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# FEDERAL

Department Editor: Charles T. Lloyd\*

## ERNST & ERNST REPORT COVERING PRELIMINARY STUDY OF METHODS OF COMPENSATION FOR CARRIAGE OF DOMESTIC AIR MAIL AND FOR THE OPERATION OF AIR TRANSPORTATION SERVICE ESSENTIAL TO THE PUBLIC INTEREST†

**I**N accordance with the directive of Senator Edwin C. Johnson, Chairman, Committee on Interstate and Foreign Commerce, we have made a "pilot study" of the problems attendant upon compensation of the certificated domestic air carriers engaged in the carriage of mail within the borders of the United States.

The intent of the Civil Aeronautics Act of 1938, as Amended, with respect to compensation to be paid carriers, was defined by the Civil Aeronautics Board in American Airlines, 3 C. A. B. 323, 335, (1942), in which the Board stated—

"The 'compensation' to be paid to the carriers in the air mail rate is not merely compensation for the transportation of mail. The use of the mail payments is a statutory device for the accomplishment of national objectives that transcend the interests of the Postal Service. These objectives, expressly stated in the Act, encompass the maintenance and continued development of air transportation to the extent and of the character and quality required for the commerce of the United States, the Postal Service, and the national defense. The compensation which the carrier receives thus becomes compensation not only for carrying the mail but for the building up of a system of air transportation which will serve the nation's commerce and security as well."

The purpose of the study was to advise the Committee as to the need (1) for the formulation of a consistent and understandable air mail rate structure and (2) for devising a method by which payments to the carriers by the Government could be identified as compensation for the carriage of air mail and as compensation for those other services contemplated by the Act.

During the progress of the study, conferences were held with operating and financial executives of a majority of the certificated domestic air carriers. Personnel of Government agencies concerned in the carriage of air mail, have made available their time in discussion of the problems involved. Members of the professional staff of your Committee have contributed to this study and extended their full cooperation.

Field studies in connection with the handling and dispatch of air mail were conducted at selected major airports.<sup>1</sup>

A brief summary of conclusions and recommendations follows:

1. Segregation of compensatory air mail pay from the total payments to the carriers by the Government will not of itself lessen the current need of the carriers nor provide the primary means of reducing total expense to

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<sup>1</sup> List of 11 carriers and 5 government agencies interviewed during this study is omitted.

the Government, unless accompanied by a mail rate structure which affords an incentive to the carriers and a means of determining auxiliary payments which cover efficient operation on routes held to be essential in the public interest.

2. Fair and reasonable rates, uniformly applied, for the transportation of mail by aircraft, should bear a definite relationship to the rates applicable to passenger transportation service which has aggregated more than 80% of the revenue ton-miles flown during the past eight years. Mail rates established in this manner would thus be consistent with the rates established for 80% of the volume, would at least provide the same incentive inherent in the other rates and would serve to eliminate the need for attempting to separate operating costs between those applicable to air mail transportation and other services. The greater portion of operating costs are joint costs applicable to all services and it should be recognized that a specific cost separation between those applicable to transportation of mail and other services is impractical.

3. The amounts of auxiliary payments for services other than the carriage of mail, and held to be in the public or national interest, should be based upon the operating effectiveness and specific requirements of the individual carriers. Such auxiliary payments could be paid from specific funds so appropriated and not be a part of the operating budget of the Post Office Department. Auxiliary payments which are predicated upon a budgeted efficient operating program applicable to the operating conditions incurred, rather than on actual historical results of operations, will serve to eliminate payments for inefficient operations and provide an additional incentive to the carriers.

4. Basic standard data should be developed which will make possible the budgeted operating costs of each individual carrier in order that equitable auxiliary payments can be provided for when the individual carrier under efficient operation cannot operate at a reasonable profit. Composite industry standards cannot be used for purposes of judging the relative efficiency of the individual carriers because of the many and constantly changing variables inherent in the operations of the various carriers.

5. The present domestic route pattern should be studied with the view toward possible elimination or consolidation of certain route segments which were certificated during the rapid growth of the industry and which may have brought about excessive competition, thus resulting in larger payments by the Government than are warranted to cover the cost of services held to be essential in the public interest. In any revision of the domestic route pattern which may call for elimination or absorption of routes or segments of routes by other carriers, it would seem that protection could be afforded the owners of such assets as may be involved. Thus, in place of continuing auxiliary payments indefinitely to cover services which are determined to be no longer warranted in the public interest or national defense, a final settlement representing the loss on disposal of operating assets would be an economical move.

6. Certain changes in the Civil Aeronautics Act of 1938, as Amended, would be necessary to permit the application of the foregoing conclusions.

In the following section, the requirements for a basic rate structure and auxiliary payments have been outlined and a method for their formulation has been proposed. Also the need for establishing standards and what may be accomplished from their use has been pointed out. It is recommended that this pilot study be followed by the detailed analysis required

to permit the implementation of the conclusions and proposals set forth in this report. The objectives capable of attainment by the fulfillment of this program and the resultant benefits include the following:

1. A consistent and understandable system for compensating the air carriers can be substituted for the diverse and complex methods which are now a burden to both carriers and Government agencies.
2. Development and use of proper standards will not only provide all concerned with an accurate means for measuring operating efficiency, but will furnish the carriers with an invaluable aid to management.
3. By use of such standards, the carriers will be enabled to forecast and measure their accomplishment with greater accuracy. By this method, the "need" of the carriers may be equitably determined.
4. Auxiliary payments (for services other than the carriage of mail) to the carriers will be identified from compensation for the carriage of mail, thus making it possible to relieve the Post Office Department of responsibility for budget and payment of funds not related to its activity.
5. Through such identification, attention will be concentrated upon operating methods and procedures and a constant incentive provided toward increased efficiency.

#### DISCUSSION

##### *Compensation for Carriage of Mail*

After giving consideration to the various factors affecting the cost of transporting mail by aircraft, it is believed that a rate structure used in compensating carriers for such service should consist of the following:

1. A fixed element to cover the handling and terminal costs necessary for and incident to the loading, handling, and unloading of mail.
2. A variable element to compensate carriers for the air transportation of mail, based upon a direct relationship to the passenger rate structure.
3. The above to be subject to a minimum poundage for each designated flight with gradual step increases for increased poundage, coupled with a provision for the control of designated flights.

By having a fixed element in the rate structure to cover costs incident to handling mail at terminal points, recognition is given to the cost of making service available and to situations where terminal costs are a relatively high proportion of the the total costs incurred in connection with short hauls.

The introduction of a basic mail rate covering both the handling and transportation of mail, used in conjunction with a minimum designated weight of mail per trip and step increases for use in compensating carriers for poundage over the minimum, gives recognition to the high degree of fixed cost to which carriers are subjected in making service available. Further, such a method will recognize the fact that carriers must maintain staffs and facilities of adequate strength to successfully handle fluctuating volumes of mail.

These provisions in the rate structure will place added responsibility on the Post Office Department in selection of designated flights and in forecasting anticipated volume.

The use of minimum charges and step increases is generally universal in rate structures of utility companies and in pricing industrial commodities.

It is found in postal rates, electric light and power rates, gas and water rates, surface transportation freight rates and Pullman fares. It is believed that this principle is equally applicable in the settling of rates for purposes of compensating carriers for transportation of mail by aircraft.

In establishing a fixed element of cost to cover the handling of mail, a series of studies would have to be made at the various terminals. These studies would employ accepted methods of motion and time analysis. Such studies would not only provide an allowance for the handling of mail but would also serve to establish uniform methods and procedures. It is contemplated that proper allowances will be made in cases when ground personnel encounter unavoidable lost time by reason of the irregularity of schedules or because of other such valid circumstances.

The basic rates designed to compensate for the carriage of air mail should bear a relationship to the passenger fare for the following reasons:

1. The passenger rates represent amounts that the public is paying for a measured amount of service.
2. The passenger rates represent the selling price of the industry's major source of revenue. The percentage of mail ton-miles to total ton-miles for the years 1946, 1947 and 1948 has approximated only 5% for each of these years.
3. A direct relationship of this kind is easily understood by the public.

In stating that the mail rate and passenger fare structures should be related, it is contemplated that the passenger fare will be used as a starting point, to which necessary adjustments will be made for such expense items as pertain to the direct handling of passengers. Either first class passage or coach rates can be used as the starting point, as long as the proper adjustments in the reconciliation are made and higher minimums and larger step increments are recognized to correspond with higher anticipated load factors in the coach rate structure.

When the adjusted rate has been established, it would be applied to a predetermined quantity of mail on routes and flights designated by the Post Office Department. In effect, a minimum space or quantity would be established for which the carrier would be guaranteed minimum compensation for the carriage of mail. To simplify computation of compensation, units of space or quantity should be established in even increments.

It must be recognized that a uniform relatively simple compensatory rate structure that bears a reasonable relationship to the passenger rate structure (that covers 80% of the total revenues), coupled with an equitable means of determining auxiliary payments when the total revenues are inadequate to cover efficient essential operations, is far more practicable than to attempt specific cost separations or over-all allocations of a joint operation which in the end can only be accomplished by many disputable arbitrary assumptions.

In support of our contention that a specific cost separation between those applicable to transportation of mail and other services is impractical, we submit the following:

The Board, in a show-cause order, used a method of cost allocation to establish a mail rate in which costs applicable to services performed jointly were allocated on the basis of the ratio of mail ton-miles carried to total payload ton-miles.

Some carriers as well have employed this ton-mile formula in an attempt to determine the cost of transportation of mail by aircraft, but the Board

itself acknowledges the method's shortcomings when it states, in an Eastern Airline rate case (Docket No. 3021)—“a straight proration of joint costs between services regardless of relative volume will unduly burden those services constituting the larger volume and will relieve the small volume service of a portion of those minimum fixed costs necessary to provide any service.” The relationship of cost and volume of the various services are expected to be ever-changing from day to day, and the ton-mile allocation method does not give proper recognition of the fixed costs associated with making the service available.

As an illustration of the inaccuracy resulting from the allocating of costs under the ton-miles flown formula, assume that the normal available payload of a flight is 3,000 pounds. Of this amount, assume the space reservation for expected mail load to be the equivalent of 200 pounds. For this planned operation 1/15th of the flying costs could reasonably be allocated to transportation of mail. However, under actual conditions, assume that the total payload is only 2,000 pounds, of which 250 pounds are mail. Under these conditions, and, as exemplified by use of the ton-mile formula, the costs allocable to transportation of mail would be 1/6th of the total cost. It is obvious that there only can be considerable question as to the equity of the results obtained.

#### *Auxiliary Payments*

The above section outlined the recommended basis for computing compensation for transportation of mail. The following paragraphs outline the recommended method for determining auxiliary payments when the total revenues are inadequate to cover efficient operation of a carrier which is deemed essential in the public interests.

As mentioned in the Act, Section 406(b) provides that in fixing and determining fair and reasonable rates of compensation for transportation of mail by aircraft, the Board shall take into consideration the need of each carrier for the purpose of enabling such carrier under honest, economical and efficient management, to maintain and continue the development of air transportation to the extent and of the character and quality required for the commerce of the United States, the Postal Service, and the national defense.

While the Act contemplated that carriers would be reimbursed for losses of the above nature, it did not contemplate reimbursement for avoidable losses resulting from management inefficiency. In the administration of the Act, the Board, therefore has a responsibility to detect such inefficiency and to withhold payments for losses incurred thereby. Auxiliary payments for services other than the carriage of mail, therefore, should be based on the individual carrier's operating performance. A later section of this report outlines the standard cost and revenue accounting techniques recommended for use by all carriers as an aid in achieving efficiency. Any auxiliary payments should be based on the accomplishment shown by the carrier in meeting the standard “Total Cost of Operations” as reported on the “Quarterly Report of Operations” (Exhibit A). Auxiliary payments when warranted for services other than the carriage and handling of mail should be based on the difference between actual revenue for the quarter and the total “Standard Cost of Operations” (Exhibit A), at the volume experienced for the period. In this manner, an incentive is provided to keep actual expenditures within the limits of standard expenditures related to the available ton-miles actually flown.

In order to eliminate the possibility of inflating the total standard cost, it would be necessary to adjust the standard cost for any excessive, uneconomical flying as indicated by the "Load Factor Variance" on the "Analysis of Variance from Standard Revenue" described later in this report. Thus, if a carrier's actual flight hours in a quarter exceeded his budgeted flight hours and the load factor did not maintain the proper relationship to the hours flown, his auxiliary payment would be affected thereby.

The above method of payment would not, however, exclude payment on an actual reimbursement basis for unusual and unavoidable expenses.

*Standard Cost and Revenue Accounting Development  
of Operating Cost Standards*

At the present time the Board is handicapped in accurately evaluating the operating efficiency of the carriers. In the Board's answer to an inquiry during the recent Senate Committee hearings, regarding the feasibility of using objective cost standards, the following statement was made:

"The Board regards the development of more objective cost standards as necessary both to the discharge of its obligations to establish fair and reasonable compensation for the carrier of mail, under honest, economical and efficient management and its obligation to foster and develop a sound healthy and efficient Air Transport Industry in the interests of commerce and the national defense. Accurate cost standards would not only provide the Board but also management and the investors, with essential tools with which to judge and evaluate the carrier's performance. The Board regards the development of cost standards as a necessary prerequisite to the attainment of efficient operations and the ultimate realization of a status of self-sufficiency.

"Some two years ago a small cost analysis group was established in the Accounting and Rates Division. Around this nucleus we hope to develop a body of specialists in the several areas of air transport operations who, through their experience in analyzing the operating costs of all air carriers, will be in a position to construct cost yardsticks for each cost area and set up attainable standards adapted to the operating peculiarities of each route."

It is apparent from this statement that the Board recognizes the need for development and establishment of objective cost standards, but the Board has been required to continue to use historical or reported costs in the absence of these desired objective cost standards.

Under this procedure, the Board relies upon historical costs to provide valid standards for comparative purposes. This procedure is questionable as the effect of any and all past unidentified inefficiencies are carried forward as a part of the yardstick which is used in comparing current and projected costs in rate-making proceedings. Also, under this procedure, it is difficult to detect warranted increases in costs which are beyond the control of the carrier.

In order to provide the proper means of measuring effectiveness, it will be necessary to establish separate "Operating Yardsticks" for each carrier, taking into account specific conditions of fleet make-up, route and schedule patterns and conditions, etc., for each carrier and to evaluate the efficiency of each carrier's operation in terms of performance against the standard established in the light of its own set of operating conditions. Thus, a carrier reporting a 95% performance against standard would be operating more efficiently than one reporting 80% *even though the standard of the former be higher by reason of different operating conditions beyond the control of the carrier.* For example, the standard maintenance and flight operation costs

per flight hour of a specific aircraft type would be greater for a carrier averaging 100 miles between scheduled stops than for one averaging 500 miles between scheduled stops.

A typical example of measuring operating performance in a specific function follows:

The standard man-hours representing the amount of work required to recondition an engine type can be determined through motion and time study techniques. When such techniques have been applied to the various operations required in the overhaul of each type engine, the result can be expressed as standard man-hours per each type of engine. It follows that when the total engine maintenance production in a given period is multiplied by the earned hours per each type of engine and compared with the total actual man-hours consumed, the degree of effectiveness is reflected.

*Use of Cost Performance Reports*

Under standard cost and revenue accounting, the monthly and quarterly financial reports take the form shown in Exhibit A. With standards realistically established for each individual carrier, the percentage of performance

ILLUSTRATION QUARTERLY REPORT OF OPERATIONS (ACTUAL SIZE 8 1/2" X 11") (PROPOSED)						
EXHIBIT A						
	AMOUNT - PERIOD			YEAR TO DATE		
	STANDARD	ACTUAL	VARIANCE	STANDARD	ACTUAL	VARIANCE
REVENUE						
OPERATING EXPENSES						
FLIGHT OPERATIONS						
ADMINISTRATIVE						
FLIGHT ADMINISTRATION						
PILOTS AND CO. PILOTS						
RADIO OFFICERS						
FLIGHT ENGINEERS						
FLIGHT SERVICE						
PASSENGER SERVICE						
COMMUNICATIONS						
TRAINING SECTION						
AIRCRAFT RENTALS						
SUB TOTALS						
STATIONS OPERATIONS						
MAIN BASE MAINTENANCE						
SALES						
ADMINISTRATION						
SALES OFFICES						
ADVERTISING						
SUB TOTALS						
ADMINISTRATION						
EXECUTIVE						
MANAGEMENT ENGINEERING						
ACCOUNTING						
SUPPLY						
AIRWAYS						
PERSONNEL						
MEDICAL						
SUB TOTALS						
TOTAL OPERATING EXPENSES						
TOTAL COST OF OPERATIONS						
PER CENT PERFORMANCE						
NET COST OF OPERATIONS						
NET OPERATING PROFIT						

(Exhibit A) thus provides a quantitative measure of the operational efficiency of the carrier.

In addition to the "Quarterly Report of Operations" (Exhibit A) standard cost accounting would provide detailed analyses of the variances isolated to show in which departments variances arose and the major causes of the variances . . .<sup>2</sup>

It is impracticable to include, in this brief study, the detailed procedures which would be followed in the development of Earned Hour standards or reasonable time allowances for all of the other functions in the industry. The above example deals only with one function. In all other departments, the same general approach would be used with suitable units of measurements of performance.

#### *Standard Revenue and Variance Analysis*

In addition to operating cost standards, standards of performance should also be established to measure the efficiency and economy of the various revenue producing departments, sections, routes, aircraft types, etc. Variances from standard revenue would be most helpful in planning schedules and flights, and in high-lighting those areas where corrective action or additional sales effort should be applied.

Revenue standards would be established taking into account the actual conditions under which the carrier must operate. For example, in one area, a load factor of 75% and aircraft utilization of 8.0 hours per day might be taken as standard for purposes of arriving at the budgeted passenger revenue per flight hour while, in another area, it may be necessary to take a load factor of 40% and a utilization of 5.0 hours per day. Budgeted revenue for each aircraft type would be established by budgeting anticipated passenger, cargo and air mail revenue based on realistic load factors and scheduled aircraft utilization expressing the anticipated dollar revenue per flight hour.

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## ISSUES INVOLVED IN A UNITED AND COORDINATED FEDERAL PROGRAM FOR TRANSPORTATION—ANALYSIS OF THE SAWYER TRANSPORTATION REPORT\*

**T**HE principal specific recommendations contained in the report on "Issues Involved in a United and Coordinated Federal Program for Transportation," submitted December 1, 1949 to the President of the United States by the Secretary of Commerce, Charles Sawyer, are here briefly summarized. In order that the nature of such recommendations as contained in the Sawyer report may be clearly indicated, it is necessary to note the particular circumstances under which this report was prepared and transmitted.

The report was made pursuant to a request from the President dated August 30, 1949, which referred to the need for "a unified and coordinated

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<sup>2</sup> The remaining detailed portions of the Report dealing with "variance analysis for use in main base maintenance" are omitted. Reference is made to several detailed Exhibit reports which cannot be readily reproduced.

\* Prepared by Burton N. Behling, Senior Specialist, Transportation, Legislative Reference Service, Library of Congress, for Mr. Edward R. Jelsma, Professional Member, Surface Transportation Subcommittee, U.S. Senate Committee on Interstate and Foreign Commerce.

Federal program for transportation" and "as a first step" called for "a report outlining the major policy issues which need to be resolved at this time." Secretary Sawyer in responding to this request undertook to provide "something more than . . . a list of alternatives" and outlined the issues "around a framework of policy."

The result of this approach, and of the further fact that the report was in preparation over a rather short period, is that in most respects it does not purport to give "recommendations" of a final or definite character but instead offers various tentative suggestions or conclusions as a basis for further study and consideration. Such reservations are emphasized generally at this point in lieu of repeated qualifying statements in the following references to particular proposals.

The report considers and makes suggestions regarding both "promotional" and "regulatory" activities of the Federal Government, as summarized under those headings below. Where pertinent, references also are made in this memorandum to (1) similar proposals made in other prior reports on transportation and (2) bills on the same subject matter which were introduced during the first session of the 81st Congress.

#### PROMOTIONAL ACTIVITIES

After reviewing the "bewildering array" of Federal promotional activities in the transport field (p. 45), the "major conclusion" of the report is that there is an "absence of any over-all promotional program" and that these activities "have now reached such scope as to warrant critical re-examination . . . to indicate whether the various promotional programs are in harmony and whether the Federal Government is obtaining adequate return for the expenditures it is making." (p. 46)

The report finds that conflicts, excesses and inconsistencies arise principally from these "significant facts": (p. 23)

1. In almost every case a promotional agency is responsible for providing only a single type of facility useful for only one form of transportation.
2. The promoting agencies have for the most part only very broad and general standards established for them by statute.
3. Each promotional agency has been the judge of the merits of its own promotional activities.
4. In several important cases the basic transport facilities are provided without charge, making it difficult to measure the utility of the separate programs in terms of the willingness of users to pay for the use of the facility.
5. There has been little coordination between the various facility programs, each program being carried on with little or no regard to the others.

On the basis of these findings the report advances as its major proposals that—

1. A centralized Federal agency to coordinate transport promotional (as distinguished from regulatory) activities be established, and
2. A system of user charges be imposed, where not now applicable, to cover the cost of transport facilities and aids provided from public funds.

Certain other proposals relating specifically to highways, ocean shipping and air carriers also are suggested, as noted subsequently.

#### *Proposal of a Centralized Promotional Agency*

To effectuate the proposed coordination and balancing of promotional activities, the report suggests "the grouping of all major promotional activities under unified direction and control," including therewith "the establishment of a permanent centralized research staff with a clear mandate to evaluate and appraise all of the various promotional activities . . . and make recommendations for a coherent and balanced program." It is stated that such a central agency "would be in a position to make a unified evaluation of the total needs of transportation, the total service provided, and the results of all Federal promotional and regulatory activities." The Sawyer report is silent as to where such an agency should be placed in the structure of the Federal Government. (p. 47)

Various proposals of this nature for a centralized and permanent transport agency have been made from time to time in the past. Most recently, the Hoover Commission on the Organization of the Executive Branch of the Government recommended that such a coordinated transport agency (excluding regulatory bodies) be established within the Department of Commerce.<sup>1</sup> Some of the other reports which have found a need for coordination of transport promotional activities have recommended the creation of a separate Department of Transportation at cabinet level, or of an "independent" Transport Authority to be set up on either a temporary or permanent basis.<sup>2</sup> S. 126 (81st Cong., 1st sess.) and earlier like bills reflect the recommendations made in 1944 by the defunct Board of Investigation and Research for the establishment of a Federal Transportation Authority as an "independent executive agency."

#### *Proposal on Highway Policy*

The report suggests that "more attention should be given to striking an appropriate balance between Federal, state, and local activities in the highway field." (p. 17) In this connection it is noted that the Federal Aid Highway Acts of 1944 and 1948 extended the Federal aid road systems to include not only a 40,000-mile interstate trunk system but nearly 600,000 additional miles of highway, "much of which might be considered of secondary importance from a national standpoint and primarily of concern to state and local areas." (pp. 15-18) As further evidence of the need of reconsideration, the report also points out that the "Bureau of Public Roads now favors enlarging the Federal contribution beyond 50 percent on the basic 40 thousand-mile trunkline system." (p. 16)

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<sup>1</sup> A significant exception in this report, however, is that the river and harbor development functions now performed by the Army Corps of Engineers would be consolidated with the Reclamation Service within the Department of the Interior. Commission on Organization of the Executive Branch of the Government, *Concluding Report to the Congress*, May 1949.

<sup>2</sup> See for example, the following: C. L. Dearing and W. Owen (The Brookings Institution), *National Transportation Policy*, 1949; Board of Investigation and Research, *Practices and Procedures of Governmental Control*, 1944; National Resources Planning Board, *Summary Report of Transportation and National Policy*, 1942; Reports of the Committee of Six and the Committee of Three to the President of the U.S., 1938; Third Report of the Federal Coordinator of Transportation, H. Doc. 89, 74th Cong., 1st sess., 1935; and Fourth Report of the Federal Coordinator of Transportation, H. Doc. 394, 74th Cong., 2nd Sess., 1936.

*Recommendation of User Charges for Public Facilities*

A major feature of the Sawyer report is its endorsement of a general system of user charges to pay for transportation facilities and services provided from public funds. (pp. 24, 48, 102-106, 108-109). Recognizing that transportation subsidies result in unequal competitive conditions as between different kinds of transportation, as well as in uneconomic allocation of traffic, the report concludes that "the Federal Government should undertake to study and receive the issue of assessing user charges as speedily as possible," where such charges are not now imposed or are inadequate. (p. 24)

In support of this recommendation the report also emphasizes that a general system of user charges would—

1. Provide concrete evidence of the actual value of the various aids which were being supplied, thus affording a basis for particular emphasis on such developments as transport users are willing to support and at the same time giving "the most convincing demonstration that the services and facilities provided are actually in the public interest." (pp. 24, 28)

2. Tend to place all forms of transport on a more equitable basis and make it possible for regulatory agencies and carriers to remove distortions in rate structures caused by transport subsidies. (pp. 105, 108)

The report also suggests that exceptions to the principle of user payments should be made only (1) on the basis of a clear finding by those directly concerned with the country's defense that the services to be subsidized are clearly essential from a defense standpoint and could not be obtained or maintained without Government support, in which event "such subsidies might be charged to the military budget," or (2) where the "need to accelerate the development of particular services or areas may temporarily justify the furnishing of facilities at Government expense." (pp. 24, 108)

Over a period of years similar recommendations for the general applicability of user charges have been made as a result of comprehensive investigations of the extent and effects of transport subsidies. Among these the following may be particularly noted:

1. Report of the Federal Coordinator of Transportation (Joseph B. Eastman) "Public Aids of Transportation," 1940.

2. Report prepared for the Board of Investigation and Research on "Public Aids to Domestic Transportation," transmitted to the Congress and printed as H.Doc. 159, 79th Cong., 1st sess., 1944.

3. C. L. Dearing and W. Owen (The Brookings Institution), "National Transportation Policy," 1949. Based in part on a study of federal transportation activities undertaken at the request of the Hoover Commission.

*Proposal for Eliminating Subsidy from Air-Mail Payments*

The report recommends, as a "step on which there is general agreement," that any payment of subsidies to air carriers, both domestic and overseas, should henceforth be separate from compensation for air-mail service. (pp. 34-41, 48-49) Similar recommendations that subsidies not be concealed in mail pay have been made many times by, among others, the Post Office Department, the Department of Commerce, the Federal Coordinator of

Transportation, and the Board of Investigation and Research. A somewhat different view was taken, however, in the recent report of the House Committee on Interstate and Foreign Commerce on "Public Aid to Air Transportation" (H.Rept. 1612, 80th Cong., 2nd sess., p. 5).

Two bills introduced in the first session of the 81st Congress (S. 1077 and S. 2437) would effect such a separation.

Also on the subject of air-mail payments the Sawyer report further suggests (1) amendment of the Civil Aeronautics Act to replace the "need clause" (characterized as in effect a 'cost-plus system') with "new provisions empowering the regulatory agency to establish in advance subsidies at fixed rates for a given time period for groups or classes of carriers" (p. 41) and (2) the initiation of steps to terminate subsidy assistance to air carriers "in cases where it is clear that little net contribution to commercial or national defense needs is being furnished by particular services." (p. 49)

#### *Proposals for Changes in Shipping Subsidies*

The report criticizes various aspects of the existing programs for construction differential and operating differential shipping subsidies. Recognizing that "some form of operating subsidy is necessary if most American shipping companies are to remain in existence in competition with lower cost foreign operators," (p. 32) the report suggests that the "trade route concept" for subsidy payments be abandoned as unduly preferential to certain carriers and that a possible alternative would be "a system of subsidies to all American shipping companies operating in the foreign trade with the subsidy computed on the basis of a certain percentage of the labor costs of the shipping lines." (pp. 32, 48)

The report also calls attention to the need for more definite standards to govern administration of the construction differential subsidy program, particularly as to "what is to be included in national defense features to be paid for entirely by the Government." (p. 29)

#### REGULATORY ACTIVITIES

Tentative suggestions in the report regarding regulatory activities affecting transportation appear to have been less fully considered than those pertaining to promotional activities discussed above. This is indicated by various notations to the effect that no intensive examination of the subjects discussed was possible in connection with the preparation of the report, and that "careful studies" would be needed as a basis for sound conclusions.

It may be well, nevertheless, to note briefly some of the more significant subjects touched upon in the report and the provisional comments regarding them. Such matters pertaining to regulation include the following:

1. Referring to the advantages which might accrue from the consolidation of all regulatory functions under unified control, the report observes that "it is probable that a consolidation of regulatory controls will eventually be necessary." But doubts are indicated as to whether "at this time" the advantages of such action would "outweigh the special considerations which led to the establishment of separate regulatory authorities for shipping and air transportation." (pp. 100-101)

2. With reference to the Reed-Bulwinkle Act (Public Law 662, 80th Cong.) the Sawyer report suggests its repeal "unless effective and continuous supervision of [carrier rate] conferences is maintained by

the regulatory agencies and unless more specific standards for prescribing rates are developed than at present." (p. 88) Bills (H.R. 2167 and H.R. 5536) were introduced in the 81st Congress, 1st session, to effect such repeal of exemption from the anti-trust laws.

3. Regarding the regulation of security issues and related financial matters, the report suggests that "carriers receiving financial assistance from the Federal Government should have effective controls over their financial practices because in their absence the Federal Government is likely to have to pay the price of financial difficulties of private carriers." (p. 91) This proposal would have reference particularly to the establishment of financial regulation over air carriers and ocean shipping operators.

4. On through routes and joint rates, the report suggests that "a more effective utilization of the different forms of regulated transportation might result if greater use were made of joint rates, routes, and facilities." (p. 71) Bills relating to the matter introduced in the first session of the 81st Congress were S. 2826 (motor carriers) and S. 792 and H.R. 2138 (through routes by mail).

5. On railroad consolidation, it is proposed that efforts be made to promote or require consolidations and unifications. It is also suggested that "immediate consideration" be given to "a more liberal policy" with respect to abandonments of unprofitable facilities and services which can be furnished by other types of carriers. (pp. 94-95) In this connection reference is made to the possible relinquishment by the railroads of small shipments (express and small amounts of l.c.l. freight) and that methods of payment for railroad carriage of mail be reconsidered so as to facilitate movement of the mails by the most efficient means. (pp. 95-96)

6. The report also contains rather extended references to rate structures, with considerable emphasis and approval given to the proposition that all transport rates should be closely adjusted to the "fully distributed costs" of each carrier and type of carriers (pp. 69-70, 108) But the report also stresses in various places the desirability of more unrestrained competition in transportation. It seems to be overlooked that less and not more competition between carriers would be the result if rates were to be fixed in accordance with some rigid system of "fully distributed costs."