROAD FACTS 36 (1980).

no longer existed. Freight markets once dominated by rail carriers were being eroded by a combination of technological and economic changes. Regulation no longer could be viewed as ensuring economically efficient or fair market results; instead, it had come to be a contributing cause of substantial misallocation of traffic. This development eventually received substantial political attention in the form of the deregulatory movement.

Congress, recognizing that the growth of other modes of transportation had raised serious questions about the necessity for protection against rail monopoly, passed the Railroad Revitalization and Regulatory Reform Act of 1976[3] (4R Act). In the place of functional regulation (e.g., control of maximum rates under all circumstances) the 4R Act introduced a system of selective market price regulations based upon determinations of market dominance.

Under the new system, railroads are viewed as multiproduct-carrying firms operating in several distinct product markets. Each market is characterized by unique conditions of supply and demand. In some markets, sufficient competition may exist to make maximum rate regulation unnecessary; in others, the development of insufficient competition may warrant continued regulation. The market dominance concept, as stated by Congress and later implemented by the Commission, was to be used to distinguish between competitive and non-competitive.

Due in part to the rigidity with which the Commission applied the market dominance principle, the pricing reforms envisaged by the 4R Act were largely unrealized. Prompted by this failure, and the continued financial plight of the railroad industry, Congress passed the Staggers Rail Act in 1980[4] (Staggers Act). The Staggers Act retained the requirement that maximum rate regulation be predicated upon a finding of rail market dominance; but the ICC was directed to redefine its operative definition of market dominance.

B. *Purpose*

Limited rate regulation represents a radical departure from previous regulation schemes. In many ways this type of control is more complex. The Commission has been forced to consider, if not answer, questions which have long plagued policy makers. What is the relevant market in determining market dominance? What factors in the relevant market, once identified, characterize its competitive disposition? How are these charac-

3. Railroad Revitalization and Regulatory Reform Act of 1976, Pub. L. No. 94-210, 90 Stat. 31 (codified in scattered sections of 45 U.S.C. and 49 U.S.C.).

4. Staggers Rail Act of 1980, Pub. L. No. 96-448, 94 Stat. 1895 (codified in scattered sections of 49 U.S.C.).

teristics to be measured without imposing undue data requirements on carriers, shippers and regulators?

The primary purpose of this article is to present an historical accounting of the market dominance principle as it has evolved through congressional enactments and Commission proceedings and regulations. Included in the accounting is a review of the work of A.T. Kearney Consultants (A.T. Kearney), the firm employed by the Commission for technical assistance, which contributed significantly to the formulation of the market dominance principle.[5] This article will also explore factors which may precipitate further changes in the implementation of the market dominance principle through new standards for monitoring market conditions.

II. Evolution of the Market Dominance Concept

A. *House and Senate Bills*

A premise of the House Committee on Interstate and Foreign Commerce in formulating its report on the 4R Act[6] was that if a carrier dominates a market, the maximum rates charged to its customers should be subject to regulation. According to the House committee's approach, the existence of effective competition for any segment of traffic was to be determined by the direct transportation cost, service options, and commodity and shipper characteristics present. It set out, in 1975, to allow for "a wider operation of competitive forces in the market place" because its members believed that, in most cases, competition could locate the most efficient price levels. The House report defined market dominance as follows:

> Market dominance *shall be presumed* in any situation in which (i) in any geographical market there are not at least 2 competing rail carriers or a rail carrier and an alternative mode of transportation both of which compete for the business in the area, or (ii) with respect to any single commodity or type of goods there is an absence of competition between the rail carriers for transport of that commodity, or where there is only one rail carrier, the absence of a competing mode which in fact provides transportation for that commodity in a reasonably effective and competitive fashion.[7]

The House committee intended to exclude general rate increases brought about by rate bureau activity from the Commission's market dominance tests because it did not want to destroy the purpose of the industry-wide

5. *See* A.T. Kearney Management Consultants, A Study to Perform an In-Depth Analysis of Market Dominance and Its Relationship to Other Provisions of the 4R Act, Interim Report II (1979) [hereinafter cited as A.T. Kearney, Interim Report II].

6. H.R. Rep. No. 725, 94th Cong., 1st Sess. (1975).

7. *Id.* at 12 (emphasis added).

increase.[8]

The Senate Committee on Commerce also concluded, in late 1975, that "deregulating and giving flexibility to the railroads [in ratemaking] . . . can supplant the need for maximum price regulation."[9] The Senate committee intended that market dominance act as a threshold test; a finding of market dominance would only direct the attention of the Commission's investigation toward areas where the possibility of abuse existed. Private interests would still be protected, but carriers would be given greater flexibility. However, the Senate committee's concept of market dominance differed from that of the House in that:

> Market dominance *shall be presumed* to exist if, prior to or after the publication of a rate, no shipment . . . of the traffic to which the rate applies have [sic] moved by any other carrier or mode of transportation other than by a proponent carrier, during the 12 months preceding the commencement of the [ICC's] proceeding to determine or investigate the lawfulness of the rate as a result of the relationship of the applicable rate . . . of any other carrier or any other mode of transportation, to the rate of the proponent carrier . . . .[10]

The Commission's role, when utilizing the market dominance principle prescribed by Congress, is to characterize market behavior. As framed initially, market dominance is a measurement or a critical value index against which to measure actual market conditions. If it is determined that actual conditions exceed the acceptable minimal levels of competitiveness, then the law is to presume that the rates charged are reasonable. If it is determined that conditions do not exceed the minimal level, then the rate in question must be reviewed to ensure its reasonableness, because of the presumption of market power in the relevant market.

One final point which emerges from these early congressional deliberations is the role of the Commission as the arbiter of market dominance regulation. Several very difficult problems involved were never adequately addressed by Congress, and thus were left for the Commission to resolve in their case-by-case decisions. An acceptable minimum level of competition was not precisely defined; nor was a yardstick provided for the difficult task of measuring actual market conditions. Furthermore, both the House and the Senate committees implicitly recognized the need to distinguish the determination of market dominance from determination of the reasonableness of rates. The task was delegated to the Commission.

The rudiments of the market dominance concept have remained largely unchanged since these 1975 Committee reports. The methods of

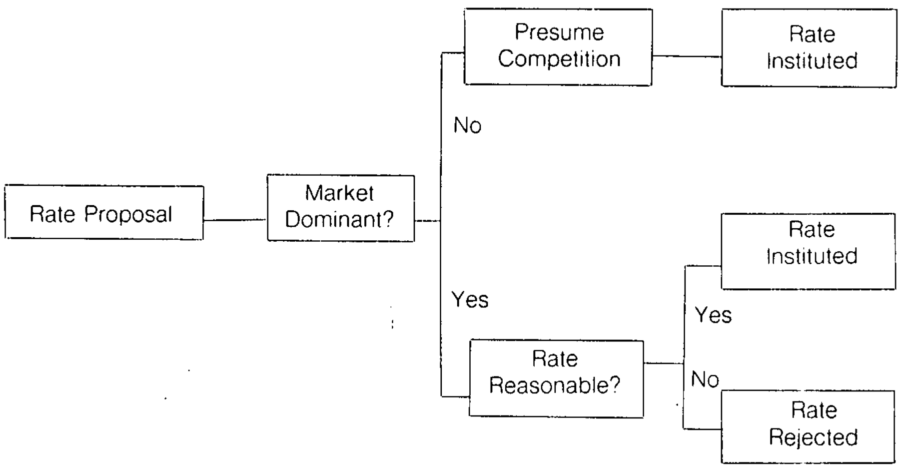
8. *Id.* at 69. A rate bureau is a group of carriers that establish joint rates, divide joint revenues, claim liabilities, and publish tariffs.

9. S. REP. No. 499, 94th Cong., 1st Sess. 47, *reprinted in* 1976 U.S. CONG. & AD. NEWS 14, 61.

10. *Id.* at 119 (emphasis added).

measuring market behavior for the traffic in question, and for separating competitive from dominated markets, are unaltered. In the former, it is presumed that rate regulation is unnecessary. In the latter, rate regulation is presumed necessary, but the existing rates are not presumed to be excessive or unreasonable. The functioning and role of the market dominance principle is presented in Figure 1.

FIGURE 1



B. *MARKET DOMINANCE PROVISIONS OF THE 4R ACT*

The market dominance test is to determine the degree of competition, and to assess which competitive forces are present to assure that market conditions are sufficient for just and reasonable rates. It is a test of reasonableness of rates *per se*. The Interstate Commerce Act was amended in 1976 to define market dominance as "an absence of effective competition from other carriers or modes of transportation, for the traffic or movement to which a rate applies."[11]

The purpose of the Interstate Commerce Act (Act) is to protect shippers against abusive rates.[12] Congress intentionally avoided the area of "monopoly power" when formulating the market dominance test because of problems created by previous violations of antitrust laws.[13] The 4R Act,

11. 49 U.S.C. § 1(5)(c) (1976) (current version at 49 U.S.C. § 10709 (Supp. V 1981)).

12. 49 U.S.C. § 10101a(6) (Supp. V 1981).

13. As used here, monopoly power refers to the potential ability of a firm to exploit its market position through exploitative pricing, discriminatory practices, or other noncompetitive market behavior without attracting competition. Congress circumvented monopoly power proof through the use of testing for market dominance because it could not adequately define many of the terms it would have to use if it fashioned legislation around a concept that was more theoretical than applicable. Through the use of the market dominance concept, the Commission would be able to con-

in its final form, also stated that:

> [N]o rate shall be found to be unjust or unreasonable . . . on the ground that such rate exceeds a just or reasonable maximum for the service rendered or to be rendered, unless the [Interstate Commerce] Commission has first found that a proponent carrier has market dominance over such service. A finding that a carrier has market dominance over a service shall not create a presumption that the rate or rates for such service exceed a just and reasonable maximum.[14]

Congress instructed the Commission to make a ruling for market dominance within ninety days of a rate increase challenge. In addition, the 4R Act required the Commission to develop rules, standards and procedures for determining when a carrier possesses market dominance over a service rendered or to be rendered at a particular rate or rates. This process was to be carried out within 240 days after the enactment of the 4R Act to provide for a quick and practical determination of the law as it was to be administered by the Commission.[15]

Under the new sections of the Act as amended by the 4R Act a rate could not be held to be unreasonably high unless the Commission first found that the railroad possessed market dominance over the traffic. A finding of market dominance, however, is only an initial step in determining if a rate is reasonable. Market dominance is used as a means of identifying transport markets where users have no meaningful modal or rail options.[16] Congress designed the 4R Act to protect shippers in those situations where rate abuse could occur.

C. The Commission's Initial Presumptions

On March 16, 1976, the Commission issued a notice of proposed rulemaking in which certain "factual situations" would create rebuttable presumptions of market dominance in rate increase proceedings. The Commission announced that a lack of effective competition could be inferred in the following situations:

1) where the rate was discussed or considered by rate bureaus; or
2) where no other carrier of any mode had handled a significant amount of the "involved traffic" during the preceding year; or
3) where other carriers had handled a significant amount of traffic but there was no evidence of actual price competition in the past three years; or
4) where the rate exceeded existing rates by 25% or more; or

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trol rate ceilings in markets that were identified as being either concentrated, oligopolistic, or monopolistic.

14. 49 U.S.C. § 1(5)(b) (1976) (current version at 49 U.S.C. § 10709(c) (Supp. V 1981).

15. 49 U.S.C. § 1(5)(d) (1976) (repealed 1978).

16. Barber, *The Market Dominance Test: The 1976 Act's New Approach to Railroad Rate Regulation*, Transp. J., Summ. 1976, at 5, 9.

5) where the rate exceeded the fully allocated cost of the service by 50% or more; or
6) where the distance between origin and destination exceeded 1500 miles, or if a single line movement, 1200; or
7) where the commodity moving under the rate customarily moved in bulk shipments.[17]

Evidence relevant to the seven fact situations could be presented by the carrier proposing a rate increase and by a shipper challenging it.

Several executive agencies attacked the notice, arguing that it did not represent the basic objectives of the 4R Act and urging that regulation of these rate increases be liberalized.[18] The Commission reduced the number of presumptions from the original seven to four by dropping presumptions 4, 6 and 7 entirely from its preliminary list compiled in the notice and altering or combining numbers 1, 2, 3 and 5. In the subsequent interim report, a presumption of lack of competition was held to arise:

1) when a carrier participating in a rate, or, in such discussion, or consideration, does not provide effective competition to the proponent rail carrier for the involved traffic or movement; or
2) when the carrier has handled 70% or more of the traffic affected by the tariff change during the year before the new rate was filed; or
3) when the rate in question exceeds the variable cost of providing the service by 80% or more; or
4) when a shipper or consignee protesting a rate can establish that it has made a substantial investment in railroad equipment that prevents or makes it impractical to use another carrier or mode.[19]

Furthermore, in a reversal of prior policy, the burden of going forward with the evidence under these circumstances was shifted from the protesting shipper to the proponent carrier. The Commission allowed twenty days for interested parties to comment on the changes made before it issued its final set of rules.

This interpretation of market dominance was still considered by many to miss the thrust of the original legislation. The Report was deemed vague as to whether market dominance could be found to exist unless one of the four presumptions pertained. The Commission further scrutinized all of the

17. 41 Fed. Reg. 11,034 (1976) (to be codified at 49 C.F.R. pt. 1108) (proposed Mar. 16, 1976).

18. Barber, *supra* note 16, at 10-11. The Attorney General, the Department of Transportation, and the Federal Railway Administration were among those who filed recommendations as required by § 202 of the 4R Act. These groups maintained that most of the new rate increases would trigger the market dominance threshold test as it was then worded. The Attorney General recommended that all the rebuttable presumptions put forward in the notice be either rejected or substantially reworked.

19. Special Procedures for Making Findings of Market Dominance as Required by the Railroad Revitalization and Regulatory Reform Act of 1976, 353 I.C.C. 875, 887-916 (1976).

responses it received and issued final rules in Ex Parte No. 320 on September 20, 1976.[20]

D. Ex Parte No. 320: Special Procedures for Making Findings of Market Dominance as Required by the Railroad Revitalization and Regulatory Reform Act of 1976

In Ex Parte No. 320, the Commission announced a three, as opposed to four, criteria test for establishing a rebuttable presumption of market dominance. Market dominance will be presumed to exist in the following situations:

1) where the market share of the proponent carrier equaled or exceeded 70% of the involved traffic or movement during the preceding year; or
2) where the rate exceeds 160% of variable costs of providing the service; or
3) where the affected shippers or consignees have made a substantial investment in rail-related equipment or facilities which prevents or makes impractical the use of another carrier or mode.[21]

The Commission further stated that a "rebuttable presumption will arise that a carrier participating in the rate or in such discussion or consideration [under a rate of bureau agreement] does not provide effective competition to the proponent rail carrier."[22] Even under these presumptions, the shipper must meet its burden of persuasion at the suspension level by presenting evidence from which the Commission may find that the rates are unreasonable.[23]

These regulations had an enormous effect on the entire railroad industry. Originally, the Commission sought to presume market dominance in every case where overt collusion was present, such as when a rate was discussed or agreed upon in a rate bureau. This stance was later relaxed in the Commission's final rules so that the presumption was limited to actions within the bureau's formal realm of activity.[24]

The market share test was based on rulings in previous antitrust cases stating that if the competitors of the railroad in question possessed one-third or more of the traffic, service on a competitive level was probably feasible. The Commission modified the rulings of these antitrust cases and set its target level to require that a carrier would be presumed dominant when it

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20. Special Procedures for Making Findings of Market Dominance as Required by the Railroad Revitalization and Regulatory Reform Act of 1976, 355 I.C.C. 12 (1976) [hereinafter cited as Ex Parte No. 320].

21. *Id.* at 23. These tests will be respectively referred to as the market share, variable costs and substantial investment tests.

22. *Id.* at 23.

23. Potomac Elec. Power Co. v. Conrail, 362 I.C.C. 169, 188 (1980).

24. *See* Ex Parte No. 320, supra note 20, at 16.

acquired 70% or more of the market. The Commission further ruled that once a case was decided, the market conditions were presumed to remain unchanged until the Commission made a different determination.[25] Although the Commission was content to merely measure the magnitude and nature of changes in a given market, shippers seemed more concerned with the actual conditions and the continuous adjustment process that occurred in that market.

At the request of many shippers, the second presumption, the variable costs test, was substituted for the fully allocated cost test.[26] The Commission finally decided that a variable cost test would more accurately reflect the absence of effective competition. It used Rail Form A costing procedures to apply this test.[27] According to research carried out by the Commission, a ratio of revenue to variable costs between 140 and 150% appeared to be the highest level of minimal market power.[28] To allow for error, the Commission then assumed market power would appear when a rate exceeded the variable costs by 160%. A rate beyond this level would suggest that market forces did not determine the rail carrier's prices.

The purpose of the third presumption, the substantial investment test, was to protect shippers which had become "captive" due to their heavy investment in rail-related facilities. In using this test, the Commission would consider the size of the investment in relation to the shipper's total costs. This test was included to prevent railroads from exploiting the advantage of being the only transporter of a shipper's goods. The railroads challenged this test on the grounds that it lacked any rational basis; the railroads believed that many supply and demand conditions of equal importance were being overlooked in forming the regulations for captive shippers.

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25. Boske, *An Analysis of Recent Developments in Railroad Maximum Rate Regulation*, 48 ICC PRAC. J. 294, 298 (1981).

26. *Commission Fixes Four Presumptions for Ruling in Market Dominance Cases*, TRAFFIC WORLD, August 30, 1976, at 13. A variable cost fluctuates with the business output (e.g. the total cost of materials). Fully allocated costs are those variable costs incurred to produce a particular unit plus a percentage of the business' fixed costs (e.g. rent).

27. The use of Rail Form A costing procedures for determining market dominance created problems for practitioners because:

> (1) [its] costs are based on the average costs for all movements on a given railroad;
> (2) the use of [this] information alway will be retrospective in that costs are derived from accounting data pertinent to operations of the previous year(s);
> (3) [its] distributional procedures assumed that all traffic utilized the same vintage mix of plant and equipment;
> (4) [a]dditional complications are associated with the manner in which long-run variable costs are estimated; and
> (5) [p]ricing according to [its] computed costs gives no recognition to the competitive conditions, the quality of services being offered, the price elasticitities of market demand, or to revenue needs.

Boske, *supra* note 25, at 301.

28. Special Procedures for Making Findings of Market Dominance as Required by the Railroad Revitalization and Regulatory Reform Act of 1976, 359 I.C.C. 735, 737 (1979).

On October 5, 1977, the Commission issued a report to Congress that was prepared in accordance with section 202(g) of the 4R Act.[29] Section Two of the report dealt with the evaluation of the market dominance provisions. The assumptions, biases and results of Ex Parte No. 320's effectiveness were discussed and estimates of the rail traffic likely to trigger the threshold tests were presented. The Commission estimated that between 48.5 and 70% of interstate traffic then carried by the railroad industry would meet the threshold conditions.[30]

Following the implementation of these tests, the Commission received numerous protests to rate filings that involved claims of unreasonableness. The Commission, however, could not attempt to make a market dominance finding on a number of the cases because the protestant failed to follow procedures laid out in Ex Parte No. 320.[31] Of the successful protests, the market share presumption, which was the most restrictive of the three tests, was used most often to establish market dominance. Several of the markets in cases involving this criterion were found to be captive and the railroads were therefore considered to have market dominance. As of May 1, 1978, market dominance had been found in 36 out of 227 rates protested, with 16 of these rates eventually suspended.[32] The protestant proved injury in 14% of the cases due to unreasonably high rates.

Several firms, principally railroads and power companies, challenged the applicability of the market dominance tests in the courts. In May of 1978, the Court of Appeals for the District of Columbia ruled against the railroads, basing their decision on the Commission's "presumed expertise" in the area of railroad ratemaking.[33] The court assumed that, because this was an untested area of regulation, the Commission's rules and procedures should stand until they could be improved upon at a later date.

E. Other Commission Decisions Concerning Market Dominance

In April of 1979, A.T. Kearney, while under contract with the Commission to perform an in-depth analysis of market dominance, released its second interim report. This report presented empirical research and analysis of market dominance and compared alternative approaches to its implementation. Based on the data collected, A.T. Kearney concluded that less than five percent of the nation's rail traffic could be considered market dominant under the rebuttable presumptions. Consequently, it concluded that reserv-

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29. *See* Interstate Commerce Commission, The Impact of the 4R Act Railroad Ratemaking Provisions (1977).
30. *Id.* at 43.
31. *See* Bureau of Economics, Interstate Commerce Commission, A Comprehensive Review of Market Dominance (1978).
32. *Id.* at S-8.
33. Atchison, T. & S.F. Ry. v. ICC, 580 F.2d 623 (D.C. Cir. 1978).

ing maximum rate regulation for noncompetitive traffic was theoretically and practically sound.[34]

The Commission continued to accept suggestions and comments for revisions in their scheme to improve the market dominance regulations. It realized that the standards and procedures utilized in rulemaking proceedings needed to be modified, revised, or refined to the point where actual market competition was being regulated. The Commission continually reviewed cases brought before it and reexamined its tests in order to develop a coordinated and practical approach to market dominance. The Commission also attempted to minimize unnecessary rate regulation. On February 5, 1979, it issued the first of several notices that helped clarify its position on the presumptions stated in its rules of market dominance.[35] These policy statements formed the basis for the Commission's stand until the passage of the Staggers Act in 1980.

In issuing a Clarification of Prior Decisions, the Commission reaffirmed its previous position on the use of the variable cost test. The cost presumption indicated, with reasonable accuracy, specific markets in which railroads had market power. The Commission concluded that the variable cost test was a useful tool and that it would continue to be utilized in findings of market dominance. The rebuttable presumptions were not meant to be absolute barriers to rate innovations and the railroads were still considered to have considerable pricing flexibility under the presumptions.

The Commission also expanded, for a short time, its definition of "market" in market dominance cases to include the international markets. In its *Coleto Creek* decision of January, 1980,[36] the Commission found that none of the three rebuttable presumptions was established by the protestant and therefore refused to review the reasonableness of the rate at issue. It determined that the railroads in question faced effective competition from foreign coal suppliers. Prior to this decision, overseas suppliers had not been considered in maximum rate cases. The *Coleto Creek* fact pattern was not unique, and therefore, the decision could be applied to a wide range of cases involving other markets or other products.[37]

The *Coleto Creek* decision made it more difficult for shippers to establish that a carrier dominated a market because of the potential for competition from the international marketplace. The relevant geographic market, then, could easily have been defined as the global market. However, this decision was to prove of little consequence; the Commission decided to change the criteria it would use in market dominance cases.

34. A.T. Kearney, Interim Report II, *supra* note 5, at IX-4.

35. Special Procedures for Making Findings of Market Dominance as Required by the Railroad Revitalization and Regulatory Reform Act of 1976, 359 I.C.C. 735 (1979).

36. Incentive Rates on Coal—Axial, CO to Coleto Creek, TX, 362 I.C.C. 572 (1980).

37. Boske, *supra* note 25, at 306.

F. *Ex Parte No. 320 (Sub-No. 1)*

On January 17, 1980, the Commission issued a notice that made substantial revisions in the regulations which pertained to the determination of market dominance.[38] The Commission intended to eliminate two of the presumptive tests, the market share and substantial investment tests, and modify the third, the variable costs test. Revisions incorporated recent experience and attempted to provide a clear and predictable measure of what the Commission's response would be to any market dominance case brought before it. The new standards required the party with the burden of establishing market dominance to make a prima facie case that the condition did in fact exist.

A prima facie case of market dominance under Ex Parte No. 320 (Sub-No. 1), required evidence which indicated that "the rate for the traffic or movement exceeded 180% of the variable costs of providing the service."[39] If the evidence indicated that the rate in question was less than 180% but more than 150% of variable costs, no assumption would be made as to the competitive circumstances. In addition, if the evidence indicated that the rate was less than 150% of variable cost, a prima facie case would be established that no market dominance existed. Furthermore, a zone of reasonableness for rate increases, within which a rate could not be suspended, was established. A rate increase under these circumstances would not be suspended: 1) if the rate was equal to or less than 150% of the variable cost ratio; or 2) if the rate increase was less than a 7% increase annually.[40] Finally, the limited rate bureau assumption was retained and the issue was to be discussed under a new set of rules that restricted rate bureau activity.

The new threshold conditions continued to utilize information from Rail Form A of Ex Parte No. 338[41] despite its drawbacks. The upper level of 180% of variable cost was based upon the Commission's experience that a rate in question above this level required further examination; the lower limit of 150% of variable cost was considered to be a close approximation of fully allocated to variable costs. The threshold levels assisted the railroads in obtaining adequate revenue levels and removed another segment of the industry (seeking rate increases which left the rate below 150% of variable costs) from rate regulation.

The burden of proof principle was addressed at length by the Commission in order to clear up any ambiguities that may have arisen over the

38. 45 Fed. Reg. 3353 (1980) (to be codified at 49 C.F.R. pt. 1109) (proposed Jan. 17, 1980).

39. *Id.* at 3357.

40. *Id.*

41. Standards and Procedures for the Establishment of Adequate Railroad Revenue Levels, 358 I.C.C. 844 (1978).

years.[42] In a rate suspension proceeding for market dominance, the burden of persuasion remained on the party that had the burden of proving reasonableness, the proponent. The protestant had to persuade the Commission that the railroad's information was not accurate or that it was interpreted incorrectly. The burden of proof could be substantiated with any relevant information that either proved or disproved the existence of market dominance for the rate at issue.

Later in that same year, A.T. Kearney submitted their final report to the Commission.[43] The report's purpose was to help the Commission refine its approach to market dominance and has been cited several times in its deliberations concerning market dominance. Market dominance was an important consideration in the Commission's railroad ratemaking policies by 1980. However, these new rules were short-lived because Congress amended the 4R Act in 1980, removing this area from the Commission's jurisdiction.

G. *The Staggers Rail Act of 1980*

Substantial changes in the procedural aspects of market dominance were advanced in both the Senate bill, and in the later House amendment, prior to passage of the Staggers Act. The Senate bill proposed a jurisdictional threshold level below which the Commission would not have authority to regulate railroad rates. A determination of a maximum reasonable rate was to be based on:

1) the amount of traffic which was transported at revenues below variable cost and efforts made to minimize such traffic; and
2) the amount of traffic which contributed only marginally to fixed costs; and
3) the carrier's mix of rail traffic to determine whether one commodity was paying a disproportionate share of a carrier's overall revenues.[44]

The House amendment to the Senate bill required that revenues exceed costs by at least 160% before the Commission would have jurisdiction to determine whether the rail carrier dominated a market. This jurisdictional threshold was expected to increase by five percent in each subsequent year through 1984.[45] The House amendment would also have established a "cost recovery percentage" as the price ratio at which the

42. 45 Fed. Reg. 3353, 3357 (1980) (to be codified at 49 C.F.R. pt. 1109) (proposed Jan. 17, 1980).

43. A.T. Kearney Management Consultants, A Study to Perform an In-Depth Analysis of Market Dominance and its Relationship to Other Provisions of the 4R Act, Final Report (1980) [hereinafter cited as A.T. Kearney, Final Report].

44. H.R. Rep. No. 1430, 96th Cong., 2d Sess. 4, *reprinted in* 1980 U.S. Code Cong. & Ad. News 4110, 4124.

45. *Id.* at 4122.

industry could recover its costs.[46]

The Staggers Act as signed into law by President Carter on October 14, 1980, limited the Commission's authority to those maximum reasonable rates that were set above a threshold level of 160% of variable costs.[47] But the Act still required the Commission to determine whether a railroad had market dominance before it could examine the reasonableness of the rate in question. Reasonable rates were defined in section 10701a(3) of title 49. The Commission had to find that a carrier did not dominate a market if the price-to-cost ratio for the period beginning on October 1 of one year and ending on September 30 of the next year was below:

1) 160 percent during the 1980-81 period; and
2) 165 percent during the 1981-82 period; and
3) 170 percent during the 1982-83 period; and
4) 175 percent or the cost recovery percentage (whichever is less) during the 1983-84 period; and
5) the cost recovery percentage for each 12 month period beginning on or after October 1, 1984.[48]

The cost recovery percentage, which was to establish the relevant rates at a percentage between 170 and 180% of revenue to variable costs, was to be determined by the Commission at a later date. If a rate was above the lower threshold level and was challenged by a shipper, the rate in question would no longer be presumed to have been set by a market dominant carrier. Under these circumstances the question of market dominance, as well as reasonableness, would be settled by the Commission on a case-by-case basis. A carrier would be shown to have market dominance if the rate at issue was demonstrated to be above the threshold.[49] If market dominance was not found, the rate would then be considered reasonable and removed from the Commission's jurisdiction.

H. Burden of Proof Under the Staggers Act

The primary burden of proof was shifted from the shipper to the carrier. A railroad proposing a rate increase had to prove that its price-to-cost ratio was below the threshold level for that year. Data from Rail Form A or any other valid costing approach could be used. Once the carrier demonstrated that the rate was below the threshold it established a prima facie

46. *Id.* at 4123. The "cost recovery percentage" would have established only the limits of the Commission's jurisdiction. Above the threshold, emphasis would have been placed on the revenue adequacy of the movement.

47. 49 U.S.C. § 10709(d)(2)(A) (Supp. V 1981).

48. 49 U.S.C. § 10701a(a)(3) (Supp. V 1981).

49. The Uniform Railroad Costing System (URCS) will replace Rail Form A as the Commission's primary railroad regulatory costing tool after it has been properly tested and reviewed.

case. A shipper then would have to refute the carrier's claim and show that the rate in question was above the threshold by either (i) restating the carrier's figures in a more accurate fashion; or (ii) by presenting a more accurate and reliable method of cost determination.[50] A rate above the lower threshold could be challenged by a shipper, who would have to prove that market power existed or that no transportation alternatives were available.

The Commission could only bring an action independent of a shipper's complaint when a rate increase placed a rate above the upper threshold or twenty percentage points above the lower price-to-cost threshold, subject to a ceiling of 190%.[51] In addition, any interested party could initiate an independent complaint. In these cases the carrier had the burden of proving the nonexistence of market dominance. If a railroad could not conclusively show that it did not have market dominance, the Commission would proceed to rule on the rate's reasonableness. On the other hand, if the railroad managed to prove that market dominance did not exist, the rate would go into effect without alteration.

Congress created these new standards for market dominance determinations because it judged the Commission's previous tests to be restrictive and complex. Congress believed that the railroads would not be able to extract monopoly profits once the protective standards in the Staggers Act were in place to protect the shipper against prior abuses. In addition, these revised requirements implied that the Commission should be more flexible in its interpretation of the law because Congress wanted the railroad industry to achieve adequate returns as soon as possible. Consequently, greater discretion was given to the Commission so that it could modify its procedures for regulating maximum rates for an increasingly competitive industry.

I. Ex Parte No. 320 (Sub-No. 2)

The Commission withdrew Ex Parte No. 320 (Sub-No. 1) because the Staggers Act achieved the same result that the Commission was striving for in its revenue-to-cost ratio. The passage of the 4R Act in 1976, and the Staggers Act in 1980, clearly narrowed the Commission's rate control jurisdiction. One of the Commission's primary tasks after passage of the Staggers Act was to interpret and to implement the provisions of section 202. On December 11, 1980, just one week before it withdrew Ex Parte No. 320 (Sub-No. 1), the Commission issued Ex Parte No. 320 (Sub-No. 2).[52] This policy statement significantly altered the Commission's procedures for determining market dominance.

50. 49 U.S.C. § 10709(d)(3) (Supp. V 1981).
51. 49 U.S.C. § 11701 (Supp. V 1981).
52. Market Dominance Determinations and Consideration of Product Competition, 364 I.C.C. 604 (1980).

The Commission's new position of rate reregulation enabled it to design rules more consistent with the intent of Congress and the relevant sections of the Staggers Act, as well as with the prevailing "deregulatory" mood of the day. The thrust of Ex Parte No. 320 (Sub-No. 2) was to allow the railroads to set the majority of their rates outside of the Commission's control of maximum rates.

Ex Parte No. 320 (Sub-No. 2) reflected the Commission's belief that there was no real need for the use of presumptions in the determination of market power because they did not enhance the accuracy of its findings. The presumptions had stressed quantitative rather than qualitative evidence and had become inappropriate for determining market dominance. The cost test had been superseded by section 10701a of the Staggers Act. The market share test was abandoned because of its inability to deal with highly complex factual situations. The substantial investment test was found to be an inefficient base for a presumption of market dominance because shippers were unable to link pertinent rail-related investments to the lack of other adequate transportation alternatives. In addition, Congress' new policy concerning contract rates (section 208 of the Staggers Act) further diminished this presumption's relevance. Only the limited rate bureau test, which was originally intended to be just an evidentiary tool for determining market dominance, remained, because the Commission believed that rate bureau activity automatically lessened competition. Thus, the Commission dropped the use of general standards for an approach more case specific, clearing the way for a new set of rulings and policy statements.

J. Guidelines for Submitting Evidence

In the place of the rebuttable presumptions, the Commission issued new rules in Ex Parte No. 320 (Sub-No. 2). The Commission's decision listed a set of evidentiary guidelines to be used in finding market dominance. These standards were intended to encourage the submission of more reliable and accurate evidence. The Commission also decided that evidence of geographic and product competition could be presented.[53]

These guidelines were separated into four major categories of competition: (i) intramodal competition; (ii) intermodal competition; (iii) geographic competition; and (iv) product competition. Each factor was to be a mandatory requirement. Evidence of each could be used by the carrier to disprove the presence of market dominance in a rate dispute.

The Commission defines intramodal competition as competition be-

53. Market Dominance Determinations and Consideration of Product Competition, 365 I.C.C. 118, 135 (1981).

tween two or more railroads transporting the same commodity between the same origin and destination, depending upon:

1) the number of rail alternatives;
2) the feasibility of each rail alternative as indicated by: a) the physical characteristics of the associated routes and; b) by the direct access of both shipper and receiver to the alternatives;
3) the transportation costs associated with each alternative (to determine if actual use of alternatives is due to excessive rates);
4) collective ratemaking among the railroads associated with the rate as evidenced by rate bureau involvement; and
5) evidence of substantial rail-related investment or long-term supply contracts (contracts signed before October 1, 1980, will be given more weight).[54]

As opposed to intramodal, intermodal competition is competition between rail carriers and other modes for the transportation. Intermodal competition for railroads exists primarily with the motor and water carrier industries, and this guideline was constructed to deal with each of these modes separately. The Commission required that evidence presented by any carrier to indicate competition between rail and water alternatives should show such factors as:

1) the number of alternatives;
2) the feasibility of each alternative as indicated by: a) the physical characteristics of the transportation routing; and b) the access of both shipper and receiver to each alternative; and
3) the transportation cost of each alternative.[55]

In addition, the Commission indicated that any evidence to be used in establishing effective competition between rail and motor alternatives should refer exclusively to the nature of the product and the needs of the shipper or receiver involved in the movement. Under these circumstances, effective competition could be deduced from information that indicated:

1) the amount of the product in question is transported by motor carrier where rail alternatives are available;
2) the amount of the product that is transported by motor carrier under transportation circumstances similar to rail;
3) the amount of the product that is transported using motor carrier by shippers with similar needs (distributional, inventory, etc.) as the shipper protesting the rate;
4) physical characteristics of the product in question that may preclude transportation by motor carrier; and

54. *Id.* at 131-35.
55. *Id.* at 133.

5) the transportation costs of the rail and motor carrier alternative.[56]

The third substantive guideline, geographic competition, refers to the ability of a shipper or receiver to obtain the product from another source or to ship to another destination. The Commission stated that this form of competition was important for products whose delivery price represents a substantial proportion of transportation costs. Evidence used to establish the potential for such competition should concern:

1) the number of alternative geographical sources of supply or alternative destinations available to the shipper or receiver for the product;
2) the number of these alternative sources or destination served by the different carriers; and
3) the similarity of the product available from each source or required by each destination.[57]

The Commission explained that to determine whether effective competition of this type actually existed, evidence presented by the carrier should indicate the feasibility of each source or destination in addition to the likelihood of competition of this form. The following types of evidence could be submitted:

1) the distance associated with each alternative source or destination;
2) relevant physical characteristics of the route associated with each alternative;
3) the access of the shipper or receiver to each transportation alternative;
4) the capacity of each source (or destination) to supply (or absorb) the product in question;
5) the transportation cost associated with each alternative;
6) collective ratemaking among the railroads in question as evidenced by rate bureau involvement; and
7) evidence of substantial rail-related investments or long-term supply contracts (contracts signed before October 1, 1980, will be given more weight).[58]

The final evidentiary guideline is product competition, defined by the Commission as the ability of a shipper or receiver to use a feasible substitute for a particular product. The presence of available substitutes, according to the Commission, can be established by evidence that these substitutes are obtainable through other carriers or modes without substantially greater cost or transportation. The evidence submitted should concern:

1) the use of a substitute product by the receiver or shipper or by others with similar needs and under similar conditions;

56. *Id.*
57. *Id.* at 134.
58. *Id.*

2) the prices of the substitute products relative to the price of the original product;
3) the efficiency of the substitute product relative to the original product; and
4) the explicit and implicit transportation costs of the substitute product and the original product.[59]

These guidelines are part of a program the Commission started after the passage of the Staggers Act to evaluate tariffs for exemption from rate regulation. The criteria are an integral part of the Commission's "deregulatory" approach to handling the problems of the railroad industry. They provide both carriers and shippers with a general indication of the type of information the Commission is interested in. The lists are not intended to be exhaustive, nor is each fact a mandatory requirement. Railroads now have the opportunity to recoup more of their costs because the standards allow more room for selective and innovative rail pricing. Potentially, the railroads will be operating under more certainty than at any other time in this century, enabling them to market their services in a more efficient manner.

These substantive criteria, however, make it more difficult for the shipper to prove that a carrier dominates a market. The National Industrial Traffic League (NITL) was among several groups which argued that these standards would make it easier for carriers to raise their prices, as most rates would be outside of the Commission's jurisdiction.[60] The NITL felt that its members would not be able to accurately demonstrate their status as captive shippers. Consequently, the guidelines were challenged at the administrative level and in the courts in an attempt to reestablish a greater degree of protection from rate abuse.[61] These efforts to block the use of the new evidentiary guidelines failed, and the criteria went into effect in August, 1981.

III. Additional Considerations

The evidentiary guidelines promulgated in Ex Parte No. 320 (Sub-No. 2) seem better suited to effecting the regulatory reform intent than the Commission's earlier presumptive standards. The degree of intermodal, intramodal, geographic and product competition should succinctly reflect the major factors affecting the elasticity of demand facing a rail carrier in a particular market. It is these factors which ultimately determine the workability of competition and the ability of the railroad to set rates. Although the market dominance principle now appears well-founded conceptually, certain

59. *Id.*
60. *Shippers Fight to Save Ability to Contest Railroad Rate Boosts Before ICC*, Traffic World, July 27, 1981, at 65.
61. *Id.*

measurement problems portend continued changes in the definition and application of the concept. The remainder of this article will explore possible solutions to some of these problems.

A. Criticism of the Presumptions and Threshold Tests

The standards developed under Ex Parte No. 320 (Sub-No. 1) were severely criticized by many different parties affected by their implementation. The main objection to the rebuttable presumptions referred to their generality; at least one of the presumptions would probably exist in any given case brought before the Commission. Because the rate regulations were vague, and potentially hazardous from the carrier's point of view, the railroads approached the new "freedom" provided by the 4R Act with scepticism and did not take full advantages of its provisions.[62]

The threshold tests, particularly the revenue-to-cost ratio test, proved to be less than adequate. While theoretically the best measures of rail dominance, these tests were only able to measure the average profit margin on sales, which is not necessarily correlated with degree of competition or return on investment. As shown in empirical research, the revenue-to-cost ratio is negatively correlated with other measures of rail market power.[63] One plausible explanation is that relatively high ratios represent the vestiges of rail market power and subsequent value-of-service rate making techniques.

Charging high rates for expensive commodities and low rates for cheaper commodities was a viable pricing strategy prior to widespread intermodal competition. A combination of questionable managerial practices and ponderous regulation continued this process of differential pricing long beyond its usefulness as a railroad pricing strategy and as a basis of public policy. Indeed, high value commodities are vulnerable to motor carrier competition. Thus, high revenue-to-variable cost ratios may not be indicative of rail market dominance.

The inadequacies of historical rate-to-cost relationships are compounded by the inadequacy of rail costing techniques. According to L.B. Boske, the use of Rail Form A costing procedures as the basis of estimating variable cost only served to make matters worse. The average historic cost concepts used in Rail Form A are inadequate to determine market dominance.[64]

B. Measuring Cost

The market dominance procedure, through revenue-to-variable cost

62. A.T. Kearney, Interim Report II, *supra* note 5, at VIII-7.
63. *Id.* at VII-8.
64. Boske, *supra* note 25, at 304.

threshold levels, has increased the costing responsibility of the Commission. In response to the need for a more sophisticated costing system to produce adequate costing results, the Commission moved to replace the old costing mechanism, Rail Form A, with the Uniform Rail Costing System (URCS). Although different from its predecessor in some respects, the URCS resembles Rail Form A in many important aspects. Both costing systems:

1) produce cost estimates based on the average cost of individual carriers or a group of carriers, or regional group of carriers;
2) incorporate an accounting-based approach to costing, relying on annual operating expense and traffic data reported by the carriers; and
3) rely on historic special studies to supplement the required annually reported operating expenses and statistics.[65]

Rates should reflect prospective costs to arrive at decisions on future operations. Since it relies on average historic system costs, the URCS may prove inadequate for rate making purposes. Revenue-to-cost ratios must be oriented toward the future cost of rail service and the overall investment of the carrier in order to be of value in proceedings resolving issues of market dominance.[66] The URCS has yielded inconsistent results in its initial application and may eventually be beset by the same problems which plagued Rail Form A costs.

The URCS relies heavily on regression analysis to calculate the revenue-to-variable cost threshold level in market dominance proceedings. The variable cost portion of operating expenses declined in 1978, 1979 and 1980 according to this analysis.[67] The problem with this result is that as the variable cost portion of operating expenses declines, the possibility that a given rate will lie above the revenue-to-variable cost threshold level increases. Instead of more rates lying outside the Commission's jurisdiction, potentially more rates will become subject to a full review under evidentiary guidelines.

The Commission appears to be somewhat at a loss to explain the changing behavior of railroad costs. The Commission's Bureau of Accounts, the group responsible for implementing the URCS, states that the inconsistent nature of costs may be due to several factors.[68] The answer may lie in a fault in the regression or the format used, only making it appear that variable costs are declining. If it is indeed a technical problem, the URCS can be corrected. However, if the change reflects a fundamental

65. Bureau of Accounts, Interstate Commerce Commission, An Introduction to the Uniform Rail Costing System: Its Development, Functions and Regulatory Role 25 (1981).

66. A.T. Kearney, Interim Report II, *supra* note 5, at VIII-16.

67. *ICC Readies Cost System But Mulls Figures That Could Expand Rate Power*, Traffic World, June 28, 1982, at 28.

68. *Id.*

shift in railroad operating structure the entire threshold test will have to be reconsidered, if not eliminated. Otherwise, the Commission, rather than the market, will be determining the reasonableness of the majority of rates. This regulatory scheme also has the drawback that it imposes substantial information requirements.

C. Data Gathering Burden

In submitting its final report on market dominance standards to the Commission, A.T. Kearney wrote that they "anticipate significant administrative [and legislative] impacts from [their] research."[69] Apparently this study did have a significant impact, for a major portion of it is reflected in the Commission's evidentiary guidelines. Therefore, the market dominance guidelines can be evaluated in terms of the criteria suggested by A.T. Kearney:

1) easily understood approaches and requirements;
2) ready availability of required data;
3) minimum cost for data preparation;
4) emphasis on competitive forces to control maximum rates;
5) adequate provision for shipper protection if market forces are inadequate to provide that protection; and
6) minimized Commission involvement consistent with the public interest.[70]

In addition, any market dominance standard, or set of evidentiary guidelines, should ensure a regulatory system that balances the needs of carriers, shippers, and the public.

Railroads should have little difficulty in supplying the additional information necessary to defend a rate change proposal, at least with respect to the revenue-to-variable cost threshold levels established by the Staggers Act, due to the Commission's general reporting requirements. Although much of the cost information required by the guidelines is publicly available, it is not as readily accessible to the shippers as it is to the railroads. Lack of access to information, combined with other evidentiary requirements, place opponents of rail rate changes at a disadvantage to the railroad proposing the change. Asymmetric access to and burden of information gathering is inconsistent with a regulatory system designed to protect shipper interests if competition fails to do so. The NITL's rebuttal to evidentiary guidelines reflects concern for this type of regulatory failure. Furthermore, recent changes in the rate bureau's role in setting rates and the types of rate changes carriers can propose may cause the alleged inequities to increase.

Rail rate bureaus may not permit individual carriers to discuss, partici-

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69. A.T. Kearney, Final Report, *supra* note 43, at i.
70. *Id.* at XI-6; *see also* Boske, *supra* note 25.

pate in, or vote on the single line rates of another carrier. With respect to interline movements, a carrier may only discuss, participate in, or vote on the applicable rate if it practicably participates in that movement. After January 1, 1984, if there are interline movements over two or more routes between the same end points, rail carriers are not permitted to discuss, participate in, or vote on rates except with a carrier which forms part of a particular single route.[71] These changes should lead to an increased number of rates filed by individual carriers and provide for greater rate competition in rail markets. While potentially beneficial, these actions will require substantially greater use of the market dominance guidelines, thus increasing both time and cost in meeting data requirements.

In conjunction with limiting rate bureau antitrust exemptions, acceptable forms of rate proposals are being circumscribed. General or across-the-board rate increase proposals have reflected the rise in operating costs and decline in cash flows sufficient for capital expenditures since World War II.[72] A general rate increase created to deal with these problems would obviously neglect the unique demand and supply conditions of a given market. As of January 1, 1984, general rate increases, currently limited to joint rates, are to be eliminated altogether;[73] thus, unique market conditions must be incorporated in future rail pricing strategies.

In fiscal year 1980, the Commission received 63,113 railroad freight rate tariffs.[74] The rate making changes outlined above will likely precipitate a greater number of individual rates being filed with the Commission, each of which must be measured against the revenue variable guidelines. Greater market-oriented pricing, then, may only exacerbate inherent information gathering burdens or inequities. These potential problems were at least partially recognized.

D. The Scope of Limited Regulation

Several authors have advocated that the Commission move in the direction of reducing individual shipper and carrier data requirements.[75] Common to these proposals is a programmatic approach to the market dominance principle whereby the Commission systematically, upon its own initiative, would review individual rail markets to assess the workability of competition. If a market is sufficiently competitive, rates would be presumed to be reasonable. If competition is not workable, the reasonableness of the rate in question would then be evaluated. Other than the

71. 49 U.S.C. § 10706(a)(3)(A) (Supp. V 1981).
72. D. Harper, Transportation in America: Users, Carriers, Government 465 (2d ed. 1982).
73. 49 U.S.C. § 10706(a)(1) (Supp. V 1981).
74. 94 ICC Ann. Rep. 113 (1980).
75. A.T. Kearney, Final Report, *supra* note 43, at XI-7; Boske, *supra* note 25, at 307-10.

change in information gathering responsibility, these proposals would retain the concept of limited regulation. It appears that the Commission, if so disposed, could undertake this course of action.

Title 49 empowers the Commission to exempt any person, class of persons, or a transaction or service by a railroad upon a finding that regulation is not necessary to carry out the national (rail) transportation policy, and either the service is of limited scope or the regulation is not essential to protect shippers from the abuse of market power.[76] Referring to the statement of rail transportation policy, we find that the policy of the U.S. government in the regulation of railroads is to allow, to the maximum extent possible, for competition and the demand for services to establish reasonable rates; and to maintain reasonable rates where there is an absence of effective competition and where rail rates provide revenues which exceed the amount necessary to maintain the rail system and attract capital.[77]

To date, the Commission has used its exemptive powers extensively. When important traffic segments are considered, only the rail transport of fresh fruit and vegetables,[78] miscellaneous agricultural commodities,[79] and the rail portions of trailer-on-flatcar and container-on-flatcar service[80] have been exempted. The exportation of coal moving by rail via Gulf and Atlantic ports, and rail boxcar traffic is being considered for exemption.[81] These segments of traffic account for large portions of all intercity traffic moved by rail, and the granting of exempt status by the Commission would have a tremendous impact on ratemaking policies.

Several points emerge from the above analysis. First, the criteria by which all regulation is to be judged is very similar to the criteria A.T. Kearney suggested for judging any Commission-established guidelines. Second, those markets already exempted were designated as such in order to be consistent with the national rail policy; regulation was deemed unnecessary because either the service provided was of sufficiently limited scope or workably competitive markets had developed. Given the importance of TOFC/COFC traffic to rail carriers, it is safe to conclude that the effective competition is central to Commission exemptions. It appears, therefore, that there is little conceptual difference between the application of Commission exemptive powers and the market dominance concepts. If a traffic segment qualifies to be relieved of rate regulation under one measure, it should logically be relieved of regulation under the other as well. Thus,

76. *See* 49 U.S.C. § 10101(a) (Supp. V 1981).
77. 49 U.S.C. § 10101a (Supp. V 1981).
78. Rail General Exemption Authority — Fresh Fruits and Vegetables, 361 I.C.C. 211 (1979).
79. Rail General Exemption Authority — Miscellaneous Agricultural Commodities, 367 I.C.C. 298 (1983).
80. Improvements of TOFC/COFC Regulation, 365 I.C.C. 728 (1982).
81. Exemption from Regulation — Boxcar Traffic, 367 I.C.C. 424 (1983).

when regulatory reform advocates are convinced of the ubiquity and consequential benefits of rail market competition, exemptions from regulation may become more common, thereby circumventing the entire market dominance mechanism altogether.

E. Other Pricing Considerations

The effect of shipper bargaining power is currently not considered under a market dominance analysis. Empirical evidence suggests that the sources of this bargaining power are intramodal competition, multiplant capacity, availability of alternative sources of supply and attractiveness of the commodity in terms of carrier costs and services.[82] The essence of shipper bargaining power is intramodal, geographic and product competition. Underlying the latter two factors is the availability of intermodal competition. These are the same four types of competition adopted by the Commission in Ex Parte No. 320 (Sub-No. 2).

Intramodal competition in the railroad industry is potentially significant, but at present cannot be relied on to protect shippers due to pricing agreements between railroads through rate bureau activity. However, intrarail competition, and therefore shipper bargaining power, should increase due to the rate making changes brought about the by Staggers Act. A recognition of this type of shipper bargaining power should be incorporated into any review of market dominance standards. Although contract service is at least nominal evidence of shipper bargaining power, no other recognition is found per se in the new guidelines. Carriers should be permitted to introduce shipper bargaining power as additional evidence of shipper alternatives for both geographic and product competition.[83]

In the future, market dominance standards should also reflect any special circumstances in rail movements. The Staggers Act attempted to incorporate such circumstances, at least with respect to seasonal traffic. This type of traffic is found in all regions of the country and on most Class I railroads. A major shortcoming of previous legislation, specifically the 4R Act, was that if any new rate was specifically labeled as a demand-sensitive or seasonal rate, the rate could automatically be subject to protest by shippers. The railroads then would be required to file supporting evidence, even when the movement was declared non-market dominant. However, A.T. Kearney believed that to ensure adequate carrier revenues legislation should integrate seasonal/peak concepts, and any revision in the market dominance standards must recognize the special needs of peak and seasonal pricing strategies.[84] By eliminating the special designations for peak

82. A.T. Kearney, Interim Report II, *supra* note 5, at VII-11.
83. A.T. Kearney, Final Report, *supra* note 43, at XI-5.
84. *Id.* at IX-8.

and seasonal rates of the 4R Act,[85] the Staggers Act has moved in Kearney's recommended direction. Yet, it remains to be seen how the new guidelines meet these special needs, and if they will prove to be at all successful.

Questions also remain as to the correct implementation of market dominance provisions even should the guidelines incorporate the shipper bargaining power and seasonal/peak rate issues. Various alternatives advanced propose that an *ex ante* determination of competitive markets be made by the Commission.[86] With these allowances for special pricing considerations, presumably more use would be made of rate making freedoms than in the past.

IV. Conclusion

Current market dominance standards reflect both the Congress' and Commission's firm belief in the effectiveness and desirability of competition. In the current marketplace, railroads are seldom in a position to display monopolistic tendencies because competition is so pervasive. If the assumptions of regulatory reform are correct, pricing freedom will achieve the results intended: the rail industry would receive a reasonable rate of return on its investment while marketing its services in a competitive environment, and shippers would possess adequate protection against carrier rate making abuse through the application of the market dominance and the corresponding zone of reasonableness principles found in the Staggers Act.

If these assumptions prove wrong and competition fails to materialize, we may find that the railroads do in fact possess substantial market power and use specific rate increases and a differentiated rate scale to further a system of unequal pricing. Railroads would thus be able to exploit imperfections in the transport market to their own advantage, while remaining outside the Commission's jurisdiction or influence. In this event, legislation similar to that existing before passage of the 4R Act, or some viable alternative, may prove to be necessary to provide for judicious regulation.

However, the market dominance concept, as drafted in its present form, is sufficiently flexible to allow for increased regulation through reinterpretation of the law. It is this flexibility which assures continued evolution of not only the market dominance concept, but of rail economic regulation.

85. Pub. L. No. 95-473, § 10727, 92 Stat. 1370, 1388 (1978) (repealed 1980).

86. A.T. Kearney, Final Report, *supra* note 43, at XI-7; Boske, *supra* note 25, at 307-10.