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Judicial and Regulatory Decisions

JUDICIAL AND REGULATORY DECISIONS

SUPREME COURT CONSTRUCTION OF MAIL RATE SUBSIDIES TO AIRLINES

THE Supreme Court of the United States has recently handed down a significant interpretation of the mail rate and subsidy provisions of the Civil Aeronautics Act.[1] This decision severely restricts the power of the Civil Aeronautics Board to exercise discretion in the granting of air mail subsidies. In *Delta Air Lines v. Summerfield*,[2] and *Western Air Lines v. C.A.B.*,[3] the Board attempted, through its power to grant compensation for the carriage of mail, to base subsidy awards on the economic and public policy which it assumed should be adopted toward the air industry. In computing the subsidy award the Board refused to offset certain past profits in the belief that not requiring their use as an offset would insure competitive equality among the airlines and would encourage mergers and route sales.

All of the commercial airlines, until recently, have been dependent from infancy upon government subsidies for their existence.[4] Monetary subsidies are granted under the guise of payment for the transportation of mail; awarded by the Board, and at the time this case was before the Board,[5] paid from the budget of the Post Office Department. The Postmaster General was of the view that the Board's interpretation was not well founded and, since forced to pay the subsidy, appealed. The Circuit Court of Appeals for the District of Columbia held that the Board had overstepped its power under the Act,[6] and the Supreme Court affirmed.

The Act authorizes the Board to fix rates for the transportation of mail in accordance with the following standard:[7]

> Section 406(b) "In fixing and determining fair and reasonable rates of compensation under this section, the Board . . . may fix different rates for different air carriers or classes of air carriers, and different classes of service . . . [T]he [Board] . . . shall take into consideration among other factors, . . . the need of each such air carrier for compensation for the transportation of mail sufficient to insure the performance of such service, and together with all other revenue of the air carrier, to enable such air carrier under honest, economical, and efficient management, to maintain and continue the development of air transportation to the extent and of the character

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[1] 52 STAT. 977 (1938), as amended, 49 U.S.C. Sec. 401, *et seq.* (1948).

[2] 347 U.S. 74 (1954).

[3] 347 U.S. 67 (1954).

[4] Subsidies are given in two forms: 1) direct monetary aid in accordance with the Act; and 2) indirect services supplied by the Government; such as Government airports, airway facilities, weather bureaus, and other navigational aids. In the last few years the domestic divisions of many of the larger carriers have been removed from the monetary need or subsidy category and put on a service rate, which the Board feels is lacking in direct subsidy, and is solely compensation for the carriage of mail.

[5] For services after October 1, 1953, subsidy payments will be given directly by the Board and only compensation for the carriage of mail will be given by the Post Office Department. Reorganization Plan No. 10 of 1953, 18 FED. REG. 4543 (1953).

[6] 207 F. 2d 207 (D.C. Cir. 1953).

[7] Section 406(a) "The [Board] . . . is empowered and directed . . . to fix and determine from time to time, after notice and hearing, the fair and reasonable rates of compensation for the transportation of mail by air craft, . . . " 52 STAT. 977 (1938), as amended, 49 U.S.C. Sec. 486 (a) (1948).

> and quality required for the commerce of the United States, the Postal Service, and the national defense."[8]

In 1948 the Board set a final subsidy rate for the domestic lines, *i.e.* routes within the United States, of Chicago & Southern Air Lines.[9] This action gave the airline its expenses for the transportation of mail, and an additional amount intended to cover all other expenses; bringing them a total percent return on their investment of 7.4.[10] During the next three years Chicago & Southern was more profitable than anticipated and accrued $654,000 in excess of the 7.4 percent return, resulting in a 12.5 percent return.

In 1951 the Board set the mail and subsidy rates for Chicago & Southern's Latin American routes. In fixing the compensation for the past operations of the foreign division the Board refused to offset the additional $654,000 which the domestic division had earned.[11] In so doing the Board interpreted the statute as giving them the discretion to consider each division of Chicago & Southern as a separate entity for subsidy purposes. In addition they felt that the "need" of the airline, which is that amount over all other revenue which will satisfy the statutory objectives, was only one factor to be considered. The Postmaster General appealed from this determination on the ground that the Board must find the need of the carrier as a whole, and award the subsidy in strict accordance with that need. The Circuit Court of Appeals and the Supreme Court accepted the Postmaster General's contention.

The problems presented are: 1) did the Court correctly interpret the statute; 2) is this interpretation in accord with public economic policy; and 3) if not, what should be done to remedy the situation. Viewing the problem from a strict legalistic approach the Court's decision would seem to be correct. However the economic policy which the Board is attempting to foster is in accord with the best interests of the airlines themselves and with the public's desire for an efficient and aggressive air industry. The following discussion attempts to point out the basis of the Court's decision and the policy arguments which make this decision somewhat undesirable.

Legal Issues Involved

Interpretation of the Civil Aeronautics Act involves two questions: 1) must the carrier's operations be considered as a whole; and 2) if so, does the Board have the power to consider public economic policy, as well as need, of the carrier, in setting the subsidy rate? In determining the first question the Board and the airlines argue that the statutory authority to " . . . fix different rates for different air carriers or classes of air carriers, and the different classes of service,"[12] means that in computing subsidy awards the Board may treat the domestic and foreign divisions as entirely separate. The basis for this conclusion stems from arguing that "different classes of service" contemplates different divisions within an airline. However, to interpret an isolated provision, reference should be made to the remainder of the statute and to prior interpretations. The Act later directs the Board

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[8] 52 STAT. 977 (1938), as amended, 49 U.S.C. Sec. 486(b) (1948).

[9] Since that time, Chicago & Southern has merged with Delta Air Lines. Delta-Chicago and Southern Merger Case. CCH AVIATION LAW REP. 21,557. Delta was the survivor of the merger and was substituted as the intervenor subsequent to the decision of the Court of Appeals.

[10] Chicago and Southern A.L. Mail Rates, 9 C.A.B. 786 (1948).

[11] Subsidies are awarded for both past and future operation. If the Board had determined to offset the $654,000 it would have reduced payment for past mail transportation by this amount and would not have reduced future subsidy rates.

[12] 52 STAT. 977 (1938), as amended, 49 U.S.C. Sec. 486(b) (1948).

to consider "the need of each such air carrier"[13] and defines air carrier in terms of a single undivided corporation.[14]

In addition, the Board itself has, in the past, determined that for the purpose of fixing rates the need of the carrier is that of the whole airline, and not the need of a single geographical division.[15] Since both the Act and prior Board determinations have considered the carrier as a single non-divisable unit for determining the need of the carrier, what is the effect to be given the provision that the Board *may* fix different rates for different classes of service?[16]

The Board itself has supplied the answer in its practices, for as a procedural expedient it often determines domestic and foreign rates at different times, and in setting future returns gives the foreign divisions a greater rate of return on investment than it gives to the domestic.[17] But in fixing rates separately the Board is still bound by the requirement that the need is that of the whole carrier, and not the need of one of its divisions. Since this provision does have a definite meaning, other than that ascribed by the Board in this case, and since both the Act and the Board have considered the carrier a non-divisible unit, the Court's interpretation seems to be correct. However, Judge Prettyman in the Court of Appeals was so impressed with certain policy considerations that he dissented on the ground that the divisions may be considered separate for rate setting purposes.[18]

Secondly the Board argues that even though they must consider the carrier as a whole, they may balance the need of the carrier with public policy.[19] The Act authorizes the Board to "take into consideration" the need of the carrier together with all other revenue.[20] By the term "all other revenue," it seems certain that Congress intended that the Board should consider all of the carrier's revenue and not just some. The need of the carrier is that amount over all other revenue which will enable the carrier to "maintain and continue the development of air transportation."[21] Having ascertained the need of the airline, the remaining question is whether the Board must award the subsidy in strict accordance with that need or, whether for policy reasons, it may allow the carrier to retain amounts in excess of their need. From a literal construction of the statute it would seem that Congress endorsed the second choice since the statutory mandate requires only that the Board take need into "consideration." However, to so hold, would leave the Board with no measurable standard in determining

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[13] *Ibid.*

[14] 52 STAT. 977 (1938), as amended, 49 U.S.C. Sec. 401 (2), (13) (1948).

[15] Chicago and Southern A.L. Mail Rates — Route Nos. 8 & 53, 3 C.A.B. 161, 190 (1941); Pan. Am. Airways Inc., Alaska Mail Rates, 6 C.A.B. 61, 67 (1944); Pan. Am. Airways, Inc., Mail Rates, 8 C.A.B. 876, 882 (1947); Western A.L. Mail Rates, 4 C.A.B. 441, 444 (1943).

[16] It is frequently said that in statutory construction effect must be given to every provision. 1 KENT'S COMM. 462 (13th ed. 1884); 2 SUTHERLAND, STATUTORY CONSTRUCTION Sec. 4705 (3rd ed. Horack 1943).

[17] As a rule the Board gives a seven percent return on investment on both foreign and domestic divisions when setting a past rate, while in setting future rates an eight percent rate of return is usually allowed for domestic divisions and a ten percent rate for foreign divisions. This added return for future foreign divisions is apparently due to the greater uncertainty surrounding foreign operation.

[18] 207 F. 2d 207, 212 (D.C. Cir. 1953).

[19] Brief for the Civil Aeronautics Board, pp. 39-44, Delta Air Lines v. Summerfield, 347 U.S. 74 (1954).

[20] 52 STAT. 977 (1938), as amended, 49 U.S.C. Sec. 486(b) (1948).

[21] *Ibid.* It is important that the Board did not determine that the carrier "needed" the extra $654,000, but only that as a matter of policy the excess should not be taken into account in determining the subsidy. If the Board had determined that Chicago & Southern did need the domestic excess, the case would be entirely different and much more favorable to the Board.

the subsidy. It seems improbable that this could have been the intent of Congress in drafting the statute in light of the carefully worked out need formula. If such discretion was intended it would have been a simple matter to have explicitly given the Board the desired discretion. The better reasoning would seem to be that unless Congress has expressly given an agency wide discretion in the granting of public funds such discretion should not be read into the statute. Following this approach need appears to be an absolute standard and the subsidy grant must be based solely on the determined need. From the foregoing discussion it appears that the Court properly interpreted the statute before it.

In accordance with recognized judicial policy it may be contended that the Board's interpretation of the Act is reasonable, and thus should be allowed to stand.[22] Assuming that the Board's construction is reasonable and founded in the record, it still does not follow that the judiciary is precluded from review. A limited scope of review is, as a rule, utilized only where the decision is a technical one particularly suited to the expertness of the Board members, and where the effect of the interpretation is limited in its scope and does not substantially affect the law in the area.[23] However, as is here involved, when an agency interprets an Act of Congress, and that interpretation will greatly affect the power of the agency itself, the Courts should review that decision in its entirety.

Economic Problems

The foregoing discussion has treated only the problem of statutory construction with no consideration of the economic and policy factors underlying the Board's interpretation. It is now necessary to examine these factors upon which the Board bases its rationale in order to see if the Court's decision is desirable.

The first consideration is that under the Court's decision there is a lack of finality once the subsidy rates are set, in spite of the fact that the Board attempted to fix final rates when it set the domestic rates for Chicago & Southern.[24] Under the Court's decision the domestic subsidy for carriers operating both foreign and domestic routes will not become final until the foreign rates are set.[25] In competitive economy it is desirable that when future rates are set they be final, and not subject to later change, in order to encourage management and operation economy. Unless rates are final, when set, a carrier operating both domestic and foreign lines would have a lack of interest in economy, since economical operation would result in a

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[22] American Airlines v. Civil Aeronautics Board, 178 F. 2d 903, 908 (7th Cir. 1949). The Circuit Court said "Our function is limited; we may only inquire as to whether the Board's interpretation of the statute [the Act] has warrant in the record, and a reasonable basis in law."

[23] Davis, *Scope of Review of Federal Administrative Action*, 50 COL. L. REV. 559 (1950).

[24] Chicago and Southern. A.L. Mail Rates, 9 C.A.B. 786, 812 (1948). The Board in fixing what it considered to be final rates said "Similarly, any economies which the carrier's management succeeds in accomplishing through effective cost controls or improved operating procedures and techniques which serve to avert or mitigate anticipated increases in prices and to decrease operating costs below the unit cost of 116.6 cents per revenue plane mile estimated herein will inure to the carrier in the form of higher earnings."

[25] Rather than being final when fixed, the excess profit earned through added efficiency under the domestic rates would be used to offset losses on foreign lines, and by the same token if the carrier were to lose money on its domestic routes such losses should be made up at the time the foreign rate is set. It seems impossible that such procedure would do anything other than retard management and operational economy.

gain only to the public treasury and not to themselves.[26] This follows from the realization that a carrier will lose money on its foreign lines and all profit that it accrues through economies on its domestic lines will be used to offset the foreign loss. Since rate finality enhances carrier economy, such rate fixing is desirable since present economy will result in lower future subsidies.

The second contention in the Board's public policy argument is that the instant decision will result in inequitable competition. The overseas lines of the air carriers today are rapidly losing money whereas the domestic lines are for the major part self-sufficient and no longer in need of subsidy.[27] With the Board's policy of rate finality undisturbed, except as to the four[28] lines engaged in both domestic and foreign operations, it is clear that these four are at a definite disadvantage. Under the rate finality plan the six other major trunk carriers would be allowed to retain whatever excess they might accrue through economy while the four operating both domestic and foreign lines will have their domestic excess profits offset against their certain foreign losses. Thus, while American Air Lines might have a fifteen percent return on investment due to economy measures after their rate was set, Delta Air Lines could not possibly have a greater return than that minimum authorized by the Board. Therefore it is clear that those carriers operating in both the domestic and foreign fields will be at a competitive disadvantage, since the carriers with only domestic lines may use their excess profits for better accommodations, advertising, or perhaps to reduce fares; while those operating in both fields would be forced to use their domestic excess to offset foreign losses. That the airlines should be allowed to expand through competition has been recognized by the Supreme Court[29] and by Congress in the Civil Aeronautics Act.[30] The competitive disadvantage under which these lines operate would have the possible effect of allowing the domestic carriers to grow larger and stronger while the foreign-domestic carriers would be forced to rely more and more on government subsidies.

A third basis of the Board's rationale is that the Court's decision will retard rather than promote interest and development in the field of international air traffic. The nation's foreign policy requires full and active participation by the air carriers in international air transportation. While it may be difficult for an airline to drop an existing foreign route,[31] a car-

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[26] This objection is partially compensated for by the fact that the Board is authorized to fix compensation sufficient to enable the carrier under *economical* management to meet the statutory objectives. If the Board were of the opinion that the carrier was not economical it could reduce its need rate so that only economical management would give the proper return on investment. As a practical matter however, it would be difficult for the Board to say that a certain carrier was not economical without definite facts to back it up and needless to say these facts would be difficult to ascertain.

[27] Civil Aeronautics Board, Report, Administrative Separation of Subsidy from Total Mail Payments to United States Air Carriers, September 1953 Revision, App. 4 and 9 (1953). For the current fiscal year ending June 30, 1954, the Board estimates that for those carriers having both domestic and foreign operations, only 4.7 percent of the total $10,474,000 which will be paid for domestic operation will represent subsidy, while 69 percent of the total $18,356,000 to be paid for foreign operation will constitute subsidy.

[28] Trans World Air Lines, Braniff Air Lines, Northwest Air Lines, and Delta Air Lines.

[29] T.W.A. v. Civil Aeronautics Board, 336 U.S. 601,606 (1949).

[30] 52 STAT. 977 (1938), as amended, 49 U.S.C. Sec. 402(d) (1948).

[31] The Act provides "[k] No air carrier shall abandon any route, or part thereof for which a certificate has been issued . . . unless the [Board] shall find such abandonment to be in the public interest . . . " 52 STAT. 977 (1938), as amended, 49 U.S.C. Sec. 481(k) (1948).

rier must be "willing" to enter the international field or to extend its existing foreign routes before the Board may authorize it to do so.[32] Since a carrier in the international field is precluded from keeping excess domestic profits, it is a reasonable assumption that airlines will not be willing to enter the foreign field. The validity of this statement was recently borne out when the Board suggested a merger between Western Air Lines, a non-subsidized domestic carrier, and Alaska Air Lines, a carrier operating between Alaska and the United States. Although the merger would have resulted in more efficient and economical operation, Western refused to merge, since by the Court's decision it would have had to offset its domestic profits on the Alaskan losses.[33]

It has been suggested that airlines will become entirely self-sufficient only if they exercise a policy of merger and route transfer.[34] Through the merger of several of the smaller lines to form a few large lines, and the transfer between airlines of unprofitable and inefficient routes to carriers that could better operate them, the Government's subsidy bill would be greatly reduced and efficiency would be increased.[35] The possibility of mergers between carriers operating foreign lines with those operating only domestic lines has been reviewed above. A merger between two wholly domestic carriers, or the transfer of a domestic route certificate between carriers could work no monetary hardship, as would a foreign-domestic merger, but the carriers have been hesitant to complete domestic mergers or sell route certificates. Working on the theory that they could not force such mergers or sales, the Board has proceeded under the view that by profit motives they could encourage such action. Such was the position of the Board in the companion case, *Western Air Lines v. C.A.B.*,[36] where, in fixing Western's mail compensation, the Board refused to include in "all other revenue" certain profit accruing to Western Air Lines on a route sale to United Air Lines.[37] Consistent with the principal case, the Court held that "all other revenue," which is to be offset against the need of the carrier, must include all of the carrier's revenue regardless of its source, and in effect held that the Board could not foster such sales through the profit motive. By the proper application of this power the Board could significantly strengthen and stabilize the air industry, however regulation to this extent by the Board might weaken the independent and competitive nature of the airlines. Since the carriers are becoming stronger and more self-sufficient year by year it would perhaps be best to rely on private initiative to settle problems of merger and route transfer, without monetary encouragement from the Board.

The Court did not deny the weight of the Board's arguments on economic policy in the *Delta* case[38] but held only that such action was not authorized by the Civil Aeronautics Act. The Board's position in that case was not one

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[32] 52 STAT. 977 (1938), as amended, 49 U.S.C. Sec. 481(d) (1) (1948).

[33] Brief for the Civil Aeronautics Board, p. 28, Delta Air Lines v. Summerfield, 347 U.S. 74 (1954).

[34] Koontz, *Economic and Managerial Factors Affecting Subsidy*, 18 JRL. OF AIR LAW & COM. 127 (1951); Comment, 60 YALE L. J. 1196 (1951).

[35] The subsidy for the domestic services of Chicago & Southern is estimated to have been reduced $539,000 a year as a result of their merger with Delta.

[36] 347 U.S. 67 (1954).

[37] Western operating a route between Los Angeles and Denver sold that route to United Air Lines for $3,750,000. Of this $648,102 was computed as profit on the sale of tangibles and $447,000 as profit on the sale of intangibles, presumably good will and the like. The Board refused to include in its computation of "all other Revenue" the intangible profit feeling that the sale was in the public interest and that the retention by Western of the intangible profit would provide an incentive for other carriers to make such sales.

[38] Delta Air Lines v. Summerfield, 347 U.S. 74, 79-80 (1954).