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THE INTERSTATE COMMERCE ACT, ADMINISTERED CONTRACTS, AND THE ILLUSION OF COMPREHENSIVE REGULATION

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The 125th anniversary of the Interstate Commerce Act[1] invites reflection on what it has contributed to our understanding of public regulation. Perhaps the most important and enduring idea associated with the Act is what we may call the administered contract.[2] At common law, transportation services, like other goods and services, were governed by ordinary contracts between customer and carrier.[3] Building on innovations in English and state railroad legislation, the Interstate Commerce Act developed a different form of contracting. Contracts for transportation services became public acts, understood to have the openness, generality, and binding force of public law.[4] This concept of the administered contract soon spread to other public transportation and utility services. It remains a feature today of what we loosely call public utility law.[5] Ironically, rail transportation, where it all began, has reverted to ordinary contracting. This aspect of the history of the Interstate Commerce Act—the rise and fall of the administered contract—tells us much about why the Interstate Commerce Act, despite all its flaws, was so widely emulated. It also sheds important light on the appropriate domain of private and public law in the provision of services to customers.

Ordinary contracts are obligations based on mutual assent between

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1. Ch. 104, 24 Stat. 379 (1887).

2. The term is not common in the law but is useful. *Cf.* Victor P. Goldberg, *Regulation and Administered Contracts*, 7 BELL J. ECON. 426 (1976).

3. *See* James B. Speta, *A Common Carrier Approach to Internet Connection*, 54 FED. COMM. L.J. 225, 253–58 (2002) (describing common law duties of common carriers).

4. *See* Interstate Commerce Act § 6, 24 Stat. at 380–82.

5. *See* Joseph D. Kearney & Thomas W. Merrill, *The Great Transformation of Regulated Industries Law*, 98 COLUM. L. REV. 1323, 1335–40 (1998).

identified persons.[6] They are private undertakings in two senses. First, they see the light of day only under special circumstances, such as a litigated dispute or public recordation to perfect a security interest. Second, the obligations that such contracts create are personal to the parties and ordinarily do not extend to third parties, except in unusual circumstances such as third-party-beneficiary contracts. Ordinary contracts are enforced by courts and arbitrators, seeking to identify the parties' agreement and to enforce it by its terms.[7] Courts and arbitrators typically do not consider questions of social welfare or regard themselves as free to rewrite contracts in order to achieve a different outcome from the one agreed upon by the parties.

Administered contracts, like ordinary contracts, are grounded in mutual assent. A service provider offers service on stated terms and conditions; if a customer agrees, this creates an obligation binding both parties. Nevertheless, administered contracts differ from ordinary contracts on many dimensions. Unlike ordinary contracts, administered contracts are public undertakings. They are filed in "tariffs" or "schedules" with an administrative body, and these tariffs must be posted in public places or otherwise made available for public inspection.[8] Administered contracts are public in a second sense as well: They are regarded as offers open to any member of the public. Although an offer of service may be designed to meet the needs of a single customer, once the proposal is filed as a tariff, any person is free to avail himself of the service on the same terms and conditions.[9]

Perhaps most significantly, administered contracts are understood to be public obligations. Some of this is inherent in the preceding point: Once a service provider agrees to offer service on stated terms and conditions, and these are filed in a public tariff, the service provider is obligated to provide the service if it is requested. Indeed, failure to provide the service when requested is a violation of law.[10] But even more strikingly, enforcement of the contract is not given to courts, at

6. 1 RICHARD A. LORD, WILLISTON ON CONTRACTS § 1:1, at 10–11 (4th ed. 2007).

7. *See, e.g.*, *id.* § 1.1, at 7–8 (collecting authorities); Stolt–Nielsen S.A. v. Animalfeeds Int'l Corp., 130 S. Ct. 1758, 1774–75 (2010); Twin City Pipe Line Co. v. Harding Glass Co., 283 U.S. 353, 356 (1931).

8. *See, e.g.*, Interstate Commerce Act § 6, 24 Stat. at 380–82; *see also* 1 HENRY S. DRINKER, JR., A TREATISE ON THE INTERSTATE COMMERCE ACT §§ 238–250, at 353–70 (1909) (describing tariff requirement).

9. *See* DRINKER, *supra* note 8, at 354 & n.69.

10. *See, e.g.*, ICC v. Delaware, Lackawanna & W. R.R., 220 U.S. 235, 252–56 (1911).

least not exclusively, but is subject to oversight and modification by a public administrative body.[11] Such an agency typically has the power to review tariffs before they take effect for compliance with general legal requirements and to reject or modify tariffs found to be noncompliant. The agency can also bring civil enforcement actions and even initiate criminal proceedings against persons who provide services without a publicly filed tariff or who provide services or pay rates that deviate from the publicly filed tariff.[12]

Finally, administered contracts are public obligations in the sense that they preempt contrary state law. This feature of administered contracts is called the "filed rate doctrine."[13] The service provider and the customer may not mutually agree to deviate from the tariff on any dimension—that is, they are prohibited from modifying the tariff by an ordinary contract.[14] And the customer may not bring an action in tort to recover for any loss or damage that has been disclaimed by the tariff.[15] This feature highlights the degree to which administered contracts function as an alternative to private ordering through the common law.

The concept of the administered contract emerged from the central purpose of the Interstate Commerce Act, which was to prevent "discrimination" in the provision of rail service.[16] The principal cause of complaint against railroads was the perception that some customers were getting better deals than others for what were perceived to be similar services. Specifically, high-volume, well-connected customers,

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11. *See, e.g.*, Interstate Commerce Act § 11, 24 Stat. at 383 (establishing the Interstate Commerce Commission); *id.* § 13, 24 Stat. at 383–84 ("[A]ny person . . . complaining of anything done or omitted to be done by any common carrier subject to the provisions of this act in contravention of the provisions thereof, may apply to said Commission by petition . . . ."); Texas & Pac. Ry. v. Abilene Cotton Oil Co., 204 U.S. 426 (1907) (concluding that, even where shipper complaining of an unreasonable rate had the statutory option of complaining to either a federal court or the Commission, the former must refer the question of reasonableness to the latter, and thus creating the primary jurisdiction doctrine).

12. *See, e.g.*, Jurgen Basedow, *Common Carriers—Continuity and Disintegration in U.S. Transportation Law*, 13 TRANSP. L.J. 1, 27 & n.160 (1983) (citing Interstate Commerce Act provisions).

13. *See* AT&T v. Central Office Tel., Inc., 524 U.S. 214, 221–24 (1998) (and cases cited).

14. *See, e.g.*, Interstate Commerce Act § 6, 24 Stat. at 381 ("[W]hen any such common carrier shall have . . . published its rates . . . , it shall be unlawful for such common carrier to charge . . . a greater or less compensation . . . than is specified in such published schedule of rates . . . .").

15. Keogh v. Chicago & Nw. Ry., 260 U.S. 156, 163 (1922) ("The rights as defined by the tariff cannot be varied or enlarged by either contract or tort of the carrier."); *see also AT&T*, 524 U.S. at 226–27; *Abilene*, 204 U.S. at 435–48.

16. Kearney & Merrill, *supra* note 5, at 1332 (and sources cited).

such as the oil and steel trusts, were getting breaks that were denied to ordinary folks.[17] The disparity in rates was endemic to the railroad industry, with its mixture of competitive and monopolistic routes.[18] The central problem was how to allocate large fixed costs—such as roadbed, terminal expenses, and administrative overhead—to individual movements. There was no clear answer to this problem. Railroads naturally sought to allocate a higher proportion of fixed costs to shippers on monopolistic routes, like rural grain elevators, which had little ability to resist higher prices. Railroads sought to allocate a smaller proportion of fixed costs to high-volume shippers like the oil and steel trusts, which typically had access to multiple transportation alternatives and could take their business elsewhere if rates got too high.[19]

One strategy the Interstate Commerce Act took against this perceived inequity was to attack the problem directly, in the form of anti-discrimination obligations, long-haul/short-haul provisions (which forbade charging more for short-distance shipments than for otherwise identical long-distance shipments over the same route), and a general prohibition on unreasonable rates and practices.[20] Enforcement of these substantive constraints, however, was difficult. It was expensive to file a complaint charging a carrier with a violation of these provisions, or to persuade Interstate Commerce Commission ("Commission" or "ICC")

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17. *See* Herbert Hovenkamp, *Regulatory Conflict in the Gilded Age: Federalism and the Railroad Problem*, 97 YALE L.J. 1017, 1046–47 (1988) ("Most scorned and least defended were preferential rates for large favored customers, the most notorious being John D. Rockefeller's Standard Oil Company."); *cf.* Jerry L. Mashaw, *Federal Administration and Administrative Law in the Gilded Age*, 119 YALE L.J. 1362, 1370 (2010) (noting that the monopolistic business practices of people such as Andrew Carnegie in the steel industry helped stimulate the reformist movement that led to the passage of the Interstate Commerce Act).

18. *See* William G. Waters II, *Evolution of Railroad Economics*, 20 RES. IN TRANSP. ECON. 11, 18–21 (2007) (describing the railroad industry's use of differential, or Ramsey, pricing models in which rates vary inversely with the elasticity of demand). *See generally* William J. Baumol & David F. Bradford, *Optimal Departures from Marginal Cost Pricing*, 60 AM. ECON. REV. 265, 277–78 (1970) (reviewing literature and analyzing Ramsey pricing in the railroad industry).

19. *See, e.g.*, ALFRED D. CHANDLER, JR., SCALE AND SCOPE: THE DYNAMICS OF INDUSTRIAL CAPITALISM 56, 93 (1990) ("In [the] oil [industry], . . . competition between railroads increased the power of the large shippers; for the intense pressure exerted upon the railroads by their very high fixed costs led their operators to grant reduced rates . . . for higher-volume shipments.").

20. Interstate Commerce Act §§ 1, 4, 24 Stat. at 379–80.

staff to commence an investigation.[21] Once commenced, proceedings quickly bogged down in complicated evidentiary questions about cost accounting. When courts began to recognize defenses based on "meeting competition," success became increasingly hard to achieve.[22]

A second strategy was the adoption of administered contracts. If railroad service could be procured only through published contracts, these contracts were available to all, and deviations were strictly prohibited, then favoritism would become much more difficult. The regime of administered contracts turned out to be much easier to implement and enforce than the substantive prohibitions against discrimination. The courts, at the urging of the Commission, soon held that any provision of service without a tariff, any failure to file and publish a tariff before providing service, or any deviation from a tariff once it became effective was a per se violation of the Interstate Commerce Act.[23] Railroad employees, shippers, agency officials, and courts could easily understand these rules and the consequences of violating them. Administered contracts did not end differential treatment. Carriers quickly learned to file tariffs tailored to specific endpoints, goods, and volumes, and so could continue to engage in differential pricing based on different competitive circumstances. But at least the plague of secret rebates, kickbacks, and preferences, which was so disturbing to the public in the late nineteenth century, was brought to an end.

The idea of the administered contract was wildly successful.[24] Within the transportation sector, the idea spread from railroads to motor

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21. *See* DRINKER, *supra* note 8, § 299, at 416–17 (noting difficulty of convincing ICC to investigate one's claim).

22. *See* Texas & Pac. Ry. v. ICC, 162 U.S. 197, 233–34 (1896) ("[A]mong the circumstances and conditions to be considered . . . , competition that affects rates should be considered . . . in deciding whether rates . . . are or are not undue and unjust . . . ."); ICC v. Alabama Midland Ry., 168 U.S. 144, 172–73 (1897) ("[W]ithin the limits of . . . good faith . . . and subject to the . . . prohibitions that their charges shall not be . . . unreasonable, and that they shall not unjustly discriminate . . . , the [A]ct . . . leaves common carriers . . . free . . . to adjust and apportion their rates so as to meet the necessities of commerce . . . ."); Louisville & Nashville R.R. v. Behlmer, 175 U.S. 648, 674 (1900) ("[T]he carrier may take into consideration the existence of competition as the producing cause of dissimilar circumstances and conditions . . . ."); *cf.* James B. Speta, *Supervising Discrimination: Reflections of the Interstate Commerce Act in the Broadband Debate*, 95 MARQ. L. REV. 1195, 1198–1200 (2012) (recounting ICC's consideration of context, including existence of competition, in determining whether railroad rates were unlawfully discriminatory).

23. *See, e.g.*, Gulf, Colo. & Santa Fé Ry. v. Hefley, 158 U.S. 98, 101–03 (1895).

24. Kearney & Merrill, *supra* note 5, at 1333–34 (and sources cited).

carriers, intercity buses, river barges, and airlines. It leaped to other industries as various as stockyards, telephony, natural gas distribution, and electricity distribution. It prevailed in a variety of federal regulatory schemes and was adopted by nearly all states as well.

Explaining why the idea of administered contracts was so successful is more difficult. Although the idea got its start in an industry characterized by a mixture of competitive and monopolistic routes, where differential pricing (i.e., "discrimination") was rampant,[25] it proved to be equally popular in industries with natural monopoly characteristics (electricity, natural gas distribution, and local telephony) and in industries that were inherently competitive and were regulated largely to protect some other industry from competition (motor carriers and river barges). So the administered contract was not a regulatory response to any specific industry structure.

Without doubt, administered contracts had some benefits. The device was critical in stamping out the more blatant forms of favoritism, such as secret rebates, and this may have contributed in some measure to public confidence in the fairness of a rapidly industrializing capitalist system. They made it marginally easier to initiate claims of discrimination, since all tariffs were theoretically available for inspection through the agency's public documents room. The reality, as I have suggested, is that even with this better access to evidence, claims of discrimination or long-haul/short-haul violations were very hard to win. Administered contracts made it possible to protest rate increases before they took effect, and to seek a stay from the Commission pending investigation.[26] This probably provided customers somewhat more leverage than they had under a regime that allowed only reparations for rates already put into effect and later deemed unlawful. But whether this had any widespread or permanent effect on the level of prices is questionable. Overall, it is hard to pinpoint any significant tangible benefit associated with the widespread use of administered contracts relative to ordinary contracts.

This is my theory: The regime of administered contracts created the illusion of comprehensive regulation without its associated costs. Forcing regulated firms to file and adhere strictly to tariffs satisfied the public's demand that the government "do something" about abusive

25. *See generally* Waters, *supra* note 18 (providing overview of railroad-industry economics).

26. *See, e.g.*, Arrow Transp. Co. v. Southern Ry., 372 U.S. 658, 667–68 (1963).

practices in various critical network industries. Every firm had to publicize every service offering in advance, and had to wait patiently for a short period (e.g., thirty days) to see if any customer would protest or the agency would suspend and investigate.[27] The public was thus led to believe that the government was on top of the industry. The reality was that all but a tiny percentage of tariff filings piled up, unread, in agency offices and later in warehouses. Meanwhile, the administered-contract regime imposed a small deadweight loss on regulated firms, but preserved their autonomy to determine what services they would offer at what prices. Administered contracts created the appearance of regulation while leaving the significant decisions unregulated, except in the most extreme cases. In so doing, they avoided the sclerosis and inefficiency that would have accompanied any effort to nationalize these industries and run them as state bureaucracies, as happened in most other industrial democracies.[28]

The regime of administered contracts under the Interstate Commerce Act came to an end fairly rapidly in a twenty-year period from the mid-1970s to the mid-1990s.[29] Using "letters of understanding," railroads began soliciting business from major shippers, such as utilities that burn coal provided by continuous-cycle unit trains running from mine head to power plant. When disputes arose in which railroads attempted to argue that such letters were not binding because they were not filed as tariffs, courts were not amused.[30] The ICC soon decided that such letters of understanding were presumptive evidence of reasonable rates and had to be reflected in tariff filings. Administered contracts were effectively subordinated to ordinary contracts. The Staggers Rail Act of 1980 expressly authorized the use of carrier–customer contracts,

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27. *See* DRINKER, *supra* note 8, § 229, at 339–40 (discussing thirty-day waiting period).

28. *See* FRANK DOBBIN, FORGING INDUSTRIAL POLICY: THE UNITED STATES, BRITAIN, AND FRANCE IN THE RAILWAY AGE 3–4 (1994) (contrasting American railroad policy with French nationalization efforts); Hovenkamp, *supra* note 17, at 1031 n.70 ("[M]any European countries had begun to socialize their railroad systems.") (citing ARTHUR TWINING HADLEY, RAILROAD TRANSPORTATION: ITS HISTORY AND ITS LAWS 236–37 (1885)).

29. *See* Thomas K. McCraw, *Economic Regulation*, *in* THE OXFORD COMPANION TO UNITED STATES HISTORY 207, 208 (Paul S. Boyer ed., 2001) (discussing railroad "deregulation" that began in the 1970s); *see also* Ari Hoogenboom, *Interstate Commerce Act*, *in* THE OXFORD COMPANION TO UNITED STATES HISTORY, *supra*, at 393 (same); Kearney & Merrill, *supra* note 5, at 1335–36, 1368, 1386 n.290 (same).

30. *See, e.g.*, Iowa Power & Light Co. v. United States, 712 F.2d 1292, 1295–96 (8th Cir. 1983) (rejecting utility's argument that rate agreed to in letter of understanding did not control because it was not filed as a tariff).

which quickly became the standard mode of doing business in the industry.[31] When the ICC was formally abolished on January 1, 1996, tariff filing ended and rail service contracts were by statute returned to state courts to be treated like ordinary contracts.[32]

What caused the demise of the administered contract in the context of the Interstate Commerce Act? President Eisenhower's interstate highway system may have been the most important cause, with the growth of the air transportation network playing a supporting role. The convenience of the new highway system and the emergence of air travel quickly reduced intercity rail passenger transportation to a detail. The railroads happily turned over all intercity operations to Amtrak, a federally subsidized corporation, in 1970.[33] The vast growth in the transport of goods by motor carriers, along with the development of commercial air freight, meant that most shippers of commercial goods had competitive alternatives to rail transportation, even if, as before, the shippers were served by only one rail carrier.[34] The primary exception consisted of shippers of bulk commodities such as coal, but these sorts of shippers were precisely the types of firms that could negotiate long-term contracts with rail carriers, and there was no reason to believe that administered contracts would provide them with better protection than ordinary contracts.

In short, the administered contract disappeared once widespread dependency on rail transportation disappeared. When the Interstate Commerce Act was adopted 125 years ago, multitudes of agricultural producers and small manufacturers were completely dependent on rail transportation to connect with the outside world, and fear of exploitation by railroads was rampant. The regime of administered contracts helped to tamp down this anxiety, at least to a degree. Once new transportation alternatives—car, motor carrier, and airplane—opened up, the sense of dependency on railroads faded away. It was only a matter of time before the ritual of tariff filing, publication, and

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31. Pub. L. No. 96-448, § 208, 94 Stat. 1895, 1908 (1980).

32. ICC Termination Act of 1995, Pub. L. No. 104-88, § 102, 109 Stat. 803, 817 (codified as amended at 49 U.S.C. § 10709(c) (2006)).

33. Rail Passenger Service Act of 1970, Pub. L. No. 91-518, § 301, 84 Stat. 1327, 1330 (codified as amended in scattered sections of 49 U.S.C.) (creating and empowering Amtrak).

34. *See* Hoogenboom, *supra* note 29, at 393 ("Railroads declined after World War II, partly because minimum-rate regulation prevented them from competing successfully with motor and water carriers. . . . [And] railroads' . . . passenger service . . . had become unprofitable because of airline competition.").

worrying about strict compliance with tariff terms came to be seen as an unnecessary regulatory burden, adding to the cost of rail transport with little or no offsetting benefit.

If this analysis is correct, it suggests that the proper domain of administered contracts should be determined by economic dependency, even though, as noted, administered contracts were sometimes imposed without regard to such dependency. The economic concepts of monopoly or market dominance are a relevant part of the inquiry. But so is a more contextual understanding of vulnerability. Someone is economically dependent on a service when that service is a necessity of economic life and is provided by a single firm or a single dominant firm. Railroads fit this description when the Interstate Commerce Act was adopted. They do not, at least not for the vast majority of economic actors, today. It is thus fitting and proper that the idea of administered contracts, which emerged under the Interstate Commerce Act, has today disappeared from the industry in which it was born.