STATEMENT OF RICHARD F. WALSH, DIRECTOR, OFFICE OF ECONOMICS AND PUBLIC INVESTMENT, U.S. DEPARTMENT OF TRANSPORTATION BEFORE THE WATER RESOURCES SUBCOMMITTEE OF THE SENATE ENVIRONMENT AND PUBLIC WORKS COMMITTEE, JUNE 16, 1981

Mr. Chairman, Members of the Committee:

In my prepared remarks today, I want to address three matters:

(1) First, the role of cost recovery in national transportation policy;

(2) Second, the status of the Section 205 Waterway User Charge Study; and

(3) Finally, the likely impacts that various user charge approaches could have on existing traffic patterns and, hence, on waterway shippers, waterway carriers, and others most directly affected.

As you know, the Administration has proposed legislation for the recovery of Federal costs on the improved inland waterway system of the United States from the commercial users of that system. Let me summarize the chief features of the Administration's bill's chief features as background for my discussion of why it deserves your early and favorable consideration.

The bill provides for the recovery of the Federal government's costs for operating and maintaining navigational facilities on inland waterways. We are proposing to recover 100 percent of operations and maintenance (O&M) costs and 100 percent of the cost of constructing new facilities. We do not propose to recover any past expenditures for projects completed prior to October 1, 1981. In recognition that these waterway improvements and services benefit other groups besides commercial navigation interests, the Federal cost recovery goals for projects authorized only for navigation have been arbitrarily reduced by 10 percent, a generous provision in view of the fact that few, if any, of these improvements or services would ever have been provided were it not for the needs of commercial navigation.

Many different types of fees or charges could be used to recover the government's costs, for example, fuel taxes, lockage fees, license fees or weighbill charges based on ton miles of movement. There are other possibilities as well. The Administration's bill provides that the Secretary of the Army will establish the actual fees and charges to be used, following an informal rulemaking process. In doing so, he will consult with the Secretary of Transportation who will provide advice from the viewpoint of overall national transportation policy. The Departments of Commerce and Transportation will also advise on the impacts of different user charge approaches, drawing on work that has been done in the study mandated by Section 205 of the Inland Waterway Revenue Act of 1978. In developing these user charges, the Secretary of the Army will strive to strike a balance between the goals of matching the user charges with the actual costs of the individual river segments on the one hand and avoiding excessive disruption of existing traffic patterns on the other.

National Transportation Policy and the Recovery of Federal Costs

The recovery from users of Federal costs of building and operating public facilities has long been established and accepted as sound public policy, especially in the field of transportation. Both the Congress and the Executive, in law and in executive order, have again and again confirmed that policy. In most modes of transportation which make use of Federally-financed facilities--the aviation and highway modes, for example--the cost recovery principle has long been honored.

The exception, of course, has been the inland waterway system. Despite repeated proposals, dating back more than forty years, cost recovery did not come to this mode until three years ago with the enactment of the Inland Waterway Revenue Act of 1978. (The St. Lawrence Seaway, it should be noted, has always recovered full operating and maintenance costs.) This law provided for a fuel tax on commercial barge operations, starting at four cents a gallon last October and rising to ten cents a gallon by FY 1985, and created an Inland Waterway Trust Fund. Although its recovery level is modest in relation to the level of Federal outlays, this Act was a particularly important step forward in that it established that the principle of cost recovery should apply here too. To underscore this, the Congress directed that a study be undertaken to provide information on which to base a permanent cost recovery system.

Two major concepts underlie the cost recovery principle. One has to do with the matter of fairness or equity in the distribution of the Federal tax burden. It seems to be only simple justice that profit-making businesses should pay for the facilities they use rather than having the general taxpayer bear their costs. There is just no good reason for government, i.e., the taxpayer, to subsidize such operations, unless it serves truly overriding national objectives. In the case of a profit-making, freight-carrying mode, it is difficult to see what that objective could be, save for that of regional development.

However, no waterways currently under construction have been specifically authorized for regional development.

The other basic concept relates to the effective functioning of the free marketplace as the mechanism which should decide how much and which traffic should go by each mode. When not distorted by subsidy or arbitrary regulation, the marketplace lets shippers decide how much of which commodity they will ship by which mode, with decisions based solely on each mode's respective cost and service characteristics. In order that the market mechanism be a truly efficient decisionmaking device, the transportation rates that face the shipper as he makes his decisions must accurately reflect the costs of each mode. To the extent that any portion of a carrier's costs are picked up by the Federal government, the rates that he quotes will understate the true cost of moving goods by that mode.

Whenever part of the true costs of any mode becomes masked by subsidy in this way, inefficiencies begin to occur. Real efficiencies in other modes are lost as traffic shifted by the artifically low rates of the subsidized mode actually moves at greater total costs.

I am well aware that many critics of the Administration's bill will agree to these principles but feel that they are not being applied consistently and evenhandedly to all modes. Indeed, some have argued that the waterway operators are being singled out for especially harsh treatment while other modes would continue to be subsidized. This is not the case. As far as the freight carrying modes are concerned, the Administration has only one policy--100 percent cost recovery. Let me review this position with respect to the waterways' competitors, the railroads and the motor carriers.

The Federal highway program has been on a 100 percent cost recovery basis since the 1930's. Admittedly, there is an open issue in the financing of the Federal highway program, and that is whether the 18-wheel, diesel tractor trailers are paying their fair share. Many argue that owners of automobiles and light trucks are paying too much, while heavy trucks are paying too little, of the highway system's costs. However, the Administration is now completing a Congressionally-mandated study of the allocation of Federal highway costs, and recommendations to the Congress on this issue can be expected early next year. If it is found that heavy trucks are being cross-subsidized by other highway traffic, rest assured that an increase in user charges for the larger trucks will be forthcoming.

The policy towards the freight carrying railroads is equally clear, and that is "no subsidy." To this end, the Administration is pushing hard to terminate any subsidy to Conrail. We are optimistic that the Congress is going to go along with us and that within a couple of years Federal subsidies to freight operations in the Northeast will disappear.

Over the last few years, some Federal financial assistance in the form of loans has been extended to certain marginal, Midwest rail carriers. Some of these loans may not be fully repaid. Nevertheless, the policy goals of these loans are consistent with the cost recovery principle. They were made with the objective of facilitating and speeding up the reconstruction and rationalization of an oversized rail system. Indeed, the government strongly resisted efforts to provide for continued operation of unneeded portions of the Rock Island and Milwaukee Railroads. The Department's whole aim in the upper Midwest has been to put the rail system on a self-sustaining basis so that permanent Federal subsidies will not be required.

Let me make one final point about the railroads. A number of people have raised questions about past Federal aid to the railroads in the form of 19th Century land grants, emergency loans, grade crossing programs, and so forth. But I submit that this is not a particularly helpful way to view this matter. At one time or another every mode has received substantial public support when the public policy objectives of the day, for whatever reason, was to promote and encourage the growth of that mode. The opening of the West, the economic development of depressed regions, emergency transitional assistance to maintain vital transportation services--whatever the wisdom of the specific decision--these were all legitimate public policy objectives that didn't and shouldn't have had anything to do with the principle of full cost recovery over the long run for all modes.

Today, we are no longer in a developmental or promotional posture with respect to any mode.

Let me repeat, and underscore, that the proposal at hand does not ask for retroactive recovery of past outlays or subsidies for completed projects. In the Administration's waterway user charge bill, the cost recovery goal applies only to current and future expenditures for operations and maintenance and for new capital outlays amortized over the lifetime of a project.

In setting cost recovery policies across all modes, the only useful and fair thing to do is to look ahead and establish consistent and equitable policies for the future, and not try to sort out who got what from whom in the past and whether the result met some idealized standard of intermodal equity.

In summary, that the simplest, most straightforward, evenhanded policy will serve us best in the long run: full cost recovery from all the competing freight transportation modes; no permanent subsidy for any of them; and the quickest possible shift to this status as can be achieved.

Status of the Section 205 Waterway User Charge Study

In the Waterways Revenue Act of 1978, the Congress directed that the Secretaries of Commerce and Transportation undertake a study of waterway user charges and report back by September 30, 1981, as to its findings. Two contractors were engaged to assist in the collection of data, surveys of waterways carriers and shippers, and the analysis of various types and levels of user charges.

This work is now nearing completion. The data collection and survey phases are over, and various user charge approaches are now being analyzed in terms of their impacts and effects on a wide range of variables. The Department of the Army has been working with the study team and the study contractors very closely in these final phases.

The preliminary model runs of various user charge scenarios have been made, and we will be refining them over the next few weeks.

Looking to the future, we expect to have a draft final report of the study ready for circulation and review within the Executive Branch by the end of August. The report should be in the hands of the Congress by the statutory reporting date, September 30, 1981. We will, of course, be delighted to share all useful interim results or study products with the Committee and its staff to faciliate your timely consideration of our legislative proposals.

Preliminary Impact Analysis Findings

Let me now turn to the preliminary estimates we have so far been able to make of the impact of user charges on waterway traffic. Let me emphasize that the results of the analyses we have been conducting for the past year are just now becoming available. The figures I will be offering you are based on the first series of computer runs. I am pleased to share this information with you, but I must note that changes could occur in the next sets of computer runs. Further, we do have flexibility to change some of the assumptions on which these calculations are based and, working with the Department of the Army, to analyze several different user charge alternatives or combinations thereof.

The immediate recovery of 100 percent of Federal operations and maintenance costs for inland waterways does produce quite noticeable changes in modal shares. Nonetheless, the future volume of barge traffic will be considerably higher than it is today under any scenario. Let me explain why this is so.

Over time, barge traffic can be expected to grow at a fairly steady rate. This will be true with or without user charges, and after a period of adjustment the rate of growth should be the same in both cases. User charges do cause shifts in traffic between modes and thereby will reduce the traffic base of the waterways from which future growth will occur, but that growth will continue to take place. In the scenarios we have examined so far, the expected 1990 barge traffic will be 40 percent greater than in 1977, even with full cost recovery.

So far, we have not done the coumputer runs that estimate the regional economic impacts of user charges. We have, however, learned enough from the first runs on modal traffic shifts to offer some preliminary conclusions on the ultimate economic impacts. The two most important commodities moving on the waterways are coal and grain. Coal movements appear to be only slightly affected. However, it does appear that there will be definite impacts on some grain farmers, expecially those located near the river. The removal of the subsidy on transportation that these farmers have long received could add something in the range of three to ten cents to the costs of shipping a bushel of grain from the upper mid-west to New Orleans.

A major factor in estimating the changes in modal shares that result from user charges is the assumption that one makes about the response of the railroads to barge rate increases. Our early computer runs assume that the railroads will not raise their rates at all in response to any user charge induced increase in barge rates. Using this assumption maximizes the estimate of likely modal shift. It seems virtually certain, however, that it is not a realistic assumption, and we will also be making model runs which assume higher rail rates. While we have no way of predicting with certainty what the railroads' likely response will be to higher barge rates, we do believe it will be somewhere between a fully matching increase of all water-competitive rates and no response at all. Thus, to the extent that railroads hold rates where they are in order to gain traffic and modal share, the impact on shippers is minimized, although the effect on carriers is the greater. In this connection, let me note that there is currently more than ample rail hopper car capacity in the Midwest to move any increase in grain traffic. Over 25,000 jumbo covered thousand hopper cars are currently idle and many rail carriers are offering discounts in order to secure traffic.

In assessing the near-term impacts of user charges, it is important to look at the assumption that we have made regarding the extent to which barge operators pass through the charges to shippers. In our analysis we have assumed 100 percent pass through. We believe that is the only reasonable assumption to make in an impact analysis of this type. We also believe that it is the right assumption for the medium and long term. For the first few years, however, we think it is unlikely that the barge operators will actually pass through 100 percent of increased costs. We expect that barge operators would probably absorb some portion of the user charges in order to hold up revenue levels, albeit at a reduced profit. With rising traffic revenues over time, and the opportunity to rationalize the barge fleet, operators would eventually be able to pass through the user charges. Thus, the effect of this assumption that user charges are all passed on is to overstate the amount of traffic shifted in the near-term.

Let me discuss a couple of factors which may tend to reduce the impact of user charges in the longer term. With respect to grain traffic, unit train facilities are likely to be built closer to the river in order to take advantage of lower rail rates for shipment either to Houston or to West-coast ports. The effect of this would be to increase the number of grain shippers able to take advantage of unit train discounts.

Rising traffic volume over time will also soften the impact of user charges. Other things being equal, the more traffic there is on the river, the lower the user charge required per ton of the waterway traffic. Major new investments, in the farther out years that are not cost effective, would, of course, have a tendency to offset this effect. Investments that meet a rigorous benefit cost test would increase traffic.

In summary, let me emphasize again that we are working with preliminary results and there could well be changes as we go forward. The overall picture that is emerging is that full cost recovery use charges do not have truly drastic impacts, but that there would be some definite and noticeable changes in traffic patterns and shipping costs. Some grain shippers will definitely feel the higher costs. However, a growing volume of grain will continue to go into export on all modes. Coal traffic, as noted earlier, will be only slightly affected. Overall, the economy is gaining as the new traffic patterns reflect more efficient use of the transportation system.

Before closing, let me say that we are glad to have this opportunity to share this information with you. We will be pleased to make more detailed information available to the committee and to keep the staff informed as the study continues to develop.

Thank you very much. I will be happy to try to answer any questions.

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