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PASSENGER FARE POLICIES OF THE
CIVIL AERONAUTICS BOARD

By Lucile Sheppard Keyes

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It is only in the relatively recent past that problems of airline commercial rate policy have been accorded much attention by the Civil Aeronautics Board or, indeed, by the managements of the air carriers themselves. Although the Civil Aeronautics Act contains provisions for the regulation of commercial rates which are substantially similar to those applicable to surface carriers under the Interstate Commerce Act, the direct regulatory attainment of reasonable and non-discriminatory commercial rates was not conceived to be one of the primary tasks of the Civil Aeronautics Board, nor did this issue assume any great significance in the period immediately following the enactment of the law.¹

This situation reflected in part the absence of independent rate initiative, on the part of individual carriers, of a type which would have posed for the Civil Aeronautics Board the problem of how to deal with the resulting repercussions on the revenues of competitors. Given the availability of mail revenues adequate to support its operations, there was no compelling pressure on any mail carrier to take the obvious risks of competitive retaliation and/or regulatory stricture involved in any significant departure from an established level of either rates or service.² The origination of such innovations by “newcomers” to the industry was effectively prevented until the post-war period by administrative control of entry. The substantial removal of the threat of new competition by this means no doubt added to the tendency toward preservation of the status quo on the part of existing carriers. In such a situation, it is hardly to be wondered at that neither Board nor carriers developed adequate cost data by which the appropriateness

¹ Two relatively early cases in which the issue of discriminatory commercial rates was dealt with by the Board are discussed below.

² Cf. Jones and Davis, “THE ‘AIR COACH’ EXPERIMENT AND NATIONAL AIR TRANSPORT POLICY,” Part I, 17 J. AIR L. & COM. 1, 3 (1950): “During the early years of the Civil Aeronautics Act it was generally agreed by the operators that special personal services such as stewardesses, free meals, extra-comfortable seats, and limousine service to and from airports were necessary to help overcome the reluctance of the general public to fly, and during this period of general expansion and growth there were no significant pressures for the development of a more Spartan type of service at lower fares.”
of particular commercial rates or the profitability of particular commercial services might be judged.\(^3\)

Until the later part of 1948, Board action with respect to commercial rates was largely concerned with overall rate levels as reflected in the magnitude of certificated air carrier earnings. A major exception was the Board's intervention in the air cargo field, where a floor was placed under air freight rates as a result of protests by noncertificated cargo carriers who were in real danger of being driven out of business by their certificated competitors. It is significant that this intervention to curb rate reduction was a result of competition initiated by "newcomers" in the air transport industry; however, the main issue presented (protection of the existence of the cargo carriers) and the rate standard adopted by the Board were essentially different from those in the passenger rate cases to be discussed here.\(^4\) Regardless of the economic merits of the reasoning in this decision, it is evident that the very existence of the all-cargo carriers provided the Board with relevant cost data which did not involve it in the complex problem of the proper distribution of overhead among various classes of traffic.

In March, 1943, as a result of the very high wartime level of airline earnings, the Board issued a show-cause order to eleven certificated

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\(^3\) In a detailed survey of airline commercial rate policy, Messrs. Gill and Bates have emphasized the fact that until recently very little attention was given to cost factors in setting airline commercial rates. This inattention is attributed to two factors: "First, neither the airlines nor the Civil Aeronautics Board knew accurately the actual costs of rendering the various kinds of airline services, either as to passengers or type of commodity carried, or as to route, segment, or station operated. ... Second, in many cases there appeared to be little need for the airlines to know their costs accurately for this purpose because they would not be able to use this criterion in setting specific rates anyway, inasmuch as this would make many fares prohibitively high from the standpoint of rail competition." Frederick W. Gill and Gilbert L. Bates, *Airline Competition* (Boston, Harvard Graduate School of Business Adm., 1949), p. 419.

The first of these factors would seem to be a result rather than a cause of the inattention to cost considerations which it is adduced to explain. The second offers at best only a partial explanation for this phenomenon. In the first place the success of the Ludington experiment tends to confirm the view that costs would have permitted profitable "coach-type" operation in competition with rail carriers on high-density routes quite early in the game, even without mail traffic (see Jones and Davis, *op. cit.*, p. 1). In the second place, even in those cases where rail fares may have set an effective ceiling on airline rates on existing routes lower than the costs which could have been avoided if commercial air service had not been offered, a knowledge of this fact would have been required as a guide for the minimization of loss on such service. One can only conclude that airline managements were not greatly concerned with the magnitude or distribution of commercial profits and losses; and this is not surprising in view of the fact that the success or failure of their enterprises did not depend on the achievement of any nice adjustment of rates and services to commercial demand and cost conditions.

\(^4\) The decision in the *Air Freight Rate Investigation* case was made on April 21, 1948 (Orders Serial No. E-1415). The standard referred to by the Board in determining the prescribed minimum was the average revenue ton-mile cost incurred by the threatened class of carriers in 1947. The use of this cost figure as a basis for a general minimum rate floor is defended on the ground that it represents "a practical minimum for the costs of an all-cargo service" and a reasonable approximation to attainable cost levels for cargo service by all types of carrier when the volume of air freight shall have reached full development. This line of reasoning enabled the Board to reject the "no-cost" and "marginal cost" standards advocated by the certificated carriers without committing itself to the "fully-allocated cost" concept advocated by the noncertificated carriers.
carriers envisaging a 10 percent overall reduction in passenger fares. The effect of these orders on the geographical rate structure was substantial; however the major purpose of the Board was related to the level rather than the structure of commercial rates.\(^5\) Similarly, the subsequent additional fare reductions undertaken in 1945 by the carriers—which were at least in part a result of the initiation of Board action designed to effect a drastic decrease in mail rates—were “across-the-board” affairs,\(^6\) as were the rate increases of 1947 (initiated by the carriers as a result of heavy losses),\(^7\) and the Board-sponsored general increases of late 1948.\(^8\)

By this time, the financial pressures resulting from the economic reverses of the airlines in the postwar period (when, contrary to the condition which had prevailed in the past, predetermined mail rates proved wholly inadequate to make up the difference between commercial revenues and total costs) and the example of the “air coach” operations of noncertificated newcomers (who had entered the sacred precincts through a legal loophole) had focused the attention of Board and carriers on the possibility of increasing net earnings by some rate actions more complicated than the mere manipulation upward of the fare level.\(^9\) Thus at the August, 1948, rate conference the Board not only counselled a 10 per cent general increase in the regular fare level,

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\(^5\) Gill and Bates, op. cit., pp. 450-451; “This [show-cause] order did not bring about the over-all blanket 10% reduction in the then existing air fares which was originally contemplated. It resulted, rather, in many and varied compromises, some of which ironed out disparities in the existing fares. . . . For instance, the Big Four . . . adopted a system-wide uniform base rate of 5.5 cents per passenger mile. These carriers were impelled to overhaul their entire tariff structure in order to bring their various rates into line with this 5.5 cents base rate.

\(^6\) Ibid., pp. 410-411: “On January 2, 1945 . . . another series of orders was issued by the Civil Aeronautics Board to the four largest domestic carriers, referring to their high profits and heavy traffic, and requiring that they show cause why an adjustment should not be made in their mail rates from the then existing level of 60 cents per ton mile to one of 32 cents per ton mile. These orders resulted in many counter fare proposals by the Big Four and other carriers not so affected, probably in anticipation of similar orders . . . the pressure of the CAB orders was not the sole reason for the adoption of these fare reductions. The managements of some of the carriers sincerely felt that they were necessary in order for them to enter the mass transportation market, and they had been leaning in that direction for some time . . . the result of these orders was that passenger fares and mail rates were reduced to a common level at 45 cents per ton mile for the Big Four. This meant that a compromise had been reached whereby passenger rates were reduced approximately 16% (5.5 cents per mile to 4.6 cents per mile).”

\(^7\) Ibid., pp. 411-412.

\(^8\) Ibid., pp. 412-413.

\(^9\) Speaking on April 19, 1950, Board Chairman O’Connell described this development as follows (Mimeographed copy of speech made before the American Association of Airport Executives. Columbus, Ohio, pp. 2-4): “The last year and a half have already witnessed some notable changes in airline pricing and an awakening of price consciousness on the part of the industry, the public, and I might add, the Board. After the war and down to late 1948, airline pricing was basically simple . . . although the fare level moved down, and then up, several
but indicated that it would look with favor upon a cautious experiment with promotional fares.\(^{10}\)

The present article deals with regulatory policies and problems which have arisen in connection with this new “price consciousness.” The first part of the discussion falls naturally into three sections: (1) the air coach experiment, (2) promotional fares other than air coach initiated by the carriers, and (3) rate policies suggested by the Board. It will here be brought out that a solution of the problem of the determination of legitimate mail payments—i.e., those payments which can be regarded as compensation for mail carriage rather than “subsidy”—is basic to a proper program of commercial rate regulation. The second part of this study will be devoted to a consideration of this problem.

**THE AIR COACH EXPERIMENT**

This phase of commercial rate policy has been comprehensively treated in a series of two articles in this JOURNAL by Messrs. Harold A. Jones and Frederick Davis. The discussion here will be limited to pointing out the main objectives of regulatory action in this field and some problems of economic policy which may arise in the future.

First of all, it appears that the ultimate objective of past regulation has been to insure so far as possible that the coach-type services should increase rather than reduce carrier net revenues. To this end, the Board established certain requirements designed to insure not only that the unit costs of such services should be lower than average, but that there should be as little diversion of traffic as possible from the regular-fare services; it has also acted to keep coach fares from being initiated or continued at a level regarded as unprofitably low.\(^{11}\) Both of the first two of these aims were served by the requirements for off-times in the postwar period it moved within the same simple framework and without much thought of pricing as a promotional or regulatory instrument.

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“In the history of this growing price consciousness August 19, 1948 is an important date. On that day the Board called a meeting of the domestic trunk-lines to discuss fare problems. The airline financial picture at the time was bleak...”

“There were perhaps several reasons for the timing of this renewed interest in the price tag which is put on air transportation. Perhaps one factor was the success of air coach services which the large irregular carriers had been operating over certain high-density, long-haul segments, notably transcontinental, at materially reduced fares and with unusually high passenger loads.”

This conference thus did not result in a general 10 percent fare increase. Gill and Bates (loc. cit.) have described the result as follows: “Following the conference, there was considerable confusion. Most carriers filed intentions to raise fares 10% effective in September. Several also filed tariffs which included round-trip and other discounts. When these increases in fares went into effect, together with the discounts which accompanied them, what started out to be a 10% fare increase actually turned out to be considerably less than 10%. The president of one major airline estimated it to be an increase of no more than 2%.”

On September 27, 1950, the Board imposed a general 4½ cent minimum (with certain minor exceptions) for coach fares to become effective on November 16. The prevailing coach rate at the time of the Board’s action was about 4 cents a mile. At the same time, the effective period of the Board’s tentative sanction
peak scheduling, elimination of "non-essential" passenger services, and use of high-density equipment, and the first was further implemented by the limitation of coach service to high-traffic routes. It is, of course, possible to question the wisdom of this particular approach to the air coach proposals on its own ground — that is, to argue that the restrictions insisted upon by the Board were in some respects or in some markets defective as a means of maximizing profits. For example, there may be in many cases a conflict between the achievement of high load factors on the coach services and the minimization of diversion from regular-fare service: in excluding from coach travel a relatively large part of the high-fare traffic by such means as the "off-peak" scheduling requirement, one may also exclude new traffic which might fill up coach planes in the daytime but would not be diverted from surface transport agencies by extremely inconvenient (though low-cost) air schedules, and it might be that the profit from this new traffic would be sufficient to offset the presumable loss from increased diversion. But given the assumption that no decrease in the regular fare level could fail to reduce profits on any given route, the Board's concern with the insulation of this market from diversion to lower-fare services seems reasonably justified. Experimentation with more liberal schemes of division of the market might have resulted in a complete breakdown of the division itself.

The Board's recent sanction of low-fare services in the transcontinental market without the most important limitation previously imposed shows a recognition that the above assumption may not now hold good on all routes. Compelling evidence was adduced to show that such services could be expected to be as profitable as high-rate services on the same run, the diversion of traffic thus being rendered of no concern. Although no change is thus involved in the main principle governing the Board's action, it has been recognized that making the coach fare the regular fare on certain runs may give rise

[1] The Board's view has apparently been that at least as a general rule the lowering of the regular fare level would decrease profits. For example, in the above-cited speech, Mr. O'Connell said (p. 7): "This industry is not yet ready for rate reductions on an across-the-board basis. Despite increased traffic, it still needs a general fare level between 5½ and 6¢ a passenger mile. We are not ready financially and we are not ready cost-wise and we are not ready subsidy-wise for a 4¢ domestic airline system. To make broad and deep fare cuts would inevitably at the present time invite either financial disaster or else enormously increased subsidization. In the immediate future, therefore, a continuation of promotional pricing on a restricted and highly selective basis seems to make sense."

to difficult regulatory problems, or at any rate may force the Board to consider carefully the problem of geographical rate relationships.

Reflection of Varying Costs in Geographical Rate Structure

As Messrs. Jones and Davis have suggested, a charge of unfair treatment may be made by users of low-density routes on which higher rates are charged and their complaints may be reinforced by the argument that as taxpayers — and therefore supporters of the airlines — they are entitled to travel at coach fares "as a matter of right." Leaving the latter point aside for the moment, there seems to be little reason to suppose that a differential rate policy reflecting varying unit costs on high and low density routes could be successfully attacked on legal grounds, provided that the differentials were uniformly applied.

While it is true that uniformity in per mile railroad passenger fares over broad areas, embracing different carriers and routes of widely varying transportation characteristics, has been permitted by the Interstate Commerce Commission, it is also true (1) that this type of rate structure has been a result of carrier rather than regulatory initiative; (2) that variations from such uniformity by individual carriers, both with respect to their entire systems and with respect to certain lines only, have been permitted; (3) that variations from uniformity as between regions have been permitted; and, perhaps most signifi-

14 Ibid., pp. 16-17.

15 On the importance of carrier action in shaping the rail passenger rate structure, and the general policy of non-interference followed by the I.C.C. with respect to passenger fares, see Kent T. Healy, The Economics of Transportation in America (Copyright, 1940, by the Ronald Press Company, New York), especially p. 507: "All told then, except for the rather spectacular action of the Commission in actual control of coach fares in the East, the extent of regulatory control of passenger fares has been almost negligible."

The "rather spectacular action" referred to here is the Commission's imposition in 1936 of a uniform maximum for basic regular passenger fares all over the country of 2 cents per passenger mile in coaches and 3 cents per passenger mile in Pullmans. The practical effect of this order was to bring down the fares in the East to a level uniform with (or only slightly higher than) those then prevailing in other areas. Significantly enough, this action was explained primarily by the argument that, in view of the experience of carriers in other regions, the Eastern roads would be better off financially with the prescribed fare level than with the higher existing fares. Passenger Fares and Surcharges, 214 I.C.C. 174, 222-223 (1936). In addition, the Commission pointed out (p. 234) that no valid argument based on transportation considerations was adduced by the Eastern carriers in support of a higher fare level.

The establishment of substantial nationwide uniformity in rail passenger rates at the time of the first World War, and subsequent departures from it, were neither engineered nor interfered with by the I.C.C. (There is a brief description of this development in the above-cited decision, pp. 186-188).

16 See, for example, Increased Passenger Fares, New Haven Railroad, 268 I.C.C. 303 (1947).

17 See, for example, the situation described in 214 I.C.C. 174, 187-188: "Prior to 1933, despite increased losses in passenger traffic and mounting deficits therefrom, little experimentation with the basic fare of 3.6 cents, except as will later appear, was attempted by respondents. . . . Commencing in 1927, various southern and western respondents began to experiment with reduced basic fares. . . . Commencing in 1931, the Boston and Maine Railroad, and in 1932 the Boston and Albany Railroad, in order to meet highway competition, established reduced round-trip one-day fares between certain stations on their respective lines, and
cantly, (4) that variations from uniformity have been permitted for the express purpose of reflecting higher unit costs on certain lines (the low density of their traffic being recognized as a pertinent cost factor) even where the Commission has intervened to prevent an intra-regional differentiation in the fare level not related to transportation considerations. It should be emphasized that the Commission has not held that nationwide or regionwide uniformity in fare levels was in itself the desideratum, but (1) that rate differentials should be justified by varying transportation conditions and (2) by implication, that such differentials should be applied uniformly if at all. Thus the Commission permitted the continuation in the Mountain-Pacific States of fares on branches and secondary lines of the defendant railroads which were much higher than fare rates found unreasonable and unduly prejudicial for main line travel, the decision taking note of the fact that this type of differential amounted to general practice among

in 1932 the New Haven established reduced fares between New York, N.Y., and Providence, R.I., and Boston, Mass. All of these New England reduced fares were canceled on or before September 27, 1934. On December 1, 1933, the southern respondents, with certain exceptions, eliminated the surcharge, and established reduced basic fares of 1.5 cents in coaches, and 3 cents one way, 2.5 cents round-trip limited to 30 days, later extended to 6 months, and 2 cents round-trip limited to 15 days, in pullmans. On the same date the western respondents generally likewise eliminated the surcharge and reduced their basic fare to 2 cents in coaches and 3 cents one way, 2.5 cents round-trip limited to 6 months, and 2 cents round-trip limited to 10 days, in pullmans. The Illinois Central Railroad Company, Chicago and Eastern Illinois Railway Company, Alton Railroad Company, and Wabash Railway Company at and west of Danville, Ill., . . . became parties to the western arrangement, and the first-mentioned respondent applied the experimental fares of the western lines over its entire system, a portion of which is in the southern district, except where necessary to meet the lower 1.5-cent coach fare of other lines in the South. The eastern carriers, with some exceptions, have met the reduced fares at border points and on traffic competitive with that moving on the reduced fares. On February 1, 1934, the Norfolk and Western Railway Company . . . reduced its one-way fares to 3 cents in pullmans and 2 cents in coaches, and this reduction was met by the Chesapeake and Ohio Railway Company . . . between the more important competitive points. Except as just indicated, in the eastern district the basic-fare structure has remained intact."

Arizona Corporation Commission et al. v. Arizona Eastern Railroad Company et al., 85 I.C.C. 76 (1923). Such a differentiation was ordered eliminated by the I.C.C. in 1923, when it acted to bring the basic passenger fare level between main line points in the States of Arizona, New Mexico and Nevada (then 4.8 cents) down to that prevailing elsewhere, including States with similar transportation characteristics (3.6 cents). The higher rates were found unreasonably and unduly prejudicial because not justified by differences in transportation factors.

85 I.C.C. 76, 92: "The evidence shows clearly that, based upon operating conditions [such as steep grades, hard water and weather conditions] and density of traffic, the States of Arizona, Nevada, and New Mexico are entitled to main-line passenger fares not higher relatively than those which prevail in other States of the mountain-Pacific group. Operating conditions, population, and density of traffic vary greatly in different parts of the United States. Nevertheless, the basic interstate passenger fare generally applicable to and from points in all States except those complaining is 3.6 cents per mile. With the exception of these States, there is no State in the Union to and from which passenger fares are established on a basis uniformly and arbitrarily higher than 3.6 cents per mile, without regard to the circumstances and conditions obtaining in different sections thereof."
the railroads.\textsuperscript{20} The higher branch line rates were specifically excluded from the application of the general rate ceiling applied in 1936.\textsuperscript{21}

The Commission's general policy of sanctioning departures from strict distance relationships in freight rates where such departure is warranted by such cost-affecting factors as density of traffic and length of haul\textsuperscript{22} would also tend to support a similar policy with respect to passenger fares by the Civil Aeronautics Board.\textsuperscript{23} Even some potentially troublesome statements indicating a Commission construction

\textsuperscript{20} Ibid.: "The evidence shows that passenger fares on branch lines of many carriers other than defendants, in the mountain-Pacific group and in the United States generally, are on a higher basis than 3.6 cents. These branch-line rates vary from 4 to 9.6 cents per mile."

This decision was later modified to permit (among other things) the Denver and Rio Grande Western to maintain higher rates on its main line than the 3.6 cents generally prescribed, primarily because of the road's extraordinarily difficult operating conditions. 88 I.C.C. 90, 91-2 (1924).

\textsuperscript{21} See note 15, above. Further precedent for differential charging for low-density passenger services can be found in The Commutation Rate Case, 27 I.C.C. 549, 552 (1913): "The commutation traffic of the New Haven is very materially more dense than on the Pennsylvania. Giving due consideration to this and other facts shown of record, we think that the New Haven schedule of fares for this service may properly be somewhat lower than that of the Pennsylvania . . . ."

\textsuperscript{22} Only a few examples can be cited here. Speaking of the class rate structures prescribed by the Commission since 1925, Dr. Locklin has said: "The structures are in general conformance with the distance principle, and distance scales of first-class rates have been generally prescribed by the Commission. The scales are constructed upon the 'tapering principle,' that is, the rates increase with distance but at a decreasing rate, thus resulting in lower rates per mile for the longer distances . . . . The rate scales are uniform for large areas, although not necessarily for the whole area covered by the investigation. [For example] In Eastern Class Rate Investigation two scales were provided for New England: A zone A scale for southern New England, and a zone B scale, 10 percent higher, for northern New England. . . . The differences in scales are usually for the purpose of reflecting differing operating costs due to variations in operating conditions or in traffic density. Even where a uniform basic scale is prescribed for a whole territory, exceptions are commonly allowed which take the form of 'arbitraries' for distances on branch lines, or on short and weak lines." (Italics supplied.) D. P. Locklin "Rates and Rate Structure," Transportation and National Policy (Washington, U.S.G.P.O., 1942) p. 89.

\textsuperscript{23} On the general question of Commission treatment of distance relationships in connection with Sections 1 and 3 of the Interstate Commerce Act, Professor Sharfman has written: "... both in . . . determinations as to reasonableness and in situations under section 3, where rate relationships are themselves specifically at issue, distance has not provided an adequate criterion of cost in the comparison of hauls, since wide differences prevail both in topographical conditions and in other circumstances which produce inequalities in construction and operating costs over related routes. Such factors as these, together with the effect of different traffic densities upon unit costs of carriage, have been recognized by the Commission in numerous instances as constituting significant elements in the cost of service and as properly qualifying the influence of the distance factor." I. L. Sharfman, The Interstate Commerce Commission (New York, The Commonwealth Fund, 1936), Part III, Volume B, pp. 569-570.

It should be observed, however, that the Commission and the Supreme Court have held that a given rate cannot be held confiscatory merely because it does not yield a profit from every operation to which it applies. Thus, in St. Louis and San Francisco Ry. Co. v. Gill, 156 U.S. 649 (1895) at pp. 665-666, the Supreme Court held that the carrier "cannot claim the right to earn a net profit from every mile, section, or other part into which the road might be divided, nor attack as unjust a regulation which fixed a rate at which some such part would be unremunerative." This view seems to be an eminently practical one, for under a contrary doctrine the task of the regulators in setting reasonable rates would be hopelessly complicated. The general desirability of a rate structure in conformity with relative costs must in practice be weighed against the necessity of setting rates which apply to more than one mile of line and more than one shipment of any commodity.
of the long-and-short-haul clause which might preclude full recognition of cost differences where this would lead to a higher rate for a shorter haul on the same route in the same direction need not concern the Board should such a situation arise in the airline field, since the Civil Aeronautics Act has no such clause. All in all, therefore, it seems unlikely that the Board could be successfully challenged by an appeal to regulatory precedent in a policy, uniformly applied, of fare differentials roughly reflecting cost differences; no difficulty from this source need be anticipated if it is decided in this manner to abandon the so-called “traditional single-level fare structure.”

The possibility that the subsidized nature of the industry might result in demands for universal low-rate services regardless of their profitability cannot be easily dismissed. Such a possibility will remain to plague both Board and carriers as long as the latter are entitled by law to a subsidy which is not clearly related to a specific national objective, and hence can be represented as a “Government dole.” Where the nature of the “value received” in return for Government support is not clear, John Doe, taxpayer, may with some justice believe that the “value received” should be a personal benefit to him or a bounty to his community.

Incidence of Support for High Cost Operations

As long as the Board continues to permit only those coach services which add to, or do not reduce, profits on operations between the points to which they apply, the second major problem suggested by Messrs. Jones and Davis—i.e., a possible shift in the incidence of the support of the less profitable services—will not arise. However, even

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25 Jones and Davis, op. cit., p. 20. It seems doubtful that the single-level fare structure referred to is of sufficient age or universality to be called "traditional." On this point, see Gill and Bates, op. cit., passim; the following passages will indicate the general nature of the relevant material: p. 398: "Before 1943 variable base rates were almost universally used among the domestic airlines." p. 443: "The period in airline fare history before 1943 can best be characterized as one in which there was little evidence of a uniform level of air fares from carrier to carrier." pp. 462-463: "It should not be inferred . . . that in the period after 1943 uniform base rates had been adopted by most of the carriers throughout their systems. What had happened was that a few of the carriers were using such a uniform base rate, but that many others had adopted a variable base rate; . . . since in most cases the competitive segments accounted for a major portion of carriers' revenues, or passenger miles, and since the base rate adopted in such markets was that of the original carrier, the passenger revenues per passenger mile of most of the air carriers became more and more comparable, as the extent of airline competition increased."
26 Jones and Davis, op. cit., p. 19: "... the drive for high load factors in high-density equipment, particularly in fast modern aircraft such as the DC-6 and Constellation, is almost certain to involve a considerable amount of diversion from regular fare services. If so, it may mean that by diverting a high proportion of the carriers' long-haul business (coach operations must of necessity be conducted over fairly long-haul segments) the more profitable portion of the regular business would be eliminated, without any proportional increase in net revenues. The overall system net revenues might thus be reduced, even though the promotional coach service were successful, since the bulk of the carriers' profitable long-haul
under these circumstances it is quite possible that the question of principle involved here may be raised by some spokesman for consumers of transport services on the high-density segments: that is, the question whether fares which actually reduce net profit on high density routes should not be permitted, where justified by particular costs on this route, even though the reduction in system profitability would make it impossible to support certain high-cost services previously offered. Such a situation would imply that the latter services had been genuinely dependent upon — i.e., subsidized by — profits from high-density routes in the past, in other words, that the rates on these routes could have been lower all along had it not been for the necessity of supporting the high-cost services. The problem here is not a shift in rate relationships because of the appearance of a new cost pattern, but a shift to provide a closer conformity to the cost pattern.\(^{27}\)

It appears that conformity to regulatory precedent would not require the continuation of support for such intrinsically unprofitable services, unless, at the very least, a clear showing of actual hardship to arise from the cessation of such support and/or of a real prospect of self-support for these services in the relatively near future could be made. Any regulatory requirement that one part of a carrier's traffic be burdened in order to support service to another part has been in principle condemned by the courts on various occasions.\(^{28}\) More specific support for the above view with respect to relationships between low-cost service would be performed at a lowered rate, without a corresponding increase in the standard rates for the high-cost traffic between smaller points, the losses on which are presently offset by a profit from the low-cost heavy traffic between major points."\(^{27}\)

\(^{27}\) The possible future emergence of such problems may have been foreseen by Chairman O'Connell in the above-cited speech, p. 8, where he lists among the "general criteria and objectives of a sound long-range fare policy" the following item: "A close relationship between the level and structure of fares and the cost to the carriers of performing various types of services so that the various classes and types of traffic each bears as nearly as possible its fair share of costs."\(^{28}\)

\(^{28}\) The following quotations are illustrative (the second seems especially pertinent here): *Norfolk and Western Ry. Co. v. West Virginia*, 236 U.S. 605, 609 (1915): "... it would not be contended that the State might require passengers to be carried for nothing, or that it could justify such action by placing upon the shippers of goods the burden of excessive charges in order to supply an adequate return for the carrier's entire service. And, on the same principle, it would also appear to be outside the field of reasonable adjustment that the State should demand the carriage of passengers at a rate so low that it would not defray the cost of their transportation, when the entire traffic under the date was considered, or would provide only a nominal reward in addition to cost."

*Northern Pacific Ry. Co. v. State of North Dakota*, 236 U.S. 585, 598 (1915): "In substance, the argument is that the rate was imposed to aid in the development of a local industry and thus to confer a benefit upon the people of the State. The importance to the community of its deposits of lignite coal, the infancy of the industry, and the advantages to be gained by increasing the consumption of this coal and making the community less dependent upon fuel supplies imported into the State, are emphasized. But while local interests serve as a motive for enforcing reasonable rates, it would be a very different matter to say that the State may compel the carrier to maintain a rate upon a particular commodity that is less than reasonable, in order to build up a local enterprise. That would be to go outside the carrier's undertaking, and outside the field of reasonable supervision of the conduct of its business, and would be equivalent to an appropriation of the property to public uses upon terms to which the carrier had in no way agreed. It does not aid the
routes is provided by the principles which have governed I.C.C. regulation of railroad abandonments.

As is well known, the leading judicial pronouncements on the abandonment question, while unequivocally ruling out regulatory action to require the maintenance in operation of an entire system which is being operated at a loss, leave open some degree of regulatory discretion for the recognition of local user interests when the entity to be abandoned is only a part of a system, even though demonstrably a losing proposition. Despite the variability of the statements of the Commission on the general position taken by it on the abandonment of parts of a system, it can be said with certainty that it has not interpreted the statute as requiring it to force the maintenance of unprofitable lines desired by local interests merely because the system as a whole is in a position to support them. In his recent comprehensive study of the regulation of abandonments, Dr. Cherington has noted that the mere fact that the system is prosperous is not enough in itself to rebut the applicant's showing of loss on a particular segment: "The strongest systems have been permitted to abandon lines despite the most vigorous protests." Furthermore, Dr. Cherington has found that

argument to urge that the State may permit the carrier to make good its loss by charges for other transportation. If other rates are exorbitant, they may be reduced. Certainly, it could not be said that the carrier may be required to charge excessive rates to some in order that others might be served at a rate unreasonably low. That would be but arbitrary action. We cannot reach the conclusion that the rate in question is to be supported upon the ground of public policy if, upon the facts found, it should be deemed to be less than reasonable." (Emphasis supplied.)

With respect to an entire system, the Supreme Court has said: "The company, although devoting its property to the use of the public, does not do so irrevocably or absolutely, but on condition that the public shall supply sufficient traffic on a reasonable rate basis to yield a fair return. And if at any time it develops with reasonable certainty that future operation must be at a loss, the company may discontinue operation . . . To compel it to go on at a loss . . . would be to take its property without the just compensation which is a part of due process of law." Railroad Commission of Texas v. Eastern Texas R.R. Co., 264 U.S. 78, 85 (1924).

With respect to a part of a system, the Court has said: "... the question is whether abandonment may justly be permitted, in view of the fact that it would subject the communities directly affected to serious injury while continued operation would impose a relatively light burden upon a prosperous carrier . . . the determination is made upon a balancing of the respective interests . . . In that balancing, the fact of demonstrated prejudice to interstate commerce and the absence of earnings adequate to afford reasonable compensation are, of course, relevant and may often be controlling." State of Colorado v. U.S., 271 U.S. 153, 169 (1926).

Charles R. Cherington, The Regulation of Railroad Abandonments (Cambridge, Harvard University Press, 1948), p. 128. In this connection, Dr. Cherington cites the following statement in Long Island Railroad Company Abandonment, 166 I.C.C. 671 (1930) at p. 677: "It is true that even though we add to the applicant's transportation losses from operation of the branch the capital charge which would be imposed upon it by the proposed grade-crossing elimination, the amount involved is relatively small when compared to the financial resources and transactions of the Pennsylvania system. Nevertheless it must be recognized that the conservation of the resources of any railroad system requires cognizance of items even less substantial than those here involved. Any unnecessary burden upon the transportation system of the country is an unreasonable burden. While it is true that loss from operation of a portion of a railroad system will not in every case justify the abandonment of such operation, it is also true that circumstances may justify the abandonment of an unprofitable line notwithstanding the prosperity of the system as a whole. The circumstances of each case must govern its disposition."
the contrary view, though adopted at times by at least one individual Commissioner,\textsuperscript{31} has been consistently rejected by the majority of the Commission, which has expressly refused to construe the statutory provision regarding public convenience and necessity as meaning that a service must be maintained as long as anybody needs it. The Commission has said that such a construction would call into question the constitutionality of the statute, and has moreover adopted the view that the fact that a service is operated at a loss is pertinent evidence that the public convenience and necessity do not require its continuation.\textsuperscript{32} It is significant here that “the vast majority of the contested applications are granted”;\textsuperscript{33} that in a great many instances where such applications were initially denied the Commission indicated that its decision could be reversed should the line not develop more traffic in the future;\textsuperscript{34} and that denials have in fact frequently been reversed when the situation failed to improve.\textsuperscript{35}

Indeed, there is weighty support in the record for the view that unprofitable lines will not be ordered continued in operation unless there is strong evidence that they will cease to be unprofitable in a relatively short time; at any rate, the balancing of carrier loss against loss to local interests does not generally result in a requirement that unprofitable lines be continued in operation, regardless of the relative magnitudes of such losses.\textsuperscript{36} It is only because of Court pronounce-

\textsuperscript{31} This contrary view was expressed by Commissioner McChord as follows: (Atlanta and St. Andrews Bay Ry. Co. Abandonment, 71 I.C.C. 784, 793 (1922): “Except in so far as it may be supported by the sovereign State, which is not subject to coercion, a highway once dedicated to the public use may not be abandoned without regard to the public interest in it. A common carrier by railroad, which does not enjoy the sovereign’s immunity but does exercise a delegated sovereign right of eminent domain, may not abandon the highway it creates, if by appropriate means it can maintain it, so long as the public convenience and necessity remain to be served. He whose property is appropriated, even by his gift, for use in constructing such a highway cannot thereafter interfere with the public use, and a corresponding obligation to the public rests upon the carrier. The duty to the public includes the duty to exhaust every lawful expedient to maintain the highway in such condition as to meet the public convenience and necessity. Only when it is beyond the carrier’s power, or when the public interest ceases, does the duty cease.”\textsuperscript{32}

\textsuperscript{32} Cherington, op. cit., pp. 130-131.

\textsuperscript{33} Ibid., p. 133.

\textsuperscript{34} Healy, op. cit., p. 528: “1,085 applications for abandonment had been granted up to July 1936 and only 49 denied. Some 17,000 miles were certified for abandonment and less than 1,000 miles were ordered to be kept in operation. Even in the latter cases future abandonment was not precluded, the Commission merely requiring that further study of the problem be made in the hope that additional traffic would be found so that abandonment would not be necessary.”

\textsuperscript{35} Cherington, op. cit., p. 180: “Of the forty applications which were denied prior to 1930, twenty-two had been renewed and subsequently granted by the end of 1941 . . . in the second decade (1930-1941) . . . Sixteen of the forty-three segments for which permission was first denied were subsequently abandoned with Commission authority.”

\textsuperscript{36} The following statements by Dr. Cherington (op. cit., pp. 133-134) which are fully supported by many references to Commission decisions, are significant here: “It is not enough simply for large numbers of witnesses to appear at the hearing and protest. They must be prepared to bring forward convincing evidence not only that they would like to have the line continued but that they need to have it continued as a matter of necessity. The testimony must persuade the
ments such as that cited above (footnote 29) and similar dicta by the Commission that this view cannot be unequivocally supported by the record; and it is significant that the Commission's regular line of decision has not been subjected to reversal.

It should here be noted that the Commission has rightly insisted that, in the measurement of the "system loss" pertinent in abandonment proceedings, the carriers should attempt to get at the actual outlays which could be avoided if the line were abandoned and the actual loss in revenues which would take place in this event. While the Commission has perhaps been annoyingly indefinite on questions of detailed accounting procedure acceptable to it, it has definitely quashed carrier attempts to include in the expense calculations allocations of general overhead costs which would not be appreciably affected by abandonment of a segment and has insisted that the revenue calculations taken into account the "feeder value" of the branch on a realistic basis.

It is true that the minimum rate power has in some instances been used to prevent a rate reduction which, although it would not in itself result in a rate demonstrably below fully-allocated cost for the traffic to which it was to apply, would tend indirectly to jeopardize the overall profitability of railroad operations. However, this has in general been done in cases where the rate reduction in question would necessitate widespread decreases in competitively related rates or rates on the same commodity for hauls having substantially similar transportation characteristics. Furthermore, the more common use of the power to prevent rates which are below specific costs for the traffic in question

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Commission that there is prospect that the railroad will be used to a sufficient extent to give some prospect of its being able to support itself...

"In any event . . . no amount of local objection will prevent an abandonment unless the local interests appear to be able and willing to supply enough business to keep the line running now or in the future."

19 Cherington, op. cit., p. 162. The Board's staff has recently tangled with this problem in the Southwest Renewal—United Suspension Case (Docket No. 3718 et al.). In the Examiner's Report, dated March 23, 1950, strange and wonderful results have been obtained by the use of two different methods of calculating the profitability of several individual stations on United's system. For example, we find (p. 56) that United lost $8,889 on its service to Eureka, California, in 1948; we also find (p. 59) that, also on the basis of 1948 figures, United would lose $27,986 annually as a result of the suspension of its service to Eureka. The method leading to the latter result, which appears to be the one chiefly relied on by the Examiner in reaching his conclusions, seems far less objectionable than the other type of calculation included in the Report. The treatment of system overhead, while questionable in detail, is, as the Examiner pointed out (pp. 50-52), probably more justifiable where several stations are to be suspended than where the suspension of only one point is being considered. In view of the facts (a) that the Board itself has not yet rendered any decision in this case and (b) that the defects in the particular accounting methods used are of small concern as compared with the generally objectionable character of the action recommended by the Examiner, it does not seem worth while to criticize these accounting procedures in detail.

29 Cherington, op. cit., pp. 163-164.

30 See, for example, Instrastate Rates on Bituminous Coal Between Points in Illinois, 206 I.C.C. 120, 128-124 (1934); Cement, in Carloads, from Linwood, Iowa, to Points in Illinois, 140 I.C.C. 579, 582 (1928); Salt Cases of 1923, 92 I.C.C. 388, 410-412 (1924).
(or are barely compensatory without compelling reason) and thus throw a burden on other traffic and thus provides a precedent for not permitting unprofitable low-fare service on high-cost lines.

In general, then, there would seem to be no legal obstacle to the adjustment of the geographical fare structure to provide a more adequate reflection of cost differences; and the weight of precedent appears to be against the enforcement of a fare structure imposing unduly high rates on one segment in order that another shall be afforded a service whose revenues are insufficient to cover the costs to which it gives rise. After all this has been said, however, it would be quite wrong to conclude (a) that all air operations whose contributions to system commercial revenues fall short of their contributions to system expenses should be abandoned or consigned to the limbo of subsidized operations (even though allowance should have been made for the temporary reprieve of those routes which showed promise of early commercial self-sufficiency); (b) that the proper level of commercial rates on route segments capable of commercial self-sufficiency is that level which will provide such self-sufficiency; or (c) in determining the appropriate total yield which should be produced by any segment, that either out-of-pocket cost or fully-allocated cost provides a generally valid "ceiling" above which the yield should not be permitted to go.

Propositions (a) and (b) are untrue because the courses of action which they envisage would involve ignoring completely the legitimate mail payments which should be attributed to such segments and would therefore logically lead to (1) the establishment of unduly high commercial rates on segments capable of commercial self-support and (2) the abandonment, or stigmatization as subsidized, of short routes which might in fact be fully self-supporting on the basis of total legitimate revenue yield.

The third proposition, which is meant to apply to total (not merely commercial) revenue yield, is untrue because neither of the two cost

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On this point, Dr. Sharfman has noted (op. cit., p. 443) that although "the Commission has sometimes spoken as if it were proper for better-paying traffic to bear part of the cost of moving cheaper commodities," "on the whole it appears to have been its policy from the beginning not to permit rates to be fixed at so low a level on any traffic as to burden other traffic." (Emphasis supplied.) The typical attitude of the Commission is illustrated by the following quotation: "Put such a rate on corn as will encourage and warrant its movement if such a rate is fairly remunerative. While rates should not be so low as to impose a burden on other traffic they should have reasonable relation to cost of production and the value of the transportation service to the producer and shipper." Rates and Charges on Food Products, 3 I.C.R. 93, 104 (1890). The contrary view—or, as Dr. Sharfman describes it, the "idea of having one type of traffic subsidize another"—is illustrated by a statement in the Commission’s Annual Report for 1890, pp. 14-15: “In every classification... articles whose value is very great in proportion to the bulk or weight are classed high in the expectation that the rates imposed upon them will pay not merely the cost of transportation and a fair profit to the carrier, but will contribute also toward adequate remuneration for the transportation of such articles as cannot bear proportionate charges."
measures referred to accurately reflects the point above which an “un-
due burden” would be placed on any particular operation. In terms
of this “burden” concept, out-of-pocket costs represent a generally valid
“floor,” below which the maintenance of any operation would clearly
entail the burdening of other traffic; but the appropriate yield to be
drawn from any given operation may lie anywhere between this gen-
eral minimum and the revenue level at which this service could be
supported as an entirely isolated operation. It is this latter level, rather
than fully-allocated costs, which constitutes the generally applicable
“ceiling” for legitimate revenues from any service.

The chief point to be made here is that the adjustment of the
geographical commercial fare structure to conform more closely to
the cost pattern and the measurement of the degree of self-support of
the various segments of any airline system (whether or not the meas-
urement is made with a view to the abandonment of non-self-support-
ing segments) cannot be done without the ascertainment of legitimate
mail payments to be attributed to these segments, and will also require
a more sophisticated approach to cost questions than is embodied in
a mere mechanical allocation of overhead.

PROMOTIONAL FARES (OTHER THAN AIR COACH)
INITIATED BY THE CARRIERS

Here again it is generally true that the Board’s chief aim has been
to insure that these promotional fares result in increased rather than
decreased net revenues to the carriers. Thus, the Board indicated that
it would approve a “family fare” plan only where there was good pros-
spect that such a plan would result in increased utilization of idle facil-
ities by traffic which would not have traveled at regular fares
and

41 C.A.B. Policy Statement on Coach and Promotional Tariffs, September 7,
1949, p. 3: “Many of the domestic air carriers have had in effect since last fall or
winter the so-called family fare plan under which members of a family may travel
by air at a reduction (usually 50%) from the regular fare if traveling with the
head of the family on certain off-peak days of the week, such as Monday, Tuesday
and Wednesday. This plan appears to have been successful in building up traffic
for the carriers during the periods of the week when traffic is usually light. The
success of the plan in generating new traffic, as opposed to simply diverting traffic
from a peak to an off-peak period of the week, is not entirely clear, but the indica-
tions from the material which has been submitted to us by the carriers are that a
considerable proportion of family fare traffic is in fact newly generated. Accord-
ingly, we are inclined to look with favor upon a continuation of the family fare
plan. Since we do not yet have available data with respect to the family fare plan
during the peak summer season we shall limit the extension to June 30, 1950.

“We will expect those carriers which do not now have the family fare plan in
effect, but which desire to file tariffs containing the plan, to support such filings
with adequate traffic data, indicating the nature and extent of their off-peak traffic
loads. We are not prepared to approve, as some carriers have proposed, a family
fare plan which would be applicable to all days of the week.”

It should here be noted that a plan which actually succeeded in diverting
traffic from peak to off-peak periods might increase net revenue in the long run
even though no new traffic were generated and the total revenue was therefore
necessarily decreased to some extent. This would be the case if the economies
made possible by a more even distribution of the traffic over time were sufficient to
more than offset this decrease in revenue. This argument assumes that “peak”
capacity could be reduced if not required to accommodate commercial traffic.
that the results of certain other promotional fares would be closely scrutinized "to make a determination as to whether they are economical [and] . . . whether they were attracting to the carriers, having the tariffs in effect, any appreciable volume of additional traffic."  

The Summer Excursion Fares Case

Interesting examples of the employment of traditional regulatory categories to revise managerial price policy in the interest of maximization of carrier profits (or minimization of losses) are to be found in recent Board opinions dealing with promotional fare proposals. In The Summer Excursion Fares Case, certain proposed 21-day round-trip excursion fares, to apply during the summer months between points in Florida and certain northern and mid-western points, were initially found to be unjust, unreasonable and unjustly discriminatory, judgment subsequently being deferred on the question of unjust discrimination. The decision was based on the results which had been obtained in a past period from tariffs which, as the board declared, "were, as to level of fares and governing rules and regulations, substantially similar to those under investigation in this proceeding." The finding of unreasonableness rested on the conclusion that the amount of "new" traffic generated (representing an addition to total revenues) would not be sufficient to offset the diversion from standard-fare carriage occasioned by the availability of the excursion fares.

Despite the Board’s declaration that "In evaluating the reasonableness of fares we must examine their relationship to cost," the treat-

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42 Ibid., p. 4, where the Board also stated: "Each carrier having in effect a promotional tariff will be required to maintain an adequate statistical record of the results of the fare, reporting this information to the Board on a monthly basis. In this manner, we hope to have a firm statistical basis for determining whether the various types of promotional fares under consideration should become a permanent part of the passenger fare structure of the domestic air carriers."


44 Orders Serial No. E-4037, pp. 4-5.

45 The evidence on which this conclusion was based was summarized as follows in Orders Serial No. E-4132, pp. 3-4: "The record shows that between excursion fare points Eastern and National, combined, performed 124,176,000 revenue passenger miles during the summer of 1947 and 115,944,000 revenue passenger miles during the comparable period in 1948, when no excursion fares were in effect. [The low figure for 1948 was due to a strike.] In the summer of 1949, when excursion fares were in effect, 134,261,000 revenue passenger-miles were flown, including excursion fare passengers. The increase in total 1949 summer traffic over 1947 summer traffic was, therefore, approximately 10 million revenue passenger-miles; and over 1948 summer traffic the increase was approximately 18 million revenue passenger-miles. Total excursion fare traffic during the summer of 1949 amounted to approximately 79 million revenue passenger-miles. Regular fare traffic therefore declined 61 million revenue passenger-miles as compared with 1948 and 69 million revenue passenger-miles as compared with 1947.

"It is our conclusion, based upon the evidence of record, that the increase in traffic in 1949 attributable to the excursion fares was less than 18 million revenue passenger-miles, because it is reasonable to assume, on the basis of industry experience, that there would have been some increase in regular fare traffic even if excursion fares had not been available. If the excursion fares had succeeded in developing new traffic without substantial diversion the increase in total traffic would have been more nearly commensurate with the total excursion fare traffic carried. It is also our conclusion that the substantial decline of regular fare passengers in 1949 is indicative of substantial diversion occasioned by these fares."
ment of the cost issue in this proceeding was confined to a rejection of the "added-cost" theory advanced by the carriers; there was no positive statement as to the costs which should have been covered by the fares in question in order that they be reasonable; and this question was, of course, irrelevant in view of the major aim of the decision. Moreover, in view of the statistical evidence presented, the Board was justified in not devoting more attention to cost considerations, for this evidence appears to support a conclusion that the excursion fares most probably resulted in a net loss regardless of such considerations. In general, it would be necessary to balance the loss on diverted traffic (which, in the absence of any difference in cost of service between the two types of traffic, and of any economies through a more even spread of traffic over time as a result of the diversion, can be measured per unit by the difference between average revenue at standard fares and average revenue at excursion fares) against the net revenue from the new traffic generated, a calculation which would necessitate the ascertainment of the costs to be subtracted from the gross revenue from the new traffic. But whatever this net might be, it would be appreciably smaller than the gross revenue from the new traffic; in this particular instance the evidence seems to show that this gross figure was probably at any rate not much larger than, if as large as, the loss occasioned by diversion.

The excursion fares were apparently found to be unjustly discriminatory on the basis of the same statistical evidence which supported the finding of unreasonableness, which evidence was here used to prove that "the limitations upon the users of such fares affected only a minor part of the traffic," and hence that the different fares were being charged for "substantially similar services." This interpretation would make the issue of unjust discrimination hinge upon the proportion of the traffic deterred from using the excursion fares by the limitations under which they were offered — i.e., the proportion of the traffic traveling at standard fares which would continue so to travel after the excursion fares had become available, a proportion which is inversely measured by the diversion from the regular fare service. In subsequently suspending judgment on the issue of unjust discrimination, the Board held that this issue could not be settled in advance of actual experience with the fares involved. This position was adopted in connection with the Board's indicated tentative approval of excursion fares substantially similar to those disallowed except that they were to be in effect for a shorter period.

46 Orders Serial No. E-4037, pp. 7-9.
47 Orders Serial No. E-4132, p. 5.
49 Orders Serial No. E-4137, pp. 5-6: "National and Eastern urge that our finding on discrimination applies to all excursion fares and that this finding is contrary to applicable law and is based upon a misapplication of the principles without consideration of the practicalities of the situation.

"In our tentative opinion we found that under these particular fares, excursion fare passengers and regular fare passengers each would receive substantially
This interpretation, although in this case providing a convenient reinforcement of the Board’s finding of unreasonableness in the interest of maximizing net revenues, would not always necessarily operate to this ultimate end. Thus, a particular proportion of traffic diverted from regular fares might in some instances be associated with a promotional fare which would decrease net revenues, and in others with a promotional fare which would increase them. Although, as has been noted above, (and under the noted conditions), diversion itself represents a loss which would have to be offset by net revenues from new traffic, a given proportion of diversion may evidently be more than offset in some instances and less than offset in others.

The Board’s particular criterion of discrimination is, as far as this writer has been able to determine, unique in regulatory history. Nevertheless, it represents a not unreasonable particularization of a traditionally accepted criterion and would thus appear to be legally defensible. Such legal difficulties as may arise may more probably result from possible attempts by the Board itself to reconcile the stated criterion with maximization of profits under varying economic conditions. It would be too much to say that the Board’s lawyers would be so devoted to substantial precedent as to be unable to supply justification for contradictory doctrines in dealing with such cases; however, it is within the realm of possibility that some court might be unable sympathetically to comprehend the requisite legal contortions.

As for the doctrine of reasonableness here employed by the Board, there is ample precedent in recent regulatory history for the interpretation of this legal requirement to compel policies regarded by the regulators as more profitable than those proposed by the regulatees; however, the Commission has been generally reluctant so to revise managerial judgment, and the Board’s failure to consider more fully the relationship between the revenues obtained under the disallowed

similar services with a fare differential beneficial to the excursion fare passenger. Our finding does not per se render unlawful other reduced fares of a promotional nature which carriers may wish to file. It is true that the excursion passengers would not receive the full privileges of a regular fare passenger. The most important limitations on the excursion fare round-trips permitted in our tentative opinion are that the passenger must complete his round-trip in 21 days and that the round-trip must be made during the limited period of July 5-August 31, 1950. Whether these differences in privileges have any substantial effect on the services offered or are mere paper differences is a question of fact. The record in this proceeding suggests that the differences in service do not make practical differences. Upon reexamination of this record, however, we believe the facts are not sufficiently conclusive, and we will, therefore, defer our judgment on the question of unjust discrimination until the completion of the limited experiment with excursion fares for the period July 5-August 31, 1950. We propose to require the filing of complete reports of the operations under such excursion fares so that we may be in a position to ascertain whether the limitations placed thereupon are in fact substantial, justifying the difference in fare levels.”

50 See, for example, Passenger Fares and Surcharges, 214 I.C.C. 174 (1936).

51 D. P. Locklin, op. cit., p. 109: “Minimum rates are frequently prescribed, or proposed reductions are disapproved, when collateral losses of revenue to the carriers proposing the rates seem likely to offset revenue from new traffic to be obtained by the reduced rates. This frequently happens when reductions are proposed for competitive reasons, even though a considerable volume of traffic moves by the carrier in question at the higher rates. Cases are not difficult to find
fare structure and relevant costs leaves it open to the charge of throwing an "undue burden" on the affected traffic.

The treatment of the discrimination issue here, while on a much subtler level, reflects the same broad approach as the treatment accorded it in *Air Passenger Tariff Discount Investigation*, 3 C.A.B. 242 (1942). Here the so-called Air Travel Card Plan and a similar volume discount arrangement open to U. S. Government employees were found not to
give rise to any undue or unreasonable preference or unjust discrimination; and [to be] . . . just and reasonable classifications, rules, regulations and practices . . . except in details and with modifications indicated.

The favorable effect of the discounts on carrier traffic and revenues was given major emphasis in the opinion. Despite the recognition that the benefits of the volume discount were probably not uniformly applied to all passengers who spent the required minimum on air transportation, the classification was found not to result in unjust or unreasonable rates, "considering the impetus that subscribers have given to the development of air transportation by taking advantage of the plan" (p. 250). On the discrimination issue, the Board cited a catch-all Supreme Court statement admitting every possible factor to be relevant in the determination of this issue, and then declared (p. 251):

Viewing the issues here in that light, it appears that there is no competitive relationship in the customary sense between the classes of traffic involved, that the reduced rates are reasonably open to all, that the Plan constitutes a convenience and benefit to a considerable part of the traveling public, that the interests of the carrier are reasonably promoted, and that the difference in rates is not clearly improperly adjusted with reference to the actual savings and profit to the carrier flowing from the Plan.

In *Government Travel Discount Tariff Investigation*, 6 C.A.B. 825 (1946), the Board declared that discounts for official government travel as well as for personal travel of government employees "eventually should be eliminated in their entirety" (p. 832). This decision, however, did not reverse the broad stand previously taken in this connection; on the contrary, it embodied the view that the differential fare policy was justifiable to the extent (and only to the extent) that it constituted a sound promotional device (p. 832):

Even if such discounts were justified in the past as a device to promote the development of air transportation, they now have outlived their usefulness for such purpose and should be abandoned as rapidly as circumstances will permit. Such a removal of inequality in which rate reductions have been prevented because of the collateral losses. The Commission recognizes, however, that the question of whether a reduction in rates on particular items of traffic will increase or reduce revenues cannot be determined with certainty. Since the question is one which is primarily within the province of management, the Commission is not likely to interfere on the grounds that the revenue results are uncertain." (Supporting citations omitted.)
ties in the fare structure not only is in accord with the provisions of the Civil Aeronautics Act regarding discriminations, but also creates a sound basis for reductions in the level of fares for all classes of passenger traffic.

It is highly significant that in this proceeding the carrier maintained that the discounts, although profitable in the past, had now become a losing proposition.\textsuperscript{51a}

\textbf{Northern Consolidated Airlines' Passenger Excursion Fares}

Similar issues were involved in \textit{Northern Consolidated Airlines' Passenger Excursion Fares},\textsuperscript{52} where the "reasonableness" concept was employed to limit the period for which certain promotional fares proposed by an Alaskan carrier in order to develop tourist and vacation travel during an off-peak season should be applicable, and both this concept and that of "undue preference and prejudice" were used to increase the average fare level for this travel as compared with that proposed by the carrier. On the first point, cognizance was first taken of the fact that available flights were being operated at low passenger load factors, and that little increase in cost would be occasioned by aditional traffic to the extent that it was accommodated on these flights. "On the other hand," the Board continued, (pp. 5-6):

"it is not clear that the increased traffic which Consolidated hopes to generate will, in fact, offset the reduction in its revenues occasioned by diversion of traffic from the regular fares . . . [however] we are sympathetic with Consolidated's proposal to experiment with lower promotional fares and believe it desirable to give the carrier's management an opportunity to make a fair test of the potential traffic under lawful promotional fares . . . It is likely that the end of the tourist season will cause the proposed fares to reduce Consolidated's gross revenues and, accordingly, we cannot now find that the fares are reasonable for the period subsequent to September 3, 1950 . . . Therefore, we will require that the promotional fares under consideration be cancelled, without prejudice to Consolidated's right to refile promotional fares, with such other revisions as are indicated herein, with an expiration date of September 30, 1950.

The principle here involved is evidently the same as that in \textit{The Summer Excursion Fares Case}, discussed above.

Similarly, the test of discrimination by the proportion of regular-fare traffic likely to be affected by the limitations on the availability of the excursion fares was applied to the "undue preference and prejudice"

\textsuperscript{51a} P. 830: "Pan American pointed out that the need for a government discount to enable air transportation to compete with established surface transportation had entirely disappeared, and that the discount now was a serious liability to it. It introduced evidence to show that increases in the amount of government travel meant a reduction in its Latin American revenues in 1943 of over $1,300,000 resulting from use of the discount."

\textsuperscript{52} Orders Serial No. E-3958 (March 3, 1950.)
dice" concept in the Northern Consolidated opinion; but it was not up-on this concept that the findings of undue preference and prejudice were based. In one instance this finding seems to have been based on an estimate of difference in value of service which was simply declared to be less than that implicitly put forward by the carrier; in another, this finding (and a finding of unreasonable) was related to a disregard of distance relationships in the construction of some of the round-trip rates, resulting in fares "totally unrelated to costs of operation and the value of the service." The issues raised here are essentially the same as those in The Hawaiian Common Fares Case now to be discussed.

The Hawaiian Common Fares Case

In this proceeding, a proposed tariff blanketing fares to Hawaiian points from the mainland was found unreasonable and unduly preferential and prejudicial. The effect of this blanketing was not only to afford substantially varying amounts of transportation for the same money but to bring about "a fare reduction ranging from $6.50 to $13.50 in the through fare from common fare West Coast cities to the outer islands," and a consequent reduction in yields per revenue passenger mile amounting to as much as 8 percent. In spite of a showing by the chief proponent carrier (United) that its fully-allocated costs would be covered by total revenues (there being included in the calculation the mail revenues at the rate then in effect), the rates were found unreasonable because (a) the Board thought it unlikely that the costs of Pan American and Northwest would be covered, (b) all three of the carriers were requesting higher mail payments for their operations as a whole, and (c) the approval of rates constructed on the blanket principle would provide a precedent for

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53 Ibid., pp. 7-8. "In the absence of data which would justify the fare differentials between two one-day fares and the ten-day round-trip fares and between the regular one-way fares and the ten-day 'open-jaw' and 'circle' fares, it would appear that the proposed fares unduly prefer the ten-day passengers and unduly prejudice the regular fare passengers . . . however . . . Regular fare tickets are valid for one year. Tickets under the proposed tariff are valid for only ten days. The record shows that fewer than 19 percent of Consolidated's passengers completed their trips within ten days. Thus, some differential in fare seems to be justified, it being obvious that the one-year ticket is worth something more than the ten-day ticket." (Emphasis supplied.)

54 Ibid., p. 8: "We believe that the maximum differential justified by the difference in value of the two types of services provided is not in excess of 37½ percent of the one-way fare, i.e., we believe those ten-day 'circle' trip and 'open-jaw' trip fares which are less than 62½ percent of the regular one-way fares and that those ten-day round-trip fares which are less than 125 percent of the applicable one-way regular fares are unduly preferential and prejudicial."

55 Ibid., p. 7.

56 Ibid., p. 8: "... a passenger from San Francisco can fly as much as 8.3% more mileage for the same fare . . ."

57 Ibid., p. 6.

58 Ibid., p. 15.

59 Ibid., p. 15.

60 Identical tariffs filed by Pan American and Northwest were withdrawn when the Board suspended the fares.
further approval of similar rates in similar circumstances; and the Board believed that such a fare-making principle by which varying amounts of transportation are furnished for the same money under similar conditions inevitably results in a fare structure which will invite economically unsound conditions.\textsuperscript{61}

The Board nevertheless expressly left the way open for the approval of such fares as reasonable where it could clearly be shown that net revenues would be increased by them.\textsuperscript{62} In support of its belief that in this particular case net revenues would not be increased, the Board pointed to the fact that a recent increase in the rates commensurate with the proposed effective reduction had failed to result in a decline in total traffic, and to the weakness of the evidence presented by the carriers on this point.

The reasoning as to undue preference and prejudice, however, does not seem quite so well adapted in principle to the Board's purposes. Although it was not unequivocally stated that any fare structure involving common fares for consecutive points would be ipso facto unduly preferential and prejudicial, it was indicated that such a fare structure would be so found "unless justified by special circumstances, among which may be compelling competitive relationships between carriers which require the carrier to grant the preference to the farther moving passenger in order to obtain the traffic, or actual differences in cost of service, or similar recognized transportation standards,"\textsuperscript{63} and that these "special circumstances" would not include a long-run increase in the traffic of the carrier.\textsuperscript{64} Thus it is conceivable that a strictly consistent application of this interpretation might embarrass the Board in some future proceeding where fares of this nature would clearly increase carrier profits.

On this issue, regulatory precedent again seems adequately in accord with the Board's action, despite numerous instances in which group rates have received I.C.C. sanction, and despite the fact that the Commission has habitually laid an especially heavy burden of proof.

\textsuperscript{61} Orders Serial No. E-3965, pp. 3-4. See also Orders Serial No. E-3625, p. 6: "Generally, we feel that a sound fare structure for consecutive points on a route requires that the respective fares increase with distance because costs increase with distance, and that a departure from this principle will tend to lessen the revenue of the carriers, weaken their economic position, and impair their capacity to render adequate and efficient service. Ordinarily, therefore, we believe common fares applied to consecutive points are unsound in principle . . . ."

\textsuperscript{62} Orders Serial No. E-3965, pp. 4-5: "Compelling competition from other carriers requiring the same fare for a longer distance may be one possible justification [for common fares to consecutive points], but such a justification is not found in this record. A clear cut showing that in the particular circumstances, this generally unsound fare structure will nevertheless improve the revenues and strengthen the economic position of the carriers may possibly be another, but in our opinion the record is not convincing on this point. The carriers' witnesses and the witness for the Hawaiian Visitors' Bureau did, it is true, forecast increased tourist traffic from the ability to offer a single fare 'package' to all the islands, but the basis for this hopeful prospect appears to us highly speculative."

\textsuperscript{63} Orders Serial No. E-3625, p. 9.

\textsuperscript{64} Ibid., p. 10.
The finding of undue preference and prejudice between localities competitive for tourist traffic on the basis of a rather speculative showing of potential injury was contrary to the Commission's general practice in the specific application of Section 3 to group rates, but not to its usual construction of this Section. The inapplicability of the traditional requirement of competitive relationship to preference and prejudice as between passengers (also here found by the Board) has, as the Board pointed out, already been affirmed by the Supreme Court. However, it should perhaps be reemphasized that the main concern of the Board in attacking blanket fares has been the belief that they operate to reduce net revenues; here, as in the statement on domestic fares shortly to be discussed, the Board aimed directly at an upward revision of the proposed or actual blanket fares applying to longer distances, rather than a correction of the fare relationship as such. This approach may be contrasted with that of the I.C.C., which regards it as of the essence of undue preferences and prejudice that it may be corrected either by an increase in the preferential rate or a decrease in the prejudicial one. The contrast, though obviously insignificant in

Dr. Sharfman has noted that the tolerant attitude of the Commission toward such group rates, although in part justified by transportation factors, seems also partly based on commercial considerations which the Commission generally refuses to recognize. He has summarized the Commission's position as follows (op. cit., pp. 673-674): "It [the Commission] has maintained the position early enunciated 'that the propriety of its [i.e., the group rate principle's] application is properly open to challenge in every case'—in other words, that group rates constitute one of the arrangements which may be permitted where circumstances warrant, but which will not be required. But to an extent not ordinarily manifest where individual carriers adjust rates to attract traffic, the Commission has often revealed a positive sympathy with the practice of blanketing rates on an equal basis, sometimes over considerable areas. This sympathy has not extended to the point of imposing group rates, except where the blanketing principle has met with general approval as a solution for a chaotic rate situation, and in circumstances in which, the practice having already been adopted by the carriers, its uniform and equitable application has been required. It is apparent, nevertheless, that when group rates are attacked as unduly preferential of the furthest removed sections of an area and unduly prejudicial to nearer points, the Commission imposes an especially heavy burden of proof upon complaining parties. It insists, in particular, that proof of injury be positive and substantial. The obvious presumption that the failure of rates to correspond to transportation service creates in itself a discriminatory situation seems to have carried but slight weight. Absence of injury has been shown through submission of evidence that the market is capable of absorbing the volume of product carried to it, and that the rates to the more remote points are compensatory. The existence of injury appears to have been determined through a process of balancing the gains to some as against the losses to others arising from the group arrangement, without the usual care, it seems, in recognizing that it is of the very nature of a preferential relationship that it bestows benefits and hence is not to be justified thereby." (Supporting citations omitted.)

Orders Serial No. E-3625, pp. 9-10.

Ibid., p. 8.

See, for example: (1) Utah State Automobile Association v. A. T. and S. F. Ry. Co. et al., 92 I.C.C. 376, 386 (1924): "Doubtless complainant would be benefited by a reduction in the rates on gasoline, but preference in and of itself can be eliminated by raising the lower rates as well as by reducing the higher rates. It is, therefore, clearly pertinent in determining this question of injury alleged to
terms of legalistic justification of the Board’s action, is a revealing one in that it brings out the novelty of the Board’s use of this category.

In addition, the Commission and the Courts have held that a presumption of unreasonableness attaches to a higher rate for a shorter than a longer haul on the same line, a position which could logically be extended to provide support for the Board’s general view that special justification is needed for the practice of charging the same rates to consecutive points.

The use of the costs of competitive carriers as a criterion of reasonableness is perhaps open to some question in terms of regulatory precedent. It is true that the power of the Commission to prescribe rates to cover the expenses of higher-cost competitors has been confirmed in a decision of a Federal Court, but a contrary view has been implied in a Supreme Court decision where this use of the Commission’s power was not directly at issue. However, the apparently contrary doctrine recently enunciated by the Commission (in connection with the amended rule of rate-making in the Transportation Act of 1940) is evidently not applicable to competition between air carriers; the crucial new phrase—“by the carrier or carriers for which the rates are prescribed”—is not included in the rule of rate-making in the Civil

flow from preference, to consider whether or not complainant would be better off if the rates on the crude oil were made higher.”

(2) *Duluth Chamber of Commerce v. C., St. P., M. and O. Ry. Co.*, 122 I.C.C. 739, 742 (1927): “... to prove that this discrimination results in a violation of section 3 it must be shown that complainant suffers injury by reason of the discrimination, and that this injury will cease if the discrimination is removed, regardless of the manner of its removal.”


70 Since the passage of the Transportation Act of 1920, the Commission has the right to prescribe minimum rates, and we agree with the Commission that a construction of the law is too narrow which limits its right to prescribe such rates to cases where the rates proposed are unreasonable per se, or are so low as to cast a burden on other traffic. It has the right to prescribe minimum rates also to prevent ruinous rate wars and to guarantee reasonable earnings, not only to the carriers affected, but also to competing carriers, who may labor under a higher cost of doing business.” *Anchor Coal Co. v. United States*, 25 F. (2d) 462, 471-472 (1928).

71 The evidence failed to show that the rates of the Texas and Pacific and the L. R. and N. were not compensatory. The Commission refused to find that they were so low as to cast a burden on other traffic. There was therefore no basis for an order fixing minimum reasonable rates under section 15(1) of the Act.” *Texas and Pacific Ry. Co. v. United States*, 283 U.S. 627, 633 (1938).

72 See, for example, *Seatrain Lines, Inc. v. Akron, C. and Y. Ry. Co. et al.*, 243 I.C.C. 199, 214 (1940): “... the rule of rate making in section 16a has been recently amended so as to require us, in the exercise of our authority to prescribe just and reasonable rates, to ‘give due consideration, among other factors, to the effect of rates upon the movement of traffic by the carrier or carriers for which the rates are prescribed...’ This admonition is repeated in Sections 216(1) and 307(1), containing rules for rate making relating to motor and water carriers, respectively. The words which have been italicized for emphasis are of particular interest. They were not in either of the bills originally passed by the Senate and the House of Representatives but were added by the committee of conference. Their meaning, supported also by the legislative history, seems to be that no carrier should be required to maintain rates which would be unreasonable, judged by other standards, for the purpose of protecting the traffic of a competitor.”
Aeronautics Act. It is perhaps worth noting that although the Commission has regarded average costs of all carriers within a given region as a proper consideration in the prescription of general regional rate floors for motor carriers, it has subsequently regarded the costs of the carrier proposing a rate as a significant test of compensatoriness, even though the rate were below the previously prescribed minimum.

In so far as the Board's finding of unreasonableness was based on the anticipated effect of the proposed effective fare reduction on the net revenues of United's entire system, it raises the same problems as were discussed above in connection with possible low-net coach fares on relatively high-traffic segments. Here, however, the question of the "system need" mail payment obtrudes itself directly: The Board emphasized the fact that, although the proposed fares were not expected to result in a need for additional mail payments on the segment of United's system to which they applied, such payments were being sought by United and by the two competitive carriers for their entire systems. It was not expressly contended that either the payments on United's Hawaiian segment or, indeed, the additional payments being sought were higher than a reasonable compensation for the mail service rendered. However, it is unmistakably implied that the existence of the petitions for higher mail rates in some way justified the maintenance of passenger yields at a higher level than might otherwise be allowable. It is obvious, of course, that where mail payments are determined so as to equal the excess of total costs over commercial revenues, the maintenance of commercial profits at the highest possible level — i.e., the enforcement of a monopolistic price policy — will, other things being equal, result in the smallest bill to the government. In this context, the fact that a particular service, or indeed, the entire system, might be a self-supporting on legitimately earned mail payments and commercial revenues at a non-monopolistic level is quite irrelevant.

73 Central Territory Motor Carrier Rates, 8 M.C.C. 233, 256 (1938): "It is impracticable to prescribe rates based upon the costs of individual carriers or groups of carriers. To do so would only perpetuate the destructive competitive practices which now prevail. Necessarily, the rates which we prescribe are affected by cost and they must be based upon the average cost of all carriers handling the various kinds of traffic."

74 D. P. Locklin, "Rates and Rate Structure," p. 113: "The effect of prescribing minimum rates over large areas is to prevent some rates which might be justified by the low costs of particular operators. The Commission, however, is not committed to uniformity in rates by all motor carriers competing for the same traffic or serving the same general area."

James C. Nelson, "New Concepts in Transportation Regulation," Transportation and National Policy, p. 229: "Perhaps the chief test of reasonableness employed has been whether truck-mile revenues from a proposed rate would be sufficient to cover average costs of some type, often the carrier's truck-mile costs. For our purposes it is sufficient to note that the historical average cost of the proposing carrier is commonly, though not universally, regarded as a significant test of whether a proposed rate is compensatory." (Supporting citations omitted.)

75 This was not, of course, shown for the Hawaiian segment of United's system, because (a) the cost calculations were not intended to show the expense of maintaining this segment as an independent unit and (b) the mail revenues were not shown to be no more than reasonable compensation.
in determining commercial rate policy as is, indeed, the whole question of legitimate mail revenues. But however commendable the conservation of Government funds may at first sight appear to be as an object of public policy, it is open to serious question as an ultimate guide in transportation rate-making. The problems which arise in this connection will be more thoroughly treated at a later stage of the discussion.

Suggested Fare Policies Initiated by the Civil Aeronautics Board

In *The Hawaiian Common Fares Case* (in which the tentative opinion was issued in November, 1949), one of the points brought up by the carriers in defense of the proposed blanket fares was the fact that such fares were already in existence for other services (of varying distance) under C.A.B. jurisdiction. In response to this argument, the Board pointed out that it had neither investigated nor formally approved any of these fares: "It may be," the Board continued, "that an investigation might disclose that some or all of such common fares are unlawful." The existence of such fares was moreover held to be irrelevant "in the absence of any evidence that the circumstances and conditions affecting the existing common fares are similar to those affecting the proposed fares." Public counsel furthermore expressed the view "that the existence of the common fares on the West Coast is unsound in principle, costly to the carriers involved, and unfair to communities and passengers," and quoted a letter from the President of United Airlines to the effect that United was losing from 4 to 6 million dollars a year in revenue as a result of transcontinental rates figured on the New York-Los Angeles mileage.

On February 3, 1950, Board Chairman O'Connell addressed to the carriers a letter stating that "a study of the entire problem of the construction of domestic passenger fares" was about to be begun by the Board's staff, and requesting carrier views on "three immediate possibilities for tariff adjustment":

(1) the placing of all fares on a mileage basis; (2) discontinuance of the meeting of fares over circuitous routings when the circuity exceeds 20 percent; and (3) providing that when stopovers are made, the fare for the total journey be computed by combining the individual fares between the points visited by the passengers.

The Chairman enclosed a statement prepared by the staff of the Board dealing with fares by circuitous routings, common fares, and fares for passengers utilizing stopover privileges, and requested comment on this statement.

The general objective of the proposed fare revisions is made quite clear in the text of the statement. Thus, the three tentative recommen-
dations mentioned by Mr. O'Connell are explained as follows (pp. 3-4):

While this entire matter [i.e., the application of fare-making concepts originating in surface transportation] is presently being studied, it appears that certain immediate steps should and can be taken in an attempt to remedy those situations having the most harmful effect on the carriers' financial results. (Italics supplied.)

Again, in discussing the origin of common fares in the competitive principle of equal fares between the same points by different carriers over different routes (combined with the principle that no fare to an intermediate point or a given route should be higher than the fare over the entire route) the statement concludes (p. 2):

Competition between carriers is of course highly desirable, and no effective competition would exist if carriers could not charge the same fares for travel between the same points. The practice of meeting fares between competitive points, however, does reduce the average revenue yield of the longer route carriers and in some cases this reduction is very substantial. (Italics supplied.)

The practice of granting stopovers at no additional charge — specifically, stopovers at common fare points — was also considered from the point of view of its effect on carrier profits. Although the staff had found it impossible "to analyze the foregoing factors in terms of their effects on the financial results of the carriers," it noted that United Air Lines had "submitted information showing that for the six months ended May 31, 1949 its revenues could have been reduced by $751,346 as the result of the Chicago-West Coast fare structure" (p. 2).

In point of fact, the staff did prepare an estimate of the additional revenue which could be obtained from traffic between New York, Boston, Washington and Chicago on the one hand and certain West Coast points on the other, if (1) the fares between Chicago and the West Coast points were constructed on a 6-cent-per-mile uniform basis (using the shortest air carrier route as the fare-making route) subject to a $113.75 minimum (the present fare, which worked out to something more than 6 cents a mile between Los Angeles and Chicago), and (2) the fares between New York, Boston and Washington and the West Coast points were constructed on a similar 6-cent basis subject to a minimum equal to present fares and to a maximum equal to the Chicago combination (using the above suggested Chicago-West Coast fares). This estimate was made by employing the stunningly simple assumption that no change in volume of traffic would result from the

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78 Almost all of the carrier representatives who commented on the Board's proposals were opposed to the elimination of the stopover privilege. As to the effect of this practice on expenses it was variously stated (a) that stopovers entailed very little extra cost and (b) that the elimination of the stopover privilege might itself give rise to confusion and added costs in ticketing procedure. The opinion was almost universally held that the stopover privilege was a great "selling point" and that its elimination would result in diversion of traffic to surface carriers.
proposed fare increases. From it the staff drew the following unqualified conclusion (Appendix No. 1, p. 7):

Upon this basis we may assume [not presume] that transcontinental airlines are losing $1,111,381.76 annually on traffic between three Pacific gateways, on the one hand, and Chicago, New York, Boston and Washington on the other.

The blanketing of fares to West Coast points other than gateway cities was also attacked and the suggestion made that certain of these fares be constructed by addition of local fares to fares to gateway cities. (Appendix No. 1, pp. 7-9.)

In addition to its effect on average revenue, the statement pointed out, the practice of charging equal fares over circuitous routes competitive with more direct routes may result in higher costs of carriage than would be experienced under a direct routing of all traffic. (p. 3). Thus the proposed limit of 20 percent on permissible circuity without a fare difference was supported by reference to possibilities of lower unit costs as well as higher unit revenues. It was also pointed out that stopovers "result in additional costs occasioned by complicating the

79 Of particular interest in this connection are the following comments submitted by Mr. E. O. Cocke, Vice President—Traffic, T.W.A. (Letter to the Director of the C.A.B.'s Bureau of Economic Regulation, dated March 31, 1950): "If the fares to certain Pacific coast points were raised, as suggested in the statement attached to the letter . . ., the amount of traffic lost to the rail carriers alone would undoubtedly more than offset any possible increase in revenue from those passengers who continue to travel by air to Pacific coast points. It is estimated that as far as TWA is concerned, the theoretical loss of revenue resulting from the use of common rate points is approximately $20,000 per month. This is equivalent to only about 75 round-trip transcontinental passengers so that if the elimination of common fare points (with the resulting increase in fares) would divert as many as 2 round-trip passengers a day to the railroads or would otherwise take these passengers from TWA, there would be a net loss of revenue to TWA."

It is also significant that Mr. Patterson himself appeared far from enthusiastic about the proposed revision of fares to major West Coast cities. He advised the Board to study thoroughly the history and background of the common-fares practice before taking any action, and said: "We are of the opinion the Board can never successfully dispose of the theory of common rates." (Letter to Board Chairman O'Connell, dated March 31, 1950.)

80 It might appear unnecessary to guard against genuinely wasteful competition if the competing carriers were trying to maximize profits; actually, the I.C.C. has thought it necessary to place limits on circuity in railroad routes permitted relief under Section 4 in order to meet competition. Dr. Locklin has discussed the Commission's treatment of this problem as follows (Economics of Transportation, p. 555):

"The degree of circuity must not be too great, however. Not only does the through rate become less than reasonably compensatory over an extremely long route, but the transportation of goods by an extremely circuitous route is wasteful. The Commission very often restricts fourth-section relief to lines that are not more than 70 or 80 percent circuitous. In some cases the degree of circuity permitted varies with the distance of the direct route. A typical case of this sort limited the degree of circuity to not more than 70 percent when the distance by the direct route was 150 miles or less, to 50 percent when the direct route exceeded 150 miles but did not exceed 1,000 miles, and 33 1/3 percent when the direct route exceeded 1,000 miles. In other cases the Commission has limited relief to routes over which the proposed through rates would yield 5 mills per ton-mile or more . . . Still other methods of restricting circuity have been used." (Supporting citations omitted.)

On the face of it, it would appear that the prescription of a minimum yield approximately equal to out-of-pocket costs would be preferable to a rigid percentage limitation, if it is desired to approach the problem of maximum circuity on a rule-of-thumb basis.

In this connection, it is significant that the consensus of the carrier represen-
ticketing and reservations procedures in relation to what would be necessary for a through trip" (p. 3).

It is perfectly obvious, however, that the main purpose of the suggestions offered was not the achievement of a system of rates based on costs, but the increase of carrier profits through selective rate increases and (if necessary) the withdrawal of certain relatively unprofitable services. Thus, no consideration at all was given to the propriety in terms of absolute costs of the proposed fares to West Coast points, or to that of the present fares accepted as minima in their construction. The more detailed reflection of distance relationships by means of a reduction in fares for shorter distances rather than by the increases of fares for longer distances was likewise not considered. The proposed adjustment of fares to vary with distance served rather as a convenient and plausible method of increasing the effective fare level and thus adding to net revenues.

As has been noted, the staff report calculated the effect on commercial revenues of the proposed fare increase between certain points on the basis of an assumed totally inelastic demand for the services in question. Under this assumption, there would also be no change in the total cost of service, so that the calculated increase in gross revenues could be taken to equal an increase in net revenues. As a general rule, however, it would seem necessary to take into account in this type of calculation the possibility that the traffic might decline in some ratio to the fare increase; in this event, the gross revenues would not rise in direct proportion to the fare increase, and the calculation of the resulting change in net would furthermore have to take into account the (possibly less than proportionate) change in total cost attendant upon the decline in the volume of traffic. It would therefore appear advisable for the Board to proceed with caution in prescribing strict distance relationships between fares in all instances or attributing to such relationships an absolute value not subject to correction by a detailed consideration of the financial effects of their application in any given situation.

The representatives commenting on the Board's proposals was opposed to a rigid percentage limitation on circuitry; even those who thought that some limitation might be necessary to prevent managerial indiscretion generally favored individual treatment of specific instances by the Board. Several pointed out that the quotation of equal rates over circuitous as compared with more direct routes had in fact enabled them to utilize more fully capacity on schedules which would in any case have had to be operated to serve intermediate points, with consequent improvement in load-factors and in net earnings.

In this connection, one wonders if the Board's staff or Mr. Patterson has ever figured out how much it "could have cost" the carriers to calculate fares on the present basis—or, indeed, on a straight 6-cent mileage basis—as compared with, say, a straight mileage rate of 10 cents, or a "tapering" rate beginning at 10 cents per mile for short hauls, or a reverse taper (justified in terms of relative value of service) beginning at 6 cents, etc., etc.

It should be noted that no carrier representative commenting on the Board's proposals favored the placing of all rates on a straight mileage basis. One such representative characterized this proposal as the "Utopian dream of all rate analysts" (Letter from Sigmund Janas, Jr., Vice President—Traffic, Colonial Airlines, to the Director of the C.A.B.'s Bureau of Economic Regulation, dated April 14, 1950). Among the factors mentioned as making this proposal inadvis-
Since the proposals advanced here were in the nature of suggestions rather than orders, the question of legality or conformity to regulatory precedent is not practically significant. It is perhaps worth pointing out, however, that even under the present regulatory regime for surface transportation, where the financial welfare of the carriers seems to be recognized as an aim of coordinate importance with the protection of the shipping or traveling public, the I.C.C. has usually adopted a more passive role than that taken by the Board in this instance; it has not generally felt called upon to initiate drastic changes in price policies in order to increase the profits of the regulatees.

On July 18, 1950, after having received the comments of the carriers on its proposed revisions in fare policy, the Board instituted a formal investigation to determine the lawfulness of the airline fare structure to and from points on the West Coast, including classifications, rules, regulations and practices relating to such fares, and, in the event that any of these should be found unlawful, to determine and prescribe lawful fares, practices, etc. to replace them. The selection of the West Coast fare structure for special investigation was explained as follows in the opinion accompanying the above-cited Order (pp. 2-3):

For reasons of administrative expediency... we have included for initial action in this proceeding only those pairs of points comprising the most important areas where these fare situations [deemed by the Board to be possibly illegal] are prevalent. We recognize that the matters we propose to investigate... are only symptomatic of the over-all problem. We believe, however, that our investigation in this limited area may well provide a basis for later adjustment of other similar fare situations to the extent it may appear to be necessary.

This proceeding (Docket No. 4586) may, of course, result in positive action by the Board which will raise important questions related to regulatory precedent. At the present time, however, it is impossible to foresee the precise nature of the issues which may be involved.

**CONCLUSIONS**

In general, the recent activities of the Board in connection with commercial rates appear to be supported by regulatory precedent in able or impractical were the following: varying average costs on different routes on any given carrier's system; necessity for meeting competition; and necessity for charging the same fare between the same two points on nonstop and local schedules.

83 On this point, see James C. Nelson, *op. cit.*, pp. 197-204. The following quotations are illustrative:

(1) p. 201: "By 1920, then, a more significant and much more difficult rôle had been assigned economic regulation. It had to protect both shippers and carriers..."

(2) p. 203: "The underlying general objective in 1920 of promoting an adequate transportation system by regulatory action to implement carrier profits was continued in the Motor Carrier Act of 1935 and the Transportation Act of 1940..."

84 Orders Serial No. E-4431.
the sense that they do not depart so radically from such precedent as to make probable their being reversed in the courts. A possible exception may be found in the (implied) doctrine that the charging of rates which are reasonable on a certain segment may be prevented by regulatory action in order to support less profitable services elsewhere; in addition, there may be some doubt as to the legal validity of holding up rates for the purpose of protecting the traffic of competitors. Even the general approach of the Board—i.e., its single-minded pursuit of maximum profits for the carriers—finds a partial analogy in the recent history of surface carrier regulation, although the specific use of categories generally associated with the protection of transport users from discrimination in this connection is somewhat of an innovation. It has been pointed out that the invocation of these categories (even as specifically interpreted by the Board) may necessitate some fast legal footwork in the future in order to prevent their assuming a life of their own contrary to the general purpose of the Board.

To say that regulatory precedent does not generally rule out rate regulation oriented toward the conservation of commercial revenues, however, is far from saying that traditional regulation has as one of its aims the maximization of carrier profits. On the contrary, total revenues sufficient to cover total costs (including capital costs) would seem to be enough to meet the “positive” or “need” requirements of the rate-making rules included in the Interstate Commerce Act as well as similar provisions incorporated in Section 1002 (e) of the Civil Aeronautics Act; and it does not seem likely that the broad policy declarations in either Act envisaged the sanction—still less the active initiation—by the regulators of only such price policies as would produce the highest possible profits.

As the Board’s position in The Hawaiian Common Fares Case suggests, the special circumstance which may be adduced to support such

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85 It has been suggested that the Board’s policy might better be described as one of ruling out rate policies which are believed to decrease net earnings rather than aiming at maximum earnings for the carriers. The suggested description may mean one of two things, namely (a) ruling out rate policies believed to decrease net earnings as compared with a certain approved level, e.g., present net earnings or (b) ruling out rate policies believed to decrease net earnings as compared with the maximum possible net earnings. Interpreted in the latter manner (b) the proposed description, as compared with maximization of net earnings, embodies a distinction without a difference. The former description (a) is not an adequate description of the Board’s policy if it is taken to refer to present earnings; if the “approved level” is equal to or above the maximum now possible, the description is, of course, compatible with the Board’s policy, but makes no practical difference as compared with unqualified profit maximization. The Board has not merely disapproved rate policies which might decrease present net earnings; it has approved rate policies which are expected to increase net earnings, and has even attempted to initiate such policies. There may indeed be some other “approved level” which the Board regards as a reasonable maximum—e.g., those earnings which would represent commercial self-sufficiency for each carrier as a whole. However, this standard has not yet become an operative maximum, and as long as commercial revenues fall short of covering total costs, the practical results of such a standard will remain the same as those arising from an unqualified aim of profit maximization.
a policy in the airline field is the "subsidized" nature of the carriers—
i.e., their peculiar relationship to the public treasury whereby their
commercial losses must be made up by Government contributions. As
has been noted, given this relationship, it is obvious that, at least as
long as commercial revenues fall at all short of covering total costs, a
policy of minimizing losses before mail pay can be argued for on
grounds of governmental economy. But it is also obvious, in view of
the fact that mail is carried by the airlines, that at some point before
total costs are covered such a policy must result in shifting to the com-
mercial traffic costs which should be borne by the Post Office Depart-
ment. It is for this reason that the conservation of government funds
does not appear to be an appropriate guide for air transport rate-
making.

If it is accepted that the government as buyer of air transportation
is not entitled to preferential treatment—that is, that the commercial
traffic should not be called upon to subsidize the carriage of the mails
—then it follows that a commercial rate policy aimed at maximization
of net revenue or minimization of net loss before mail pay is generally
justified only where the operation in question cannot, or can only just,
be supported by the commercial revenues thereby obtained plus the
maximum legitimate mail payment. In this case, the commercial traf-
ffic and the mail traffic would receive equal treatment. Where the op-
eration can be more than supported by such revenues, i.e., where the
total cost of the operation to which the commercial rate is applied is
less than could be borne by commercial demand plus demand for
mail transportation, the problem of the proper distribution of total
cost between commercial and mail traffic must be considered to arrive
at an equitable rate system. It is conceivable that under certain pecu-
liar circumstances a monopolistic rate for commercial traffic might be
justified under these conditions, but in many cases such a rate policy
would involve placing an undue burden on this traffic.

It has been noted that in the above-discussed cases the question
of the appropriate mail rate and revenue has not been considered by
the Board—and properly not, because under a general rate policy of
maximizing net revenue or minimizing net loss before mail pay, the
problem does not arise: to put it another way, the assumption is that
the appropriate mail payment is the smallest possible. It has also been
suggested, however, that a commercial rate policy aimed at conformity
to cost would immediately bring up this problem. It is now submitted
that the appropriateness of the former policy can itself not be deter-
mined unless it is first known whether or not the service is more than
capable of being supported by total demand—including both com-
mercial and mail. The problem of the determination of the legitimate
mail payment is seen, therefore, to be a basic one in connection with
the regulation of commercial rates. The second part of this study will
be concerned with this problem.