Michigan Law Review

Volume 29 | Issue 3

1931

CHANGING FACTORS OF REASONABLE RATES

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IN this period of financial difficulties there arise many old familiar problems. Some are inherent in times of "tight" money; some perhaps may be solved once and for all; others may possibly be met in such a way that certain of their bad features will be permanently modified. In this last class seem to be certain problems of public utility financing.

Risk factors furnish the more important stop valves upon the flow of money into investments. To the extent that these risks can be identified and reduced or eliminated in relation to public utilities they will, of course, cease to function as obstructions to proper improvement and expansion in that vitally important field.

Investment is discouraged by uncertainty. Uncertainty is inherent in apparent imminence or possibility of change.[1] Apparent imminence of change is brought about by agitation, and, of course, will dissolve to a great extent with the ending of the agitation. If the present agitation in the utilities field can be terminated in any reasonably sound manner, some investment confidence would, no doubt, return and none can question the great desirability of such a phenomenon at this time.

Something more will be submitted in the following, concerning this matter of agitation, but prefatory to that it seems logical to say something about certain other changing factors of reasonable rates which tend to affect the mind of the owner of money as he ponders utility investments—"To buy or not to buy—that is the question."

Prior to the political movement that culminated in the creation of the present utility regulatory bodies, the "common callings," which were well known in the Year Book period, had practically dwindled

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[1]Some interesting materials which bear upon the problems of the time are the following: Henry C. Spurr, "Will the Public Utilities Be a Major Political Issue?" 6 PUBLIC UTILITIES FORTNIGHTLY 3 (1930); see James Couzens, "Why the Couzens Bill Will Not Undermine the Powers of the State Commissions," 6 PUBLIC UTILITIES FORTNIGHTLY 131 (1930); see also COOKE, M. L., PUBLIC UTILITY REGULATION, pp. 294-295.

to include only the innkeeper and the common carrier. These were subject to the requirement that they serve all patrons who required their services up to the limit of their capacity or facilities to serve. The duty to serve all of the public implied a duty to serve at reasonable rates[2] since if the innkeeper or carrier were allowed to charge any rates which he saw fit to impose upon whatever arbitrary basis he pleased, he could by such means readily defeat his duty to render universal service.

Such was the condition of the law just before the time when the tremendous growth of public utilities in the United States took place.[3] Roughly speaking, this period of expansion covers the era between 1810 and 1910. During that century there were issues of various sorts which led to complaints that the interests of members of the public were not being properly considered by certain

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[2]Lord Hale, "De Portibus Maris," HARGRAVE LAW TRACTS, 78 (ed. 1787); see WYMAN, PUBLIC SERVICE CORPORATIONS (1911) sec. 16.

In an anonymous case, recorded in Godbolt, p. 440, Justice Dodderidge says: "An action upon the case lies against an innkeeper who denies lodging to a traveller for his money, if he hath spare lodgings, because he hath subjected himself to keep a common Inn."

And in 6 Term Reports 14, in the case of Kirkman and Another v. Shawcross (1794), Lord Kenyon, Chief Justice, says: "Innkeepers are bound by law to receive guests who come to their inns, and are also bound to protect the property of those guests. They have no option either to receive or reject guests; therefore I said it was a material circumstance in the present case that these persons had an option either to work or not as they pleased. The case of the innkeeper does not bear any resemblance to the present; for as they cannot refuse to receive guests, so neither can they impose *unreasonable* terms on them. The case of carriers has also been mentioned; but that is not like this. They have no right to say they will not receive any goods but on their own terms; I believe there is an act of Parliament giving power to the Justices at the Quarter Sessions to regulate the price of the carriage of goods." (Italics ours.)

References are made to many interesting, related authorities in BACON'S ABRIDGMENT, tit. "Inns and Innkeepers" (C) 1 and (C) 2 and tit. "Carriers" (B) and (D).

[3]See WYMAN, PUBLIC SERVICE CORPORATIONS, secs. 20-33 (1911).

The practical telephone dates from the work of Bell in 1876, the telegraph from that of Morse in 1844. Gas has been distributed for home use at least since 1812 and electricity for domestic use since 1882. Railroad construction probably started with the Baltimore & Ohio in 1830, and electric railways seem to have started practical operation in 1879.

utility companies.[4] Voters were informed that their interests should be more carefully conserved; that they were being overcharged by the utilities; that they were receiving very poor service from the utilities; that certain combinations in restraint of trade existed among the utilities and that certain rate wars on the one hand and rate operating agreements on the other[5] were equally inimical to their welfare. These ideas had their effect at the polls. Governors, legislators, judges, mayors, and aldermen took office pledged to reduce the rates of the utility companies. Utility regulatory bodies shortly began to make their appearance.[6]

With a new emphasis the proposition was repeated that the patron of the utility was entitled to a "reasonable" rate. Forgotten was the fact that traditionally in the common law the patron was entitled to a "reasonable" rate only because such rule was logically inherent in the requirement that the common carrier and the innkeeper serve all without discrimination.

"Reasonable" rate took on a new meaning. It no longer meant only that there must be no indiscriminate or arbitrary denial or refusal of service. It came to mean more broadly that the interested parties were jointly entitled to a rate which on the one hand did not unreasonably or unlawfully, from an economic point of view, deny to the patron the services of the utility company, and on the other hand was reasonable because of its yielding to the utility investor a fair net return upon the value of the property devoted to the public use.[7]

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[4]See POND, PUBLIC UTILITIES (3d ed. 1925) secs. 618-623. See also supra note 3 and infra note 5.

[5]See RIPLEY, RAILROADS, RATES AND REGULATIONS, pp. 431, 446 (1916).

[6]The state Public Utility and Railroad Commissions nearly all date from between 1895 and 1915. For a list of creative acts see Comparative Summary of Laws relating to the Regulation of Telephone and Telegraph Companies by Commission, compiled by the American Telephone & Telegraph Company, p. 7 (1918).

[7]For expression of the "legal" and the "economic" theories as to rate making see WYMAN, PUB. SERV. CORPS., sec. 1190. Here is "not confusion, but disagreement," says that author. Perhaps sound reasoning should embrace both theories in an age of legal reception of economic ideas. See POND, PUBLIC UTILITIES, n. 3, secs. 445, 618; 3 SPURR, GUIDING PRINCIPLES OF PUBLIC SERVICE REGULATION (1926) pp. 525-557; WYMAN, PUBLIC SERVICE CORPORATIONS (1911) secs. 1060-1069.

At this point it is well to remember that the term "reasonable" suggests a *standard* of law rather than a *rule* or *principle.* We speak of the conduct of the "reasonable man" in a negligence case and there it is always necessary to consider what was "reasonable" under all the surrounding, relevant circumstances. We speak of "fair" conduct of a trustee and here again we are dealing with a standard which requires investigation of all the surrounding circumstances. If the term "reasonable" implies a limitation both upon the "demands" or the "claims," or necessities of the patrons, and also implies limitations upon the powers and privileges of the utility investors, all of the surrounding circumstances bearing upon what may be deemed to be "reasonable" must be considered.[8] Thus a tremendous social and economic field is opened for investigation in each "reasonable" rate issue. From the standpoint of the public there is involved the question: "Is the rate so high that it unreasonably denies to those who would like to patronize it the advantages of the service of the public utility by driving them to some potentially competitive facility?"[9] If the rate is not open to the charge that it is so high that it unreasonably denies the services of the public utility to prospective patrons, it is submitted that the officers of the company should have power to fix it at whatever figure seems suitable to them in view of related business conditions. There may be a considerable difference, or spread, between the high rate which unreasonably prevents some people from patronizing the utility company and that rate which is so low that it can not be imposed upon

[8]"Whether the proper level in the rates authorized has been reached or not greatly depends upon the character of the community served, the ability of the consumers to pay, and the character of the service rendered." Per Commissioner Shaw in Re Central Illinois Pub. Serv. Co. (Ill.) P. U. R. 1919E 910, 913. See Pub. Util. Comm. v. East Providence Water Co., P. U. R. 1927C, 417, 48 R. I. 376, 136 Atl.. 447 (1927).

[9]When the public utility, whether power, transportation or otherwise denies a share of the profit of its existence and service to its patrons, in effect it denies to him its services and its rate requires adjustment. See WYMAN, PUB. SERV. CORP., secs. 1211-1214; cf. infra note 18; In re Arkansas R. Rates, 168 Fed. 720 (C. C., E. D., Ark. 1909). Railroad rates must not "confiscate" goods of patrons in sparsely settled country. But in railroad cases the Commission may not make the needs of the shippers the entire basis of the rates. 3 SPURR, GUIDING PRINCIPLES OF PUBLIC SERVICE REGULATIONS, p. 555. See also 3 SPURR, *op. cit.* pp. 549 *et seq.* (and authorities cited); see POND, PUBLIC UTILITIES, n. 4, sec. 623; see authorities cited supra n. 8.

the company because that would amount to confiscation. But within this field it would seem that the fixing of rates might well be entrusted to the sound business discretion of the officers of the company,[10] and held to be a matter of utility management with which public authorities do not interfere.[11] This would add some certainty to utility investments.

Whether a rate is so high that it unreasonably denies the services of the utility company to prospective patrons, requires an analysis of the social and economic conditions of the city, state, region or other community served by the utility. Relevant to this issue is the question: "How much can the patrons pay?" and "How much should a reasonable man be expected to pay rather than refrain from patronizing the utility and adopting some alternative course?" The question is not, "What are the patrons *willing* to pay?" but rather, "What can the abstract, reasonable man fairly be expected to pay under the existing social and economic conditions?"[12] If it is com-

[10]A rate which leaves no profit to the consumer or leaves a too meager profit would be held to amount to a denial of service, a "confiscation" of his goods or property. Thus a railway company could not starve a community out of existence by charging a rate nearly as high as would enable the former to handle all of its freight, etc., by private truck or similar vehicles. See supra n. 9. See Re City of Milwaukee (Wis.) P. U. R. 1927B, 229; 1 SPURR, GUIDING PRINCIPLES OF PUBLIC SERVICE REGULATION (1924) p. 74 *et seq.*

See Walker Bros. Catering Co. v. Detroit City Gas Co., 230 Mich. 564, 203 N.W. 492 (1925); Coplay Cement Mfg. Co. v. Public Service Commission, 271 Pa. 58, 114 Atl. 649 (1921); City of Hutchinson v. Southwestern Bell Tel. Co., 109 Kan. 545, 200 Pac. 301 (1921); Illinois Bell Tel. Co. v. Commerce Commission, 304 Ill. 357, 136 N.E. 676 (1922); North Hempstead v. Public Service Corporation, 231 N. Y. 447, 132 N.E. 144 (1921); Public Service Commission v. Pavilion Natural Gas Co., 232 N. Y. 146, 133 N.E. 427 (1921); Gillen v. Public Service Ry., 97 N. J. Law 333, 116 Atl. 621 (1922); Duitz v. Kings County Lighting Co., 188 N. Y. S. 67 (Sup. Ct. 1921); Nathaniel T. Guernsey, "State Commission Laws Regulate Rates, Not Profits," 13 VA. L. REV. 257 (1927); William E. McCurdy, "The Power of a Public Utility to Fix Its Rates and Charges in the Absence of Regulatory Legislation," 38 HARV. L. REV. 202 (1924).

[11]See Nathaniel T. Guernsey, "Regulation and Management," 13 IOWA L. REV. 145 (1928).

[12]This is an expression of the economic theory which makes value of the service the basis of calculating the reasonable rate. See WYMAN, PUBLIC SERVICE CORPORATIONS, secs. 1190, 1382-1384; D. F. Pegrum, "Legal v. Economic Principles in Utility Valuation," 6 J. OF LAND & P. U. ECONOMICS 127, 235 (1930). Cases dealing with the importance of the ability of the customer

plained that gas rates are too high, the relative cost and convenience of using gas as a means of cooking should be compared with those factors involved in using gasoline, wood, or electrical stoves or other methods for cooking. If it is complained that electrical rates are too high, there should be made a comparison between the cost and convenience of electricity and the cost and convenience of other methods of lighting. If it is complained that street railway rates are too high, the cost and convenience of that method of travel should be compared with the cost and convenience of travel by automobile or bus.[13] The investigating agency should bear in mind, however, that the standards of luxury, conveniences and necessity change; that that which is now a luxury tends to become a common convenience and may later come to be regarded as a necessity.

Relevant to this investigation would be an examination of the various social features of the community affected—of what races are the various people; what has been their background; could they be induced to use the services or commodity offered by a utility company at an attractive rate?[14] It may be discovered that in a given city fifty per cent of the people do not patronize the utility.[15] This would be an important thing in the city of American or Americanized population who are acquainted with the conveniences offered by the utilities and who may be assumed to wish to enjoy those conveniences.[16] If it is found that this large percentage of Americans are not using gas because they think the rate is too high, that fact, while not alone conclusive, furnishes some persuasion that the rate is unreasonable and has resulted in a denial of the service of the company. On the other hand, if this fifty per cent of the population consisted mainly of recent immigrants from a part of Europe where domestic use of gas is unknown, where people almost exclusively cook by means of wood or coal stoves, the fact that they are

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to pay are cited in 3 SPURR, GUIDING PRINCIPLES OF PUBLIC SERVICE REGULATION 549. See supra notes 7, 8, and 9.

[13]3 SPURR, *op. cit.* 561-563.

[14]3 SPURR, *op. cit.* 537, 539-540, 542, 550, 560, 588, 591, 599.

[15]See Re Arkansas Light & Pwr. Co. (Ark.) P. U. R. 1920D 775; Webster v. Burnett County Light & P. Co. (Wis.) P. U. R. 1924E, 281.

[16]Public Serv. Comm. v. Flathead Valley Elect. Co. (Mont.) P. U. R. 1926C, 822, 826.

not using gas might lose any persuasive power to demonstrate that the gas rates are high.

It is important also to note certain economic conditions. Let us assume that in a given community there is a certain expenditure each month for certain, specific non-necessary articles. The amounts expended for these commodities is likely to be ascertainable to a fair degree of accuracy. Let it be assumed that in this community the expenditure upon these non-necessaries is the same as the amount which will be spent by the community for gas if the rates imposed by the company are upheld. In another community of similar average per capita income the same comparison indicates that gas is relatively twice as high, and that no complaint is being made. The figures, while not alone conclusive, would have some tendency to indicate that the price being charged for gas in the first community is reasonably within the means of the patrons.[17]

It is true that much has been said against the recognition of any relation between a utility rate and "what the traffic will bear," but there is nevertheless some economic truth suggested in that idea which emphatic condemnation can not entirely destroy.[18] Other economic factors are of course relevant—the question whether the community is growing or becoming less populous;[19] the question whether the industries in the town operate throughout the year or are seasonal;[20] the question whether the community is essentially manufacturing, agricultural, educational, or otherwise. It has long been recognized that differences in the character of communities in certain physical aspects may justify differences in utility rates[21]—economic and social differences are fully as important.[22] All of these

[17]Supra note 9.

[18]See Commissioner Shaw in Re Central Illinois Public Service Company (Ill.) P. U. R. 1919E 910. But see WYMAN, PUBLIC SERVICE CORPORATIONS, secs. 1211-1214.

[19]Re Merrill City Water Works Co. (Wis.) P. U. R. 1924D, 131; see 3 SPURR, GUIDING PRINCIPLES OF PUBLIC SERVICE REGULATION 542.

[20]Re Illinois Bell Teleph. Co. (Ill.) P. U. R. 1928E, 279.

[21]Re Long Island R. Co. (N. Y. T. C.) P. U. R. 1928C, 748; Public Service Comm. v. Flathead Valley Elect. Co. (Mont.) P. U. R. 1926C, supra note 16; Re Philadelphia R. T. Co. (Pa.) P. U. R. 1926B, 385; Housewives Council v. Portland R. Light & P. Co. (Or.) P. U. R. 1926A, 53.

[22]Public Service Comm. v. Flathead Valley Elect. Co. (Mont.) P. U. R. 1926C, 822, supra notes 16 and 22; Re Consolidated Gas Co. (N. Y.) P. U. R. 1928E, 19. See the cases cited supra note 21.

ever-changing factors have some relevant bearing upon the question as to whether the rate of the utility is reasonable or is so high that it unreasonably excludes members of the public from the benefits derived by patronizing the public utility company involved in the particular case. The intelligent investor will study all of these factors as bearing upon the rate that must contain his dividends or interest.

"REASONABLE RATE" FROM THE STANDPOINT OF THE INVESTOR

It is generally accepted that a "reasonable rate" will ordinarily yield a "fair return." "Fair" in respect to what? This would mean, from the standpoint of a prospective investor, "fair as compared with other income from invested money." As observed at the beginning of this paper, the factors which enter into the determination of what is a *fair* return upon invested money are nearly all identified with the risks attending the investment.[23]

Money invested in a hazardous business commands a rate of return commensurate with the degree of risk in the enterprise. Thus any risks bearing upon the collection of "reasonable rates" (which the investor thinks of as including operating expenses plus his "fair return") have a direct bearing upon the possibility of obtaining additional capital for investment in the particular utility business. The greater the risk of a failure of dividends, paradoxically, the greater assurance of certainty or high dividends the investor will demand before putting in his money. This is not a perversity peculiar either to the *large* capitalist or to the *large* investor in utility stocks or bonds. The result is that the utilities which need new money all the time for growth have difficulty in obtaining it in the face of unstable factors which may threaten to prevent the collection of what the investor deems to be a "reasonable rate."

The foregoing indicates that the true conception of "reasonable rate" includes two approaches; one from the standpoint of the patrons of the utility and the other from the standpoint of the investor.[24] The social and economic conditions which enter from the

[23]Aluminum Goods Manufacturing Co. v. Laclede Gas Light Co. (Mo.) P. U. R. 1927B, 1; West v. United Rys. & E. Co. of Baltimore, P. U. R. 1928D, 197; Re Holyoke Street R. Co. (Mass.) P. U. R. 1928A, 578; see Bluefield Water Works and Improv. Co. v. Pub. Serv. Comm., 262 U. S. 679, 692-694, 43 Sup. Ct. 675 (1922); D. F. Pegrum, "Legal v. Economic Principles in Utility Valuation," 6 J. OF LAND & P. U. ECONOMICS 127, 235 (1930).

[24]See WYMAN, PUBLIC SERVICE CORPORATIONS, secs. 1190, 1191, 1203, 1213.

standpoint of the patron have been mentioned. From the standpoint of the investor the elements of current rates of return on moneys variously invested in other types of venture and certain risks bearing upon the collection of a rate which will pay costs of operation plus the "fair return" upon the investment will be considered. These risks or *changing factors,* which figure in the calculations of any well informed investor, are numerous and a modest attempt to catalogue some of them follows.

Risks Attending Investment in Public Utility Enterprises

There is ever attendant upon new enterprises a risk of failure and its very presence when studied makes clear to some degree the conduct of the financiers of the early railroads in demanding large bond bonuses to protect stock investments and partly explains the so-called "wildcat" financing of the times.[25] Against the risk of losing his entire investment the investor demanded a large share in the winnings if the investment turned out well. While conditions in the early periods of the development of the other utilities were similar, they have not been so much commented on for three reasons. First, the degree of success which might be confidently expected could be closer estimated in connection with the municipal utilities; that is, they were a little less speculative in character; secondly, the amount of the investment was usually less; and thirdly, the business of each railroad touched many communities in a general way while the business of the local utility did not.

The investor also assumes his share of the risk that after a time of success the business may become obsolete or fail for exhaustion of either a commodity upon which it depends or of decrease in the population which the utility serves. The operation of this risk is seen in the many rusting street car tracks in the smaller cities of the United States; the defunct natural gas pipe lines in some parts of the country; the old railroad spurs or branch lines from which the rails and ties have been removed and which are growing up to burdock, Johnson grass and cockle-burrs. Here and there a power plant stands idle while electricity comes into the community over a high-voltage transmission line and many utilities of other types

[25]See Ripley, Trusts, Pools and Corporations, (Rev. ed. 1916), Introd. at p. xxiii *et seq.*

have closed or sold their properties to close up their business with a capital re-distribution of but a few cents on the dollar. The success of railroads today is menaced by air traffic and bus and truck lines, and every utility which depends upon inventions is subject to the risk that there will be superseding inventions.

The obvious risk of poor management which runs the gamut from poor judgment to downright embezzlement with all of its tragic possibilities will be passed over to reach a group of more serious risks.

These may be gathered under the general heading: Risk of Governmental Interference.

Whether a utility is being operated efficiently or carelessly; whether collecting high rates or low; whether making a large net profit or none, it is subject to investigation and regulation. In some instances unjustifiable attacks have been made on utilities by perfectly honest, but misinformed men. On the other hand certain speakers may be suspected of making attacks without any real confidence in their charges but merely to stir up public interest in themselves.

Some utilities have tried to shut off such attacks by making various contributions. This meant that avoidance of the subject of public utilities could be obtained only by contributing to many and various funds. Such donations, when commented on, either directly or by innuendo, have been given the character of bribery and corruption.[26] The solution of this difficulty would seem to be that utility companies and owners cease to give to any funds, political, religious or otherwise, directly or indirectly. Some who have learned to depend upon utility company donations may resent the adoption of such a policy. But those who are fair will understand it; those who are not, should be frankly and openly met, if they adopt actively hostile attitudes.

Another, more direct risk of governmental interference takes the form of possibility of suits to establish lower rates or to require some form of expensive additional public service, possibly without adequate compensation. This risk is limited in some states by statutory measures providing that such suits may be brought only

[26]See Samuel Crowther, "Regulation by Intimidation," 5 PUBLIC UTILITIES FORTNIGHTLY 799, 804 (1930).

by certain designated public officers or by a minimum number of complainants.[27] To the extent that such laws reduce this risk of litigation and interference with utility companies, they operate to stabilize utility investments. One great risk in such litigation, no matter how started, is that a proper rate-base or valuation of the property of the utility company will not be determined on by the rate-making or the reviewing tribunal. Even the details of valuation evidence such as the manner of calculating depreciation, allowance for piecemeal construction and similar items are likely to reflect certain prejudices. The presence of such prejudices in the atmosphere in which a rate case is tried, is sometimes more important than the evidence at the hearing.[28]

Speculation concerning the investors' risks attendant upon valuation controversies brings one to the difference of opinion between proponents of the prudent investment theory and adherents of the cost of reproduction theory. These matters were thoroughly discussed at the Buffalo meeting of this section in 1927. It seems worth stating, however, that the two theories were recently discussed at a meeting of social scientists (The Seventh Commonwealth Conference, held in Iowa City, Iowa, on June 30-July 2, 1930) and that the one indisputable merit of the investment theory, i.e., that it offers a sure base for future rates if once established, was the one thing insisted upon at that meeting. Practically nothing was said in support of the reproduction theory. It seems unfortunate that the reasoning which has persuaded the majority of the United States Supreme Court against the able arguments of such men as Justices Brandeis, Holmes, and Stone[29] is so little considered or ap-

[27]See the statutes of N. H., Me., Mass., Ind., Mont., N. D., Or., R. I., S. C., Vt., Wash. These acts are collected in "Commission Laws," compiled by the Am. Tel. & Tel. Co. (3d ed. 1914) pp. 428-438.

[28]See Smith v. Illinois Bell Tel. Co., 270 U. S. 587, 591, 46 Sup. Ct. 408, 409 (1925). Clarence M. Updegraff, "Deductions from the Economic Basis of Public Utility Rates," 13 IOWA L. REV. 249, 266 (1927).

[29]See Missouri ex rel. Southwestern Bell Tel. Co. v. Public Service Comm. of Missouri, 262 U. S. 276, 43 Sup. Ct. 544 (1923); Bluefields Waterworks & Improvement Co. v. Public Service Comm., 262 U. S. 679, 43 Sup. Ct. 675 (1923); McCardle v. Indianapolis Water Co., 272 U. S. 400, 47 Sup. Ct. 144 (1927); St. Louis & O'Fallon Ry. v. United States, 279 U. S. 461, 49 Sup. Ct. 384, 387 (1929); United Railways & Electric Co. of Baltimore v. West, 280 U. S. 234, 50 Sup. Ct. 123 (1930).

preciated by certain lawyers and economists. This reason seems to be inherent in the due process clause. Property can not be confiscated. Just compensation does not depend upon the one-time, long-ago, value of the property to be taken, but upon the present value. This is obviously true in the eminent domain cases and it is equally true in the rate-making cases.[30] To take or to reduce unfairly the income of property is confiscation; to attempt to put it upon an income basis which ignores its present value is as violative of due process as would be the taking of a building and lot, say for a postoffice, on the basis of some former valuation, as, e.g., the value when the building was new, or the cost of erecting it.[31]

This matter is brought up not with the hope of deciding the dispute for once and for all, but with the idea of pointing out that despite the many refusals of the United States Supreme Court to adopt the prudent investment theory, it is still being urged by certain publicists, by some sincere social scientists, and by others who so far fail to see its constitutional impossibility. It is to be assumed that if they once do recognize its constitutional impossibility they will then urge a constitutional amendment to do away with the application of the due process clause to this class of cases. The fact that the "prudent investment" idea is thus being kept alive by a large group of influential thinkers constitutes another *risk* which the investor in utility stock must be persuaded to take before he will part with his money.

What the social scientist sincerely believes, even though erroneous, may be taught and may become a serious factor in the form of a general public belief. For that reason prospective investors in utility stocks and bonds are concerned with, and may well be disturbed by contentions that public utility commissions are not intended to be impartial bodies but rather representatives of the people in their dealings with utility companies.[32] This fallacious idea should be corrected whenever it appears.

Equally disturbing is the thought that property transferred by public authority to utility companies to induce capitalists to invest

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[30]See the majority opinions in the cases cited supra note 29.

[31]Clarence M. Updegraff, "Deductions from the Economic Basis of Public Utility Rates," 12 IOWA L. REV. 249, 265 (1927).

[32]See CRECRAFT, GOVERNMENT AND BUSINESS, (1928) p. 442.

money in them for the development of the business of the companies is, in some mysterious way, as if by some hocus pocus, again the property of the public.[33] This juggling of ownership which is so foreign to our presently accepted notions of title would not be agreeable to the courts in any case where the company induced to locate by public grant is in a business of purely private nature, but it has been given more than merely a polite hearing in some utility cases.[34] The present tendency to give more and more legal effect to currently adopted social and economic doctrines when coupled with this argument of continued public proprietorship may well give the utility investor grave concern. Indeed, it tends to loosen the foundation work of the whole general common law conception of title.

To be more general, the risks of governmental interference include the possibility of a move against the utility company by an officer of either the legislative, the judicial, or the executive branch of the government. The interference may be just or unjust, but in any case its possibility furnishes a menace to the security of investments in utility properties and *pro tanto* furnishes to any investor an argument against investment in utilities and a basis on which to demand higher interest or greater assurance of dividends.

These risks which tend to oppose the making of investments in utilities must be met and off-set by utility officers who are always busy to obtain the necessary additional capital which year after year must go into the work of keeping the capacity and efficiency of the utility company abreast of the constantly increasing demands to be satisfied in our growing country.

Efforts of Public Utility Financiers to Counteract or to Reduce Some of the Unnecessary Risks of Utility Investments Not Found in Other Businesses

Public utility rates must yield a "fair return" or the necessary new money can not be obtained for expansion of the public utilities business. If new money is not supplied so that the utility company can grow as the demands of the community grow, there may result a business depression in the city or town affected and public

[33]See Clarence M. Updegraff, supra note 31, at p. 262 (1927).
[34]Re Long Island R. R., supra note 21.

dissatisfaction until the condition is corrected.[35] This may result in insolvency of the utility company, a receivership, reorganization and probable losses to stockholders, bondholders and other creditors. A period of financial readjustment is likely to take place which may be calamitous to those interested in the utility, inconvenient to the community, and from an economic point of view, inefficient.

For these reasons public officials of statewide jurisdiction, whether utility commissioners, judges, or others, have sometimes imposed upon communities much higher utility rates than local authorities would have been willing to approve.[36] In such cases it was apparent to those taking a comprehensive view of the situation that the higher rates and the consequent prosperity of the utility company were really necessary to the well-being of the community.[37] It is to be remembered that the property of the cities of the state implies prosperity of the state itself, and prosperity of the states, of course, reflects the national condition. Nothing more definitely marks a community as a bad place for either an individual or a business corporation to locate than inadequate, inefficient, run-down public utilities. If I know your utilities, I know your community; if they are good, it is, and vice versa.

About two decades ago utility companies in many communities and of many sorts had fallen into difficulties in the matter of obtaining necessary additional capital. They were failing to keep pace with the general progress, and felt the need of mutual, experienced, technical guidance. This condition stimulated a natural tendency to group together for mutual protection, to exchange information and to organize into associations. As an almost inevitable next-step beyond this coöperation, holding companies came into their present prominence.[38] The associated utility companies for some time have

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[35]See Moody, J., in Knoxville v. Knoxville Water Co., 212 U. S. 1, 29 Sup. Ct. 148 (1909) and Speer, J., in Tift v. Southern Ry. Co., 138 Fed. 753 (C. C., W. D., Ga. 1905).

[36]Re Bronx Gas & E. Co., P. U. R. 1918D, 300, 320; see also 1 SPURR, GUIDING PRINCIPLES OF PUBLIC SERVICE REGULATION 69.

[37]1 SPURR, GUIDING PRINCIPLES OF PUBLIC SERVICE REGULATION, pp. 69-71. Here the author quotes the Hon. Chas. Evans Hughes, then governor of New York, to the effect that rates are to be "just and reasonable" to the patron, the investing public and the utility corporation.

[38]See Kenneth Field, "Group Management," 6 PUBLIC UTILITIES FORTNIGHTLY 86 (1930).

shared technical information and one of their measures was to determine upon counter publicity to oppose that of those who attacked them.[39]

An interesting side of the present so-called "power trust" investigation is illustrated by a story which appeared upon a recent front page of one of our great, nationally circulated newspapers.[40] It is suggested there that one great holding company made a profit of 96% in 1928. The story also indicates that certain other holding companies are making enormous profits and that they have prevented certain federal legislation. These charges have the rather obvious answer that each individual, operating, subsidiary company of any holding company is subject to local regulation by the state through some agency or another, and that the parent company would not be likely to show such enormous profits, even though beyond the reach of local regulation,[41] if the subsidiaries are being operated properly. The holding company may possibly offer some problems but it can hardly constitute a real barrier to effective regulation of the subsidiary, operating company. So far as the blocking of federal legislation is concerned, attention might be called to the fact that the utility holding companies have no power to vote in Congress and that if the Congressional program has been interrupted, it has been by members of the United States Senate or House of Representatives.

In this connection it should be remembered that the public utility companies and their associations are entitled, legally and ethically, to educate the public, men, women, children, and even teachers, as to the true functions and true values of public utility companies Their efforts at disseminating correct information through periodicals, over the radio, through the classrooms and otherwise, can not per se be criticized. It seems questionable, however, whether cer-

[39]See Roger W. Babson, "The Rising Tide of Public Opinion," 5 PUBLIC UTILITIES FORTNIGHTLY 67, 204, 740 (1930).

[40]The United States Daily, July 3, 1930.

[41]See William M. Wherry, "The Regulation of Holding Companies," 3 PUBLIC UTILITIES FORTNIGHTLY 620 (1929); "Massachusetts Tackles the Problem of Regulating the Holding Company," 5 PUBLIC UTILITIES FORTNIGHTLY 839 (1930); Martin J. Insull, "Is the Control of Operating Companies Sufficient?" 14 Proceedings of the Academy of Political Science 86 (1930); see also a collection of short comments in 6 PUBLIC UTILITIES FORTNIGHTLY 41-46 (1930).

tain groups were wise in attempting to offer indirectly the type of information in question. In some instances the effort to maintain secrecy as to the origin of the information published has been discovered and fees, retainers and donations properly paid have been referred to as "bribes," whereas they could not have been given that character if they had been more openly contracted about and more frankly distributed.[42]

In this respect certain utility organizations have made a tactical mistake which should be corrected at once by a frank avowal that they are now carrying on and will continue their policy of educating the American people, patrons and prospective investors, concerning the true aspects of utility company service, value and financing.[43] It would seem that whatever fallacies there may be in municipal ownership might well be pointed out by a utility company whose business existence or integrity is subjected to risk by devotees of that theory. It is to be assumed that some people will attack the propriety of such publicity even where most meticulous care is taken to observe complete frankness, truth and fairness, but the public utility investors can not afford to be silent in the presence of such attacks as they have been subjected to in the past and as may be leveled at them in the future. The people generally should know that one reason for the high cost of utility service is the constant governmental tampering with utility interests.

Recent events, namely, the *O'Fallon* case,[44] the recent increases in freight rates in the Northwest,[45] and the *Baltimore Street Railway* decision[46] give evidence that there is a thoughtful, well informed official group in the United States who appreciate that finding a reasonable rate is not merely one of valuation but one of valuation plus the ascertainment and weighing of social and economic conditions of the patrons of the utility, plus the ascertainment of the conditions of risk bearing upon the investment, or rather the attraction of the necessary new funds to the coffers of the ever-growing utili-

[42]See Ivy B. Lee, "The Man Behind Steps Out," 5 PUBLIC UTILITIES FORTNIGHTLY 141 (1930), and Roger W. Babson, supra note 39.

[43]Supra note 42.

[44]Supra note 29.

[45]See Rate Structure Investigation, Part 2, Western Trunk Line Class Rates (I. C. C. 1930).

[46]Supra note 29.

ties. This may be in part, at least, the result of the public relations compaign carried on by utility groups during the past decade.

The present criticism of certain power groups and the present somewhat blind but very real condemnation of holding companies testify that a new public relations basis must be sought. This is due to a real or unreal, natural or cultivated, suspicion of utility companies. Such a situation calls for action on the part of the utility investors. Possibly their most sound course would be in the direction of advocating the establishment of a Federal Utilities Commission. Quite possibly such a regulatory body would be easier to educate as to the needs and true characteristics of utility financing than any of the present governmental boards or commissions.[47] It might be given power to express the federal authority wherever such authority exists outside of the present jurisdiction of the Interstate Commerce Commission or similar bodies and be, like them, subject to certain federal judicial review.[48]

This does not seem to be the time for those utility investors who are directing affairs of utility organizations to withdraw from the fields of publicity as vanquished and rebuked culprits. They should emphasize and cultivate their public relations as never before. This they should do in a quite frank and open manner, especially since it appears to be the surest way of avoiding some of the risks of unwise governmental interference.[49]

While modern studies have disclosed the fallacies in the natural lawyer's objection to too many laws generally,[50] there is reason to think that too many regulatory laws, too much investigation, and too much interference with and suspicion of the utility companies, make their operation needlessly expensive. There is no one to bear this expense but the consumer. Thus superficial over-regulation on his behalf may and often does work to his injury by bringing about expenses which indirectly result in requiring him to pay more dearly

[47]Clarence M. Updegraff, "The Extension of Federal Regulation of Public Utilities," 13 IOWA L. REV. 369 (1928).

[48]Supra note 47 at p. 375 *et seq.*

[49]See Samuel Crowther, supra note 26; 5 PUBLIC UTILITIES FORTNIGHTLY 799, 807 (1930); see supra note 39.

[50]See POUND, THE SPIRIT OF THE COMMON LAW, ch. V and VI (1921); see 5 PUBLIC UTILITIES FORTNIGHTLY 807 (1930).

for utility services than would be required to support the company under less regulation.

The utility investor becomes more and more cautious each day as he observes the fluid, uncertain, changing factors of reasonable rates. Perhaps less regulation and agitation would restore his confidence and benefit both the patrons of and the investors in public utilities as much as the wisest legislation that can emerge from the present period of doubt and dispute.