STATEMENT OF CLAUDE S. BRINEGAR, SECRETARY OF TRANSPORTATION, BEFORE THE HOUSE COMMITTEE ON INTERSTATE AND FOREIGN COMMERCE ON THE TRANSPORTATION IMPROVEMENT ACT OF 1974, MARCH 26, 1974.

Mr. Chairman and Members of the Committee:

I appreciate this opportunity to meet with the Committee to discuss the Department's proposed railroad legislation, the Transportation Improvement Act of 1974, H.R. 12891.

The date of today's hearing is perhaps a good omen. It was exactly one year ago today that the Department submitted, in response to P.L. 93-5, our report on the northeastern rail problem. At that time the Nation was facing a major transportation crisis--the threatened shutdown of rail service across a significant portion of the country. From the modest beginning of our March 26, 1973 report, Congress responded, in time, with the Regional Rail Reorganization Act of 1973.

Our urgent task now is to shift our perspective to the national scene. If we are to avoid future "Penn Centrals," it is critical that action be taken to improve conditions throughout the rail industry. The gains to the Nation from doing so are enormous, while the costs of failing to act could be appalling. The legislation we have submitted is designed to start on the road to the necessary strengthening of the Nation's private sector railroad system, thus avoiding a replay of the northeastern rail crisis in the rest of the country.

No one challenges the fact that a healthy, progressive railroad industry is a great national asset. Rails are a low-cost, energy efficient and environmentally sound form of transportation. Unfortunately, the railroad industry--with its 200,000 route miles of track--suffers from a series of problems which prevent it from providing the full measure of high quality, low-cost service of which it is capable. As a consequence, we all suffer; rails, shippers, consumers and the national economy.

The financial and operating condition of the railroad industry reflects its troubled state. Net profits for its 73 Class I carriers (those with annual revenue of $5 million) are less than 2 percent of equity. Many railroads cannot generate sufficient earnings to make needed improvements in track, roadbed and facilities, while funds from outside sources are not available or only on onerous terms. As a consequence, a substantial part of the total rail industry in the U.S. is in a state of serious deterioration. This crisis is as real and as important as the crisis of the 8 insolvent railroads in the northeast which we faced last year. Many, many miles of line are subject to "slow orders," and on some lines the maximum safe speed is less than 10 mph. The railroad industry, furthermore, is burdened by many miles of uneconomic lines which they are forced to operate at a loss. On the other hand, parts of the railroad system are operating at or close to capacity, but, because of lack of financial resources, the needed expansions cannot take place.

In short, the railroads are in a mess. Low earnings are depriving them of the ability to make improvements in plant which are needed to reduce costs and improve service. But the inability to reduce costs and improve service hampers their competitive position, thus cutting into net income--so the cycle is repeated. If we are to revitalize the railroad industry and achieve the full measure of benefits which healthy, progressive railroads can offer, we must break this cycle. We have neglected the railroad industry too long. The costs of continued neglect could be enormous.

Clearly, a major cause of the railroad industry's problems is an outmoded, overly restrictive Federal regulatory policy. This policy, which has its roots in the 19th Century, has seriously hampered the railroads' ability to adapt to changing economic and competitive conditions in the transportation industry. It has hindered the industry in innovating new services, in responding to competitive conditions in transportation, in attracting traffic on which railroads have a competitive advantage, and long delayed the abandonment of lines that are clearly uneconomic. As a consequence, the railroad industry is not operating at anywhere near maximum efficiency, nor making its proper contribution to the national economy. The outdated regulatory system is not only sapping the vitality of the industry, but threatening its long-term ability to function as a viable, privately-owned system. An industry that handles a third of the Nation's freight tonnage cannot be permitted to slide into the morass of nationalization.

I recognize that this Subcommittee has previously been responsive to the need for legislative action to meet the railroad industry's problems. In the 92nd Congress, this Subcommittee held hearings on various bills which dealt with the railroad industry and the Subcommittee reported out favorably on the Surface Transportation Act of 1972. A similar bill, the Surface Transportation Act of 1973, H.R. 5385, was introduced by Congressman Adams on March 8, 1973.

We now propose to build on this fine past work with the "Transportation Improvement Act." While we regard STA as positive legislation, we see the need for a broader approach to the railroad industry's long-term problems than the STA provides. In our view the STA simply does not deal sufficiently with the basic problem—the need for fundamental regulatory reform. As this is the basic area of difference between the TIA and the STA, I will focus my comments on the particular regulatory reforms proposed in the TIA.

We see improvements in the ratemaking system as the cornerstone of the regulatory reform provisions in the TIA. The current system of rate regulation severely limits an individual railroad's freedom to establish rates. As a consequence, it has created serious rigidity and distortions in the railroad rate structure. It has discouraged experimentation with new service, hindered the introduction of new service, and prevented railroads from adapting to changing economic and competitive conditions. In particular, it has prevented railroads from attracting traffic on which they have a relative economic advantage. Our bill makes a number of changes in the existing pricing rules as a means to improve the efficiency with which transportation resources are used. Let me review these provisions for you.

The bill provides that a rate decrease may not be found unlawful under Section 1 of the Interstate Commerce Act on the ground that it is unjustly or unreasonably low unless it is below variable cost. Under today's practice, rates may be found unlawful on the grounds that they are too low, even though the rate is compensatory. This provision would encourage railroads to reduce rates on traffic where they have a cost advantage.

The bill also modifies the existing law with respect to suspension of rate changes under Section 1 by providing that a proposed rate increase may not be suspended as being unjustly or unreasonably high if it is below the applicable class rate. With respect to rate decreases, the bill provides that a rate may not be suspended on the grounds that it is unreasonably or unjustly low. However, all of the other grounds for suspension which exist in the Act today under sections 2, 3 and 4 would remain. These changes in the suspension provisions of the Act should encourage railroads to reduce rates on traffic where they have a cost advantage and permit them to increase rates where necessary because of higher costs.

The bill also provides a procedure for initiation of rates involving the development of a new service involving a capital expenditure of $500,000 or more. This provision is designed to reduce the delay and uncertainty associated with the introduction of new services, and thereby to encourage experimentation and the introduction of service innovations.

The bill also directs the Interstate Commerce Commission to raise all rates which are below variable cost to the variable cost level. We estimate that the railroad industry loses something in the order of $500 million annually in handling traffic at rates below variable costs. Such rates are a serious financial drain on the carriers.

The present regulatory process has also resulted in the rates of one mode being held too high to protect another mode. The bill prohibits the ICC from holding the rates of a carrier of one mode up to a particular level for the purpose of protecting the traffic of a carrier of another mode, so long as the rate in question is not below variable cost. This provision should lead to more competitive and cost-related intermodal pricing and introduce greater rate flexibility into transportation ratemaking. The net result should be a more economic division of traffic and more efficient use of transportation resources.

Complementing these various changes in the area of ratemaking, the bill makes a number of changes with respect to rate bureau practices. Although rate bureaus provide a number of valuable services to their members and to the shipping public, they also dampen competitive forces in the ratemaking process and discourage pricing flexibility and service innovation. As a result, they have interfered with the establishment of rates based on the cost of the most efficient carrier, and have provided a mechanism through which carriers seek to set and hold rates above a competitive level.

The bill prohibits railroad rate bureaus from voting on single line movements and limits consideration of joint line rates to those railroads which actually participate in the joint movement. The bill also prohibits rail rate bureaus from taking any action to suspend rates established by independent action, while prohibiting motor carrier or freight forwarder rate bureaus from protesting a rate filed by independent action unless the protest is supported by facts showing that the rate appears to be not compensatory.

The bill also requires all rate bureaus to dispose of proposed rate changes within 120 days from the time a rate change is proposed to the bureau. In addition, the bill requires all rate bureaus to maintain and make available for public inspection records of the votes of members. These provisions are designed to bring about speedier rate bureau treatment of proposed rate changes and to encourage greater initiative by individual carriers in making rate changes.

The basic thrust of the proposals is to remove the inhibiting influence of the rate bureaus on ratemaking and to place greater reliance on competitive market forces. I am confident that this will result in a more economic division of traffic, a lower overall freight bill, and improved service and lower cost to the consumer.

In addition to the regulatory reform provisions of the TIA which I have discussed, the bill contains a number of other important provisions. Many of these provisions are similar to those in the STA. The bill would speed up abandonment procedures and provide a more precise and appropriate standard for abandonments. The bill would also require the ICC to prescribe uniform methods and criteria for estimating the rate of return on capital. The ICC and this Department would be required to recommend new uniform cost accounting and revenue accounting methods. Discriminatory local taxation--a problem which results in the railroad industry's annually paying some $50 million in excess taxes--would be prohibited. The bill would also prohibit subsidized rates for government shippers and make needed improvements with respect to intrastate ratemaking. The bill also authorizes the Secretary of Transportation to design a national rolling stock scheduling and controlling system. All of these provisions are discussed in detail in the Analysis of the Need for the Bill, which is attached to my testimony. They complement the provisions of the bill which I have discussed and will help improve the operating conditions and performance of the railroad industry.

The regulatory reform changes and the other provisions which I have discussed are critically important to resolving the railroad industry's problems and improving its prospects. But, regulatory reform alone is not enough. There is also the need to provide financial assistance to the railroad industry. Because of the industry's low rate of return, many railroads are simply unable to generate adequate funds to make needed capital improvements. On the other hand, the investment community has been reluctant to provide external capital to the industry because of the heavy level of existing liens on rail properties. As a consequence, needed improvements in rail plant and additions to rolling stock are not being made. The failure to make these improvements means that opportunities for productivity increases, cost reductions and service improvements are being lost.

Our bill would provide $2 billion in Federal loan guarantee authority to finance improvements in rights-of-way, terminals, rail plant facilities and rolling stock. The conditions tied to the guarantees would assure that the capital improvements and additions to rolling stock would make a significant contribution to overall efficiency of rail operations. Thus, the loan guarantee provisions of the bill are designed to encourage needed long-term restructuring of the existing national rail system.

Mr. Chairman, although the private-sector railroad system in the United States is experiencing difficulty, it is not dying. It is struggling hard for survival under most difficult conditions. Clearly, the time has come to take firm steps to reverse the decline and put it back on the road to health. Unless we take such action now we are inviting further deterioration, future Penn Centrals, and the eventual need for major public funding of the railroad industry. In the long run, this could lead to only one result--nationalization.

This legislation provides the new direction needed to avoid that result: We must modernize the regulatory process—moving it into the latter half of the 20th Century—and help the railroad industry in making needed improvements in plant and facilities. The Nation stands to gain enormously as a consequence.

Mr. Chairman, this completes my prepared statement. My colleagues and I would be happy to attempt to answer your questions.