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State Rate Regulation and the Supreme Court, 1922-1930

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The constitutional canons of rate regulation may be simply stated. Rates of enterprises affected with a public interest or devoted to a public use\(^1\) are subject to legislative and administrative regulation, but the rates prescribed by governmental action must not be so low as to yield to the enterprise less than a fair return on the fair value of the property employed therein. Such is the rule of constitutional law. All that remains is the problem of its application. This involves the choice of the appropriate canons to be used and the ascertainment or estimate of the facts in each particular case. Since the issue of confiscation depends upon the facts as well as upon the law, the facts must be subject to judicial inquiry. Thus courts must think like engineers and bookkeepers as well as like lawyers. The ultimate decision may turn upon any one of several factors or upon some combination of two or more of them. For this reason, cases on rate regulation have a peculiar propensity to be \textit{sui generis}. The effort to sum them up by general statements is likely to yield little enlightenment for its pains.

Most rate cases are started in these days by an effort on one side or the other to get an injunction. A few arise out of statutory proceedings to secure more direct judicial review of administrative action. However the fight is begun, it comes to the Supreme Court of the United States as an issue whether the court below should be affirmed or reversed. The decree below may be thought right even if in a number of details the court

\(^1\) For Supreme Court decisions from 1922 to 1930 on what enterprises may be included within the class of those affected with a public interest or devoted to a public use, see Thomas Reed Powell, "State Utilities and the Supreme Court, 1922-1930," 29 Mich. L. Rev. 811-838. The second installment of the article (29 Mich. L. Rev. 1001-1030) reviews decisions for the same period on the Imposition of Duties and Liabilities on Public Utilities.
below may be thought wrong. Likewise the decree below may be thought wrong even though the court that rendered it was not wholly wrong. If the Supreme Court may find in a single point adequate grounds for affirmance or reversal, it need not pronounce itself upon other points which have also been contested. The appellate court passes upon the record, not upon the quarrel. Some of its judgments are merely tentative. The lower court may be told to do its work over again without being advised as to what conclusion it should reach. Where the injunction asked for is an interlocutory one, its denial or issue is not scrutinized as carefully as when a final injunction is involved.

For these and other reasons we seldom, if ever, get the whole story of any rate dispute in the opinion which the Supreme Court may utter about it. An adequate account of any single controversy would require examination of everything that happened before and after the case reached the Supreme Court, and it would take more space than can here be given to outline the story of all the controversies that came before that court in eight years. Even the reporting of Supreme Court action and Supreme Court talk must fall far short of conveying full enlightenment of what that court had to do with the controversies. Voluminous records which come to the court present much which the court cannot set forth in detail in its opinions. The opinions themselves often contain much that must be neglected in any such survey as is possible here. It is more feasible to tell what the controversy is about than to tell much about it. As a study of law, our summary is bound to be pathetically inadequate. The most that it can hope to do is to give some inkling of the work of the Supreme Court as arbitrator of the rate controversies that come before it by reason of the prescriptions of states and municipalities. As a study in government as contrasted with law, the record may have significance for its illustration of one phase of the judicial centralization that has come about on the basis of the Fourteenth Amendment.

In view of the fact that each case may present several points and that consideration of one point is not wholly independent of consideration of another, it has been thought best to present, first, a separate account of each case with indication of the various points involved so that the struggles may be viewed as
the lawyers presented them. Law suits are lawsuits and not merely duels of two contending principles. Yet principles in the law there are perhaps, and so an effort will be made later to make a more analytical arrangement of the accounting or legal issues that are involved in the quarrels recited and to offer a report of Supreme Court utterance or action on each issue. There has been dispute about generalities even though the disputants agreed on the disposition of the case before them. Perhaps generalities have their place even when they do not decide cases.

I. Conspectus of the Cases

An order of a state commission reducing the rates of a telephone company was set aside by a unanimous court in Missouri ex rel. Southwestern Bell Telephone Co. v. Public Service Commission, but the justices did not all agree in the reasons for their agreement. Mr. Justice Brandeis, for himself and Mr. Justice Holmes, concurred because of opinion that the order prevented the utility from earning a fair return on the amount prudently invested by it. He presented no figures of the investment or probable return in the case at bar, but devoted himself wholly to a consideration of the superiority of the rate base of "prudent investment" over that of "reproduction cost new, less depreciation." For the rest of the court Mr. Justice McReynolds based the decision on the fact that the commission had ignored the cost of reproducing the property in its existing state, that consideration of this factor would result in a valuation of at least $25,000,000, that the return under the contested rates as estimated by the commission would, after allowing six


This case is of course considered in many of the other articles published during the period under review and listed in succeeding notes.
per cent for depreciation, which the commission accepted as appropriate, amount to only five and one-third per cent which was wholly inadequate as interest rates were at the time. The company's engineers had contended for an estimate of over $31,000,000 which was made up of about $24,000,000 for reproduction cost of the physical plant less depreciation, about $1,000,000 for working capital, and over $5,000,000 for cost of establishing the business. This latter item was neglected by the court in reaching its estimate of $25,000,000, but it was not explicitly rejected as inappropriate. The book value shown by the company as actual cost of plant, equipment, and working capital was nearly $23,000,000. The commission objected to the inclusion in this of certain items of non-useful property. It reached an estimate of some $20,000,000 by taking as a standard its own estimates of the value of selected parts of the plant in 1913, 1914 and 1916, and then applying to the valuation claimed by the company a percentage determined by the difference between the values fixed by the company and by the commission on the three selected sections of the total plant. The commission did not claim this valuation to be more than tentative. For all that appears, these earlier valuations made by the commission had regarded reproduction cost as of the times they were made, for the only specific criticism passed by Mr. Justice McReynolds upon its action was the failure to accord any weight to the greatly enhanced costs of construction since the earlier dates.

The opinion of the court consists largely of quotation from the report of the commission and from the opinions in earlier cases. To this there is added:

"It is impossible to ascertain what will amount to a fair return upon properties devoted to the public service without giving consideration to the cost of labor, supplies, etc., at the time the investigation is made. An honest and intelligent forecast of probable future values, made upon a view of all the relevant circumstances, is essential. If the highly important element of present costs is wholly disregarded, such a forecast becomes impossible. Estimates for tomorrow cannot ignore prices of today."


Recent Developments of the law of rate regulation are discussed in Frederick K. Beutel, "Valuation as a Requirement of Due Process of Law in Rate Cases," 43 Harv. L. Rev. 1249; Frederick K. Beutel, "Due Process in Valuation of Local Utilities," 13 Minn. L. Rev. 409; Cassius M. Clay, "Control of Public Utility Rates and the Supreme Court," 64 U. S. L. Rev. 464; L. Dale Coffman, "The Meaning and Ascertainment of 'Value' of Public Utilities," 15 Iowa L. Rev. 401;
For a like failure to give any substantial weight to price of labor and commodities at the time of the rate prescription, a state commission and a state court were reversed in *Bluefield Water Works & Improvement Co. v. Public Service Commission.* Mr. Justice Brandeis concurred specially for the reasons given by him in the preceding case. In this case the commission had fixed a value of $460,000 in place of the company's estimate of $900,000. The commission had reached its result by adding $10,000 for working capital and ten per cent for going value to the cost of the plant, less depreciation, as shown on the company's books. It had been guided largely by an estimate made by it in 1915, to which it added subsequent expenditures for construction. The rates fixed by the commission were estimated by it to be sufficient to leave the company six per cent on the commission's valuation, after deducting two per cent for depreciation. The net return of six per cent was declared by Mr. Justice Butler to be too low. This was unnecessary to the disposition of the case, since the rate-base was also too low. Other matters of dispute respecting various items of value to be considered in making up the total were left unconsidered.


The articles listed here and later as discussing a particular case are not restricted to the particular case to which they are appended.

Refusal of state commission and state court to give strict application of the standard of replacement cost less depreciation in valuing the physical properties of a gas company was held in *Georgia Railway & Power Co. v. Railroad Commission* not to be in itself a sufficient cause for holding a rate confiscatory. Mr. Justice Brandeis states that "the commission gave careful consideration to the cost of reproduction, but it refused to adopt reproduction cost as the measure of value." No reasons are given why the careful consideration resulted in rejection. Some of the construction had been recent when high prices prevailed, so that as to this, cost and reproduction cost would not be wide apart. Reproduction cost was given weight in the allowance of $125,000 for appreciation in the value of land owned, but this was a minor matter in the total of $5,250,000 which the commission fixed. That part of the plant which was in existence in 1914 was put in at something near its cost or its reproduction cost as of that time, though the 1921 costs were round 70 per cent higher than those of 1914. The company contended for a total valuation of at least $9,500,000. This included $1,000,000 for the alleged value of a non-exclusive franchise and $1,000,000 for recoupment of past losses, both of which the court held had been rightly excluded by the commission. It included also about $450,000 in the items of working capital and going concern above the amounts allowed by the commission and approved by the district court. These reductions were approved by the Supreme Court as findings of fact not clearly shown to be erroneous. This left about $1,800,000 more of the claim of the company which was disallowed by the commission and the two courts. For aught that appears, this sum may fairly represent the price-rise from 1914 to 1921 if applied to the property used in 1914. There is no suggestion that the company’s estimate of present reproduction cost was excessive. The opinion goes on the ground that what the Constitution requires is not adoption of reproduction cost but merely careful consideration of it. To Mr. Justice McKenna this seemed to be a disregard of the rule


*282 U. S. 625, 43 Sup. Ct. 680 (1923). This case is given detailed consideration in a number of the articles listed in other footnotes. It is the subject of a note in 15 Nat. Mun. Rev. 485.
of the prior cases and a rejection of present value. The mystery is that he was alone in dissent. Perhaps the others who would normally be with him were influenced by the fact that the Commission had in the past from time to time allowed increases of rates as costs went up and by the further fact that the case was heard upon application for an interlocutory injunction and that the decree of denial in the court below was founded on the conclusion that enforcement should not be enjoined prior to actual experience under the reduced rate. The estimated return was seven and one-quarter per cent after allowing two per cent for depreciation and regarding the federal income tax as an operating expense. There must have been a general impression that the rates fixed were likely to prove fair to the company, but it seems difficult to disagree with the dissenting views of Mr. Justice McKenna that here reproduction cost was regarded only to be largely disregarded and that the decision and opinion of the majority seem to run counter to the attitude of the two other cases decided at the same term. 7

The contested matters between the parties in Pacific Gas &

Electric Co. v. San Francisco\(^8\) did not involve the physical items to be valued or their reproduction cost new. They were confined to the valuation of certain patent rights and to the determination of accrued and annual depreciation. These two questions were inter-related. The company had paid some $46,000 for rights to use a patented process which had resulted in annual reductions of the costs of production claimed to run from around $100,000 to around $260,000. The inauguration of the process had resulted in the abandonment of parts of the plant worth perhaps $800,000. The master had valued the patent rights at what they cost as against a claim by the company that they were worth the capitalization of the annual savings resulting from their use. The accrued depreciation had been fixed by the master at around $1,500,000, which left the property worth about 81 per cent of what it would cost to reproduce it as a new plant. The company contended that the accrued depreciation should have been fixed at about half the sum found by the master. The master had used the "modified sinking fund method" which estimated the life of each part of the plant, figured the annual reserves necessary to yield enough for ultimate replacement, and added them together to get the depreciation already accrued. The company contended that it was preferable to examine the exact condition of the plant at the time of appraisal and thus discover how much in fact it had depreciated. Mr. Justice McReynolds, for the majority, remarks that facts shown by reliable evidence are preferable to averages based upon assumed probabilities. It is not clear that the difference between the two estimates was due wholly to difference of method in computing them, and there is no determination of the precise amount to be allowed. The company, according to Mr. Justice McReynolds, does "not insist that the estimated accrued depreciation is 'grossly excessive'; if confined to the result of physical causes."\(^9\) This can hardly be accurate, for the company was contending for a lower accrued depreciation. Mr. Justice Brandeis says that "the company's objection is not to the particular method selected, but that, in applying it, the master included as depreciation what is called theoretical inadequacy and

\(^8\) 265 U. S. 403, 44 Sup. Ct. 537 (1924).
\(^9\) 265 U. S. 403, 406.
obsolescence.'10 What the company wanted was, if possible, to value the patented process at a capitalization of its savings, and otherwise to treat the obsolescence of its plant by reason of the new process, not as accrued depreciation, but as depreciation to be anticipated for which in effect the savings in operation should be charged with large annual sums to recoup it within a few years. To Mr. Justice Brandeis these questions of valuation and of estimating depreciation were questions of fact upon which there was no sufficient basis for overruling the master and the district court. Mr. Justice Holmes concurred in his opinion. The views of the majority must be gathered from the concluding paragraphs of the opinion of Mr. Justice McReynolds:

"Obviously, under the theory accepted below, appellant worsened its situation for rate-making purposes when it reduced the cost of manufacturing gas. Introduction of successful patented inventions enabled the public authorities to lower the rate base and gather all the benefits. The operating plant, made capable of producing gas at smaller cost, was declared less valuable than before. The result indicates error somewhere, either in theory or application of principle.

"Obsolescence of one or more stations and perhaps other property theretofore of great value (possibly $800,000) followed installation of the patents, but the remaining plant plus the patents, gave better results. As an operating unit the new combination had greater value than the old; but the court below disregarded the demonstrated worth of the element which wrought this change.

"The obsolescence in question did not result from ordinary use and wear. Certainly it could not have been long anticipated—the patents were of recent conception; to provide for it out of previous revenues was not imperative, if possible. Former consumers were not beneficiaries; only subsequent ones could be advantaged.

"Our concern is with confiscation. Rate-making is no function of the courts; their duty is to inquire concerning results and uphold the guaranties which inhibit the taking of private property for public use without just compensation under any guise. We may not, therefore, relegate appellant's claim for

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10 Ibid., 422.
past services to the future consideration of the State Commission, as the master suggests. After adopting the reduced costs of manufacture for estimating net returns, the court gave no proper valuation to the inventions which caused the reduction, and thereby permitted property to be taken without just compensation. The amount of money actually paid to the inventors was not the proper measure of worth. Experience had demonstrated a much higher one; and to obtain the benefit of their use appellant sacrificed much.

"Installation of the inventions necessitated new outlay of money and abandonment of property theretofore valuable—both were necessary in order that the cost of manufacture might be reduced. If appellant's permissible profits depend upon the lowered costs and it is denied adequate return upon property which made the reduction possible, or recompense for the obsolescence, successful efforts to improve the service will prove extremely disadvantageous to it.

"Whether, under the peculiar circumstances here presented, the rate base should be fixed by adding to the agreed inventory some fair valuation of the patent rights, or whether prompt recoupment should be allowed for the obsolescence caused by their introduction, or whether appellant should be saved from actual ultimate loss by some other feasible method, we will not undertake to determine upon the present record. To the end that the issues may be reconsidered in view of this opinion, the decree below is reversed and the cause remanded for such further proceedings as the circumstances require, including another reference to the master, if deemed advisable.""\n
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\[11\] Ibid., 415-416.


On other problems of valuation, see Fred Esch, "Valuation of Leased Railroad Property," 33 Yale L. J. 272; Frank Parker, "Cost of Money as an Element in the Valuation of Public Utilities," 74
The dispute in *Ohio Utilities Co. v. Public Utilities Commission* involved mainly reductions made by the commission in the values found by its own engineers and acquiesced in by the company. The commission had reduced by some $10,000 the engineers' valuation of $154,655.93 which had been reached by an itemized inventory and a valuation based on reproduction cost less depreciation. A unanimous Supreme Court reversed the state court which had sustained the commission. Mr. Justice Sutherland found no evidence in the record to justify the cuts imposed by the commission and approved by the state court, and said that it was therefore "evident that the state supreme court did not accord to the plaintiff in error that sort of judicial inquiry to which, under the decisions of this court, it was entitled." The commission had excluded $5,000 for preliminary organization expenses, apparently on the ground that there was no proof that they had been incurred. Mr. Justice Sutherland said that such proof, while it might be helpful, is not indispensable. The question is not whether such expenditures have been made but whether they would have to be made if the enterprise were to be imaginatively annihilated and re-created. Some such expenditures would necessarily be incurred, and the rejection of the entire amount is clearly arbitrary. So with interest during imaginative reconstruction which the commission had reduced about $3,000 without putting into the record any evidence in justification. Likewise unsupported by evidence were found the commission cuts of $1,316.42 on necessary working capital and of $276.15 on value of plant, the latter evidently to get an even $122,000. The commission in estimating operating expenses, made a slight shave from the figure of expenses actually incurred in the preceding year, giving as a reason that the plant had been inefficiently operated. For this the court found no evidence in the record, and, indeed, found evidence to the contrary in the testimony of the commission's engineer. After deducting the five per cent allowance for depreciation which the commission reckoned, the anticipated return would be less than 5 per

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cent, which Mr. Justice Sutherland said was so clearly inadequate as to amount to confiscation. So the case was sent back for reappraisal.\textsuperscript{13}

While the complaining telephone company in \textit{Board of Public Utility Commissioners v. New York Telephone Co.}\textsuperscript{14} was said by Mr. Justice Butler to contest the commission's estimate of property value, there is no consideration of the correctness of the $88,417,448 fixed by the board. According to the commission, the existing rates would yield 5.04 per cent on average cost and 4.93 per cent on average fair and reasonable value after deducting $3,314,716, as the annual depreciation charge. The company insisted that there should be a larger charge for annual depreciation, but there was no adjudication of this difference. It was conceded on all sides that on these facts alone the existing rates would not yield a fair return. The Board's refusal to grant a higher rate was based on its finding that the $16,902,530 set up on the company's books as reserve for accrued depreciation was excessive and on its ruling that at least $4,750,000 of that amount be used until exhausted to make up any deficiencies in fair return for the immediately ensuing years. The idea was that past excessive depreciation should be corrected by future


inadequate annual depreciation. The Board allowed for annual depreciation over $2,600,000 less than what it determined the annual depreciation to be, and thereby raised the anticipated return from 4.93 to 7.53 per cent, thus justifying its refusal to permit an increase in rates. For a unanimous court, Mr. Justice Stone not sitting, Mr. Justice Butler declared that these past accumulations are the property of the company, even though acquired by excessive reserves for depreciation, and that past profits cannot be used to sustain confiscatory rates for the future. The district court was therefore affirmed in its decree enjoining the commission from requiring the continuation of existing inadequate rates.\(^1\)

Injunction proceedings against a rate for water service fixed by a commission came before the Supreme Court in \textit{McCardle} v. \textit{Indianapolis Water Co.}\(^2\) on an appeal by the city and the commission from a decree of the district court enjoining the rates. Upon petition the commission had found existing rates too low and had granted an increase which did not satisfy the company. The commission had found the total value of the property to be $15,260,400 and had allowed rates which in its opinion would produce a seven per cent return over an average of the three succeeding years. In the injunction proceeding brought by the company, the district court had found the value of the property to be not less than $19,000,000 and had enjoined the new rates as inadequate. In sustaining this decree, Mr. Justice Butler says that this $19,000,000 could not have been reached by figuring reproduction cost less depreciation "on


spot prices as of January 1, 1924.” The company was defending this figure on the ground that it did not represent spot prices of reproduction, and the majority of the Supreme Court agrees with it on the facts. The city was contending that the figure did represent spot prices and that therefore the valuation was too high. The Supreme Court finds that on some basis other than that of spot prices the figure is not excessive. The case clearly cannot hold that present spot prices must be taken for reproduction cost. Mr. Justice Brandeis, in dissenting quotes the opinion of the district court which shows that it thought itself required by recent Supreme Court decisions to give dominating weight to spot prices, and that it fixed $19,000,000 as the minimum on that basis, awarding no more solely because the company did not ask for more. He thinks, therefore, that the affirmance of the district court affirms its application of the rule of spot prices, and that the decree should be reversed and the case sent back for determination of present value in the light of all applicable rules, among which is the one that present prices of reproduction are not necessarily controlling. Mr. Justice Stone joins in this dissent. Mr. Justice Holmes confines his concurrence with the majority to concurrence in result. Mr. Justice Butler nowhere says that spot prices are necessarily determining. He says that values must “generally follow the relatively permanent levels and trends” of prices of labor and materials, and he finds nothing in the record before him to indicate that prices prevailing on January 1, 1924, were likely to decline within three years. He clearly negatives the propriety of accepting the commission’s estimate based on average prices for the ten years ending in 1921. The commission’s engineer testified that application of the average of prices for ten years ending with 1923 would reach the result of $17,000,000 for reproduction cost of physical plant less depreciation. The commission itself included over $1,500,000 for going value, working capital and water rights, and engineers hired by the company to ascertain the truth with respect to these values had made estimates of $2,735,000 and $2,961,245. The figure set by the district court for the total value was $2,000,000 below the sum of the intangible values found by the commission and the spot-price reproduction cost fixed by the commission’s engineer. It was over $6,000,000 below the aver-
age of the two estimates made by engineers chosen and paid by
the company. Thus the company was either skeptical or
eleemosynary in proposing and accepting a valuation some
$6,000,000 lower than what it supported by evidence. The dis-

trict court was of opinion that it might have sustained a much
higher value. Thus the case on its facts stands merely for one
of the jumbles characteristic of the so-called application of the
so-called rule of Smyth v. Ames. It holds that more weight
must be given to reproduction cost than the commission chose
to give in the particular instance, but even the opinion does not
insist that spot prices must be taken to determine reproduction
cost irrespective of anticipations of the future price level. Mr.
Justice Brandeis’ dissent seems to make the majority go farther
than their printed words disclose. Undoubtedly Mr. Justice
Butler’s 1926 prescience as to future prices led him to lend
more weight to the high scale then obtaining than he would now
care to give to the results he failed to foresee. But the weight
he would give to present prices is still only the weight which he
thinks they deserve, and this, he clearly recognizes, depends
somewhat upon anticipations as to the future. Mr. Justice
Brandeis points out the ineptitude of present prices as well
when they are low as when they are high. One may imagine
that Mr. Justice Butler may lean more toward past averages
from now on than he has in the past.17

17 On various problems relating to the financing and the inter-
corporate relations of utilities, see James C. Bonbright, “The Basis
of Railroad Capitalization,” 35 Pol. Sci. Q. 30; Julius Henry Cohen,
“Conscatory Rates and Modern Finance,” 39 Yale L. J. 151; Robert
Cost in Public Utility Regulation,” 35 Yale L. J. 805; Irwin S. Rosen-
baum and David E. Lilienthal, “Issuance of Securities by Public
Service Corporations,” 37 Yale L. J. 716, 908; Irwin S. Rosenbaum,
“Regulation of Security Issues by the Ohio Public Utilities Commis-
sion,” 4 U. Cin. L. Rev. 321; Scott Rowley, “Rate-Making and the
Ownership and Financing of Railways,” 11 Iowa L. Rev. 354; Maurice
C. Waltersdorf, “State Control of Utility Capitalization,” 37 Yale L. J.
337; David E. Lilienthal, “The Regulation of Public Utility Holding
Companies,” 29 Colum. L. Rev. 404; Samuel W. Moore, “Our Lagging
Railway Mergers,” 15 Va. L. Rev. 743; William M. Wherry, “Principles
Applicable to Consolidation and Merger of Public Utilities” 6 N. Y.
U. L. Rev. 143; and notes in 41 Harv. L. Rev. 928, on control over pur-
chase of stock by holding company; in 14 St. Louis L. Rev. 299, 442,
on regulating payments by utility to holding company; in 37 Yale L. J.
675, on case holding power to prescribe uniform accounting does not
include power to determine measure of value for fixed capital; and
in 38 Yale L. J. 685, on power over issuance of shares by foreign cor-
porations.
The issue on which the dispute in United Fuel Gas Co. v. Railroad Commission was found to turn was the proper value to be assigned to the gas rights and leaseholds owned by the complainants. These were rights to extract gas from the lands of others, and were valued by the commission at $6,742,920, at which sum they were carried on the company's books. The company contended for a valuation of $36,449,176, based on testimony as to the profit that would be received from the extraction of the gas and its sale in an unregulated market. This testimony was rejected by the Supreme Court as altogether too speculative. The unregulated market which the complainants hypostatized was Pittsburg, Pennsylvania, which is 130 miles from their nearest lines. Mr. Justice Stone observed that it is inadmissible to assume that there will remain an unregulated market. He found equally speculative the estimates as to the quantities of gas that could be extracted in the future, the prices that natural gas would in later years bring in competition with other gas, and the future cost of transportation and distribution. With this evidence rejected, the court fell back on the book value of the leases recognized by the company, not necessarily as the true value, but as a value assumed by the complainants, which cannot on the evidence be put at any higher figure. The complainant objected also to the conclusion of the court below that one-half of the profits on the sale of gasoline could be attributed to the natural gas. The gas and gasoline come from a common flow and are joint products. It was shown that allowance by the gasoline extracting company of 50 per cent of its net earnings from gasoline extraction would still leave it earning amounts which varied from 80.40 to 102 per cent annually on its capital, so that the payment of 50 per cent to the natural gas company would not seem excessive. The gas company had created the gasoline company as a subsidiary and contracted with it for a payment of only one-eighth of its gross profit, but Mr. Justice Stone rejected this arrangement by pointing out that a corporation may not make a rate confiscatory by reducing its net returns by arrangement with a subsidiary under its control. The company which furnished the gas in Kentucky which was involved in the present proceeding was a newly created

subsidiary which purchased gas from its parent at 30 cents per 1,000 cubic feet, but it was agreed that this contract and the separate creation of the Kentucky subsidiary should be neglected, and attention should be directed to that part of the whole physical property of the intertwined corporations that could be regarded as properly allocated to the furnishing of the Kentucky supply. This was taken to be not more than 12 per cent, which resulted in a valuation of $5,326,530 with the inclusion of the leasehold rights at their book value. This would require $745,714 annually as a fair return on an eight per cent basis, after deducting one and one-half per cent for depreciation and four and one-half per cent for amortization. The amortization allowance was deemed to be sufficient to replace the entire property at the end of eighteen years when it was assumed that the wells would cease to be productive. The depreciation allowance was said by Mr. Justice Stone not to be seriously questioned by the company. The return under the assailed 32-cent rate was $749,839, a trifle more than the eight per cent requirement on the valuation found by including the gas rights at their book value. Several contentions by the company were left unadjudicated, since the return was found to be adequate even if they were granted. So without deciding upon their validity, the court accepted for the case the assumptions that the rate base should be present reproduction cost of property used and useful in the business, that the Kentucky business should be remunerative when considered by itself, that so-called "probable" areas of gas production should be included in the property even though not at present used, that depreciation and amortization should be calculated on the basis of present value rather than of original cost, and that the so-called "delay rentals" paid on leases not yet productive should be treated as present operating expenses. There was a lee-way of nearly $8,000,000 between the estimate of overhead charges and going concern value made by the commission and that insisted on by the company, but this difference was not arbitrated by the Supreme Court, for even on the company's figures for these items an eight per cent return would be realized. Though the court was unanimous, Mr. Justice McReynolds confined his concurrence to the result.

The facts in the companion case of United Fuel Gas Co.
v. Public Service Commission of West Virginia\(^1\) differ somewhat, but the main bone of contention was the valuation of the leasehold rights as in the case from Kentucky. With those valued at book value the Supreme Court found no reason for disturbing the decree of the district court denying an interlocutory injunction. On the valuation found by the district court the rates would yield over eight per cent, after deducting 1.12 per cent for depreciation and 3.65 per cent for amortization. There are differences of method in reporting the values claimed by the company and those found by the commission and by the court below, so that comparison of them is difficult. Evidently the company threw its chief weight against the limitation of the value of the leasehold rights to the amount at which they were carried on their own books, for Mr. Justice Stone says that “with respect to the other conclusions of the court below, there is no serious suggestion that the court abused its discretion.” The decree is affirmed on the ground of the absence of any clear evidence warranting interference with the denial of an interlocutory injunction. Mr. Justice McReynolds again concurs only in the result.

The major question in United States Railways & Electric Co. v. West\(^2\) was whether a return of 6.26 per cent upon the value of a street railroad is compensatory. The company asked for a rate estimated to produce 7.44 per cent, though insisting that this was not adequate. Mr. Justice Sutherland said that in view of the special situations of street railroads it is not certain that a return of even eight per cent would not be necessary to avoid confiscation. He declared that clearly the company was entitled to the 7.44 per cent for which it contended. The plant of the company was valued by the commission at $75,000,000, and this valuation was accepted by both parties in the state court. In the Supreme Court the company contended for the omission of $5,000,000 which had been included because the state court held that the right to use the streets is an easement which is property belonging to the company. The objection to

\(^1\) 19278 U. S. 322, 49 Sup. Ct. 157 (1929).
valuing this so-called easement was left without other consideration by Mr. Justice Sutherland than the comment that, if it ever possessed substance, it comes too late. To Mr. Justice Brandeis, on the other hand, the objection goes to the issue whether the rate is confiscatory under the federal Constitution. The state court may say that the state constitution requires the inclusion of such an element, but the Supreme Court must decide whether the rule is the same under the federal Constitution. The rate is not confiscatory under the federal Constitution if it yields a fair return on values protected by the federal Constitution. The rule of the Supreme Court, says Mr. Justice Brandeis, is that such franchises to use highways are to be valued as property of the recipient only to the amount that has been paid for them. An explanation of the commission's urging in the Supreme Court an objection not urged in the state court is that the state court had rejected its estimate of annual depreciation and had required it to figure the annual depreciation on present replacement value, thus causing it to add over $750,000 to the annual depreciation charge. This, says Mr. Justice Sutherland, was clearly right, since the purpose of the annual depreciation charge is to get a sum sufficient to restore the property and not merely to recoup its original cost. Mr. Justice Brandeis disagrees. Justices Holmes and Stone join in his dissent, and Mr. Justice Stone adds a brief separate dissent.

The issue as to depreciation had been raised by the commission both on cross-appeal and on petition for certiorari. The first was dismissed and the second denied, since Mr. Justice Sutherland held that the issue of depreciation could be considered on the appeal of the company, as it was contested throughout the proceedings, and is a necessary element to be determined in fixing the rate of fare. On the issue of rate of return, Mr. Justice Brandeis observed that 6.26 per cent on such property as that of the particular company "would seem to be compensatory." He added that the return would be 6.70 per cent if the $5,000,000 item for street rights had been excluded, and would be 7.78 per cent if in addition the annual depreciation charge had been computed according to what he deems a proper method. The commission had allowed for annual depreciation a sum equal to five per cent of the gross receipts, which had been the company's annual charge for depreciation since 1912. Mr.
Justice Brandeis points out that if the company had in the past five years charged off depreciation on the basis allowed it in the Supreme Court, it would have had no book-keeping profits, and would have paid all its dividends illegally, since the depreciation charge would have wiped out its book surplus by 1925. The rates to which the company objected as insufficient were a cash fare of ten cents, with four tokens for thirty-five cents. This was an advance allowed by the commission, which the state court held adequate because of the 6.26 per cent return. The Supreme Court holds that the injunction against these rates should have been granted, and so reverses the state court. A minor complaint of the company against abolishing a second fare zone on a suburban line was held to raise no constitutional objection if the commission allowed rates which yield a fair return on the whole property, even though the particular extension may not be operated with profit.21


On matters relating to service, see notes in 11 Minn. L. Rev. 234, on power of public service commission to waive compliance with regulations; in 41 Harv. L. Rev. 542 and 76 U. Pa. L. Rev. 456, on giving preference to railroad in operating bus service; in 21 Ill. L. Rev. 502, on discrimination between companies operating motor bus lines in favor of company with contract; in 37 Harv. L. Rev. 395, on free bus
That there are uncertainties incident to the enterprise of determining present fair value and of estimating the net returns from rates not yet in force may be inferred from Brush Electric Co. v. Galveston in which the Supreme Court approved of the action of the district court in withholding an injunction pending actual trial of rates complained of. As Mr. Justice Sutherland put it, "the evidence is so conflicting and the conclusion to be drawn therefrom in respect of this or that item so uncertain and speculative, that we do not feel warranted in disturbing the findings of the court below in the absence of an actual test under the new rates." The uncertainties here present do not seem to differ greatly in kind or in amount from those which have appeared in many other records on which the court has found itself able to reach positive conclusions. Estimates of accrued depreciation varied from 15 to 40 per cent. The master fixed it at 28 per cent which the district court increased to 33 and one-third per cent. By this and some other changes the $800,000 rate base found by the master was estimated provisionally by the district judge to be $612,000. The other difference between the master and the district judge was the reduction to four per cent of the master's allowance of four and one-half per cent for annual depreciation. Both agreed on a required annual return of eight per cent. On the master's estimates, this return was more than realized under the actual operation of the 1918 rates complained of. He found, however that the lower 1919 rates would yield less than the required fair return by $22,000. The district judge, by using a higher accrued depreciation and a lower annual depreciation, estimated that the 1919 rates would yield over $21,000 in excess of the required fair return. The parties had agreed that the undepreciated values of the physical property was $784,689 on the basis of January 1920 prices. Mr. Justice Sutherland says that the master found that this amount, "after deducting the value of the real estate, office and utility equipment, and depreciation, represented the depreciated value of the depreciable property for rate-making purposes." He

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service as unfair competition; and in 40 Harv. L. Rev. 882, on motor bus regulation.

In 32 Yale L. J. 390, 507, are discussions of Galveston Electric Co. v. Galveston, 258 U. S. 358, 42 Sup. Ct. 351 (1922), which is reviewed in 21 Mich. L. Rev. 310-313. The case in the court below is considered in 1 Tex. L. Rev. 89.

**262 U. S. 443, 43 Sup. Ct. 606 (1923).**
s prosecutor says also that the master, by deducting 28 per cent for depreciation, made "the present depreciated value of the depreciable property $534,818." To this the master "added the value of various items, including intangible property, real estate, and office and utility equipment, bringing the total up to $800,000." All this would be more understandable if the agreed $784,689 for the undepreciated value of the physical property at 1920 prices were taken by the master as the undepreciated rather than the depreciated value of the depreciable property. Even if this were done, however, the 28 per cent reduction for accrued depreciation would not give the $534,818, which the master found as the depreciated value of the depreciable property. Inasmuch as the parties stipulated and the master agreed "that the cost of the physical property at average pre-war prices undepreciated, as of January 1, 1920, was $576,898," the provisional value of the lower court recognized an enhancement of over $35,000 in an enterprise in which depreciable property was estimated to have before it only two-thirds of its originally allotted span of usefulness. It may well be that the court was as much influenced by a feeling that the position of the enterprise was far from precarious as by a feeling that the contradictions in the estimates were unresolvable. While the figures presented in the opinion do not seem to correspond with each other, the differences in the competing guesses seem to present no harder problems than the court has felt itself competent to solve in many other cases. The frank recognition accorded to the speculative character of the estimates here involved might perhaps profitably be extended beyond the confines of the particular case.  

23 By the so-called Recapture Provision of the Transportation Act, the roads were restricted in their use of so-called excess earnings. The general features of the plan were sustained in Dayton-Goose Creek Railway Co. v. United States, 263 U. S. 456, 44 Sup. Ct. 169 (1924), reviewed in 26 Colum. L. Rev. 404-407. In determining values for the purpose of recapturing the so-called excess return, the statute directed that the Commission "shall give due consideration to all the elements of value recognized by the law of the land for rate-making purposes, and shall give to the property investment account of the carriers only that consideration which under such law it is entitled to in establishing values for rate-making purposes." A question of valuation under this statutory requirement arose in St. Louis & O'Fallon Railway Co. v. United States, 279 U. S. 461, 49 Sup. Ct. 384 (1929), in which the majority found that the Commission had given no consideration to current, or reproduction costs, and held that therefore its order should be annulled because not reached in conformity to the statute. Mr.
The rates involved in *Aetna Insurance Co. v. Hyde* were ones fixed by the state superintendent of insurance under a statutory mandate to reduce rates when upon investigation he finds that for the past five years the earnings of the stock fire insurance companies within the state have yielded an aggregate profit in excess of what is reasonable. The companies did not contest the constitutionality of the statute but objected only to the reduction ordered by the superintendent and approved by the state court. The companies objected to the basis on which

Justice McReynolds said that the weight to be given to such 'cost is not before the court, and observed in addition that "no doubt there are some, perhaps many, railroads the ultimate value of which should be placed far below the sum necessary for reproduction." In dissenting opinions, Justices Brandeis and Stone insisted that the Commission had considered reproduction costs and given to them such weight as it found they deserved in the particular case, and that there was no evidence in the record sufficient to justify the court in finding that the result did not accord with the prescription of the statute. Each writer of a dissent concurred with the other, and Mr. Justice Holmes concurred with both. Mr. Justice Brandeis outlined at length the reasons for his judgment that "current cost of reproduction higher than the original cost does not necessarily tend to prove a higher present value."


24 275 U. S. 440, 48 Sup. Ct. 174 (1928). The case in the court below is discussed in notes in 41 Harv. L. Rev. 532 and 15 St. Louis L. Rev. 400.

After the rates involved in the principal case had been put in force and the superintendent had designated the classes to which they applied, the various companies brought separate actions contesting the validity of the rates and the constitutionality of the statute. The federal district court denied an interlocutory injunction on the ground that the companies had not complied with a stipulation in the prior proceedings under which they were permitted to charge the higher rates subject to restoring the excess to customers if the reduction should be sustained. There was dispute as to the terms and effect of the stipulation, but in *National Fire Insurance Co. v. Thompson*, 281 U. S. 331, 50 Sup. Ct. 288 (1930), Mr. Justice Butler found that it imposed the obligation to restore the excess and that the district court rightly denied the injunction until restoration was made.
the superintendent's computations were made, but there was no allegation by any one of them that the rates allowed to it were unreasonable or non-compensatory. The action was a joint one authorized by the state statute to secure a judicial review de novo of the superintendent's order. The Supreme Court granted certiorari but then dismissed the writ on the ground that no federal question was presented by a complaint based on the inadequacy of the rates by the test of the aggregate profits of all the companies. Mr. Justice Butler says that the Constitution does not safeguard aggregate profits sufficient to constitute just compensation for all. Such aggregate profits might not yield compensatory returns for individual complaining companies. A company receiving just compensation cannot complain because the application of the same rates to some of its competitors may infringe their constitutional rights. While no company would be able in the long run to collect higher premiums than those charged by its competitors, no company has a constitutional right to prevent the enforcement against its competitors of rates that are compensatory for them even though they are so low as to be confiscatory for it. The conclusion from the opinion is of course that the rates were fixed on a basis that affords no test of their constitutionality. The case seems to hold that objections confined to the methods of computation in applying an inappropriate standard are not directed to any test of the unconstitutionality of the resulting rates. Whether there might have been relief if the complaint had been directed against the inappropriateness of the standard of aggregate profit, rather than to the method by which aggregate profits were computed, may possibly raise a different question from the one passed upon by the court. Yet it is not unreasonable to infer from the opinion that the only test of unconstitutionality is to be found in the results of applying the rate to the business of the particular complainant.

A five-cent fare on certain lines of a street railway was contested as confiscatory in Georgia Railway & Power Co. v. Decatur,25 but the court did not pass on the question of confiscation, because it found the fare validly fixed by contract over part of the route and not justified by contract over the rest of the route. Mr. Justice Sutherland declared that the extension of the five-cent fare to territory to which the contract did not

apply was an impairment of the obligation of the contract by adding to its burdens. This strange doctrine would seem to imply that there is no power of rate regulation outside of contract. Very likely it was tacitly assumed that the five-cent fare was confiscatory. The opinion discloses that the commission fixed a seven-cent fare on concededly non-contract lines, and it appears from the brief that the company contended that the cost of service was 9.29 cents per passenger. The opinion gives no figures as to valuation or expenses or return.

In the companion case of Georgia Railway & Power Co. v. College Park, it was also held, without discussion of confiscation, that the application of the five-cent fare to an extension not covered by the five-cent contract was an impairment of the obligation of that contract.

In a number of cases the chief or only effort to support the rates objected to by the utility was founded on the contention that it was bound by contract whether the rate was compensatory or not. Where the contract is found to be controlling, there is no need to give details as to the effect of the rates. No figures are given in the opinion in Southern Utilities Co. v. Palatka in which a franchise contract for a rate of ten cents per kilowatt was held binding. The affirmance of a contract rate of $1.35 per thousand cubic feet for fuel gas in St. Cloud Public Service Co. v. St. Cloud left it unnecessary to pass upon the company's claim that it would require an increase to $3.39 to make the rate adequate. The binding contract for a five-cent fare established in Georgia Power Co. v. Decatur made immaterial the losses attributable to the line to which it applied. Here the cost of furnishing the transportation exceeded the revenue and there was less than no compensation for the use of the property. On non-contract lines the commission had allowed a fare of ten cents, subject to the requirement to sell four tickets for thirty cents.

In several cases in which the claimed contracts were found to have been abrogated or never to have been binding, the concession that the rates were confiscatory rendered it unnecessary.

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*262 U. S. 441, 43 Sup. Ct. 617 (1923).
*265 U. S. 352, 44 Sup. Ct. 492 (1924).
to discuss problems of valuation and return. Valuations had been made below in *Denney v. Pacific Telephone and Telegraph Co.*,\(^3\) and the master and the court had rejected those of the commission, but Mr. Justice McReynolds says nothing about them except that it is not contended that the rates would yield an adequate return. So also in *Railroad Commission v. Los Angeles Railway Corporation*\(^3\) he says only that it was conceded that the finding below with respect to the inadequacy of the five-cent fare is sustained by the evidence. Something more by way of recital is given by Mr. Justice Butler in *Paducah v. Paducah Railway Co.*\(^3\) in which he says that the company offered sufficient evidence to sustain its contention of confiscation and the city offered no evidence and made no serious claim that the rates were sufficient, if they could not be justified by contract. The company claimed an investment of $384,303 on which there should be an eight per cent return of $72,350.10. It showed that its actual return under the contested rates was less than operating expenses, including depreciation and taxes. The franchise basic rate was six cents. The company said it would need a basic rate of 13.5 cents to provide sufficient revenue at existing price levels, but in the hope of declining prices it offered a basic rate of ten cents. The six cent fare to which it was held was contained in a franchise of 1919 under which it began operations.

A temporary injunction against a schedule of telephone rates was affirmed in *Prendergast v. New York Telephone Co.*\(^3\) largely on the ground that the granting of such temporary injunctions rests in the sound discretion of the trial court, and that an order granting such an injunction will not be disturbed unless contrary to some rule of equity or the result of an improvident exercise of judicial discretion. The company had been required to give a bond to make restitution if the rates allowed

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\(^{30}\) 276 U. S. 97, 48 Sup. Ct. 223 (1928).


\(^{32}\) 261 U. S. 267, 43 Sup. Ct. 335 (1923).

by the temporary decree were later set aside. This protected the consumers as the injunction protected the company, and the decree was said by Mr. Justice Sanford to have in its favor the fact that it preserves the ultimate rights of both parties, as the denial of a decree would not. The company moved to dismiss the appeal, on the ground that a subsequent grant of higher rates by the commission established that the former were confiscatory. Mr. Justice Sanford rejected this on the ground that the later rates might still be questioned. He pointed out, too, that what might be right at a later time does not establish what was right under earlier conditions. The only reference to the valuation issue was the report of the finding of the district court that the fair value of the company's property could not be reduced much below $300,000,000, and that the prescribed rates could not possibly yield a fair return on such a valuation.

Questions of valuation were also left technically undetermined in *Banton v. Belt Line Railway Corporation* by reason of the finding that the company's share of the joint through rate prescribed would yield less than the specific costs of carriage. A commission order of October 29, 1912, had established the joint route, prescribed a fare of five cents per passenger, and assigned to the complainant two cents per passenger for its share of the joint carriage. The apportionment was not contested, and apparently the power to establish a joint fare was not in issue, although the company had earlier filed a petition with the commission requesting its elimination. The commission itself had in preliminary proceedings raised the joint fare to seven cents, but the carrier had objected to this as insufficient, and no final determination of the matter was had, so that the effect of the commission action was to command continued compliance with the order of 1912. On suit to enjoin the order as confiscatory, an injunction was granted by the district court. The company presented figures showing that operating expenses and taxes were more than two cents per passenger. The master found that the transfer traffic would cost more than twice what it would yield, and the district court found that the expense would be slightly in excess of the yield. Mr. Justice Butler finds that

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the evidence justifies the conclusion that the returns would not equal the expense, and the decree of the district court enjoining enforcement of the order is confirmed.

The only question in *Arkansas Railroad Commission v. Chicago, R. I. & P. R. Co.*[^268] was whether a carrier was justified in raising intrastate rates in order to make them correspond with a raise in interstate rates. The former intrastate rates had been fixed to comply with an order of the Interstate Commerce Commission with respect to the relation between interstate and intrastate rates. When this Commission later raised the interstate rates, the carrier professed to assume that the earlier order required a corresponding increase in the intrastate rates. Mr. Justice Brandeis found that the later order of the Interstate Commerce Commission refused to command an increase of Arkansas local rates and that it therefore confined the earlier order to a parity between the rates then existing and kept it from applying to later changes. He remarked that it would be well for a carrier, in case of doubt as to the effect of an order of the Interstate Commerce Commission, to apply to that Commission for a ruling on the point, rather than to proceed to act on its own interpretation. The proceeding in the principal case started by an injunction in the federal district court against the order of the state commission in suspending for examination a commodity tariff filed by the carrier. The decree enjoining the order was reversed by the Supreme Court. No questions of valuation or remuneration are presented in the opinion.

No question of valuation was involved in *Northern Pacific Railway Co. v. Department of Public Works*[^37] in which a carrier complained that existing rates on intrastate transportation of logs did not defray the operating costs of the traffic and its share of taxes, and objected to an order of the state commission reducing them. The carrier offered detailed testimony in support of its contention. The commission made little direct effort to refute this, but relied on an estimate as to the cost of the log traffic by assigning to it a share of the operating cost of all freight traffic over the systems of the roads involved, without taking account of specific differences in the kind of merchandise, the length of haul, the density of traffic, or the character of the

route. This, said Mr. Justice Brandeis, was a fundamental error which vitiated the whole process by which the commission reached its conclusion, and made the conclusion an arbitrary act wanting in due process because of absence of evidence to support it. The state court was reversed for denying relief in an action by the carrier to set aside the order.

Another contest over a particular rate on intrastate carriage of logs arose in Chicago, M. & St. P. R. Co. v. Public Utilities Commission as a result of the decision of the state court sustaining an order of a commission to reduce existing rates by ten per cent. The carriers had offered evidence tending to show that operating expenses chargeable to the intrastate log traffic did not equal the revenues therefrom. Both commission and state court refused to consider and give weight to that evidence, basing their refusal on the conclusion that the intrastate carriage of logs was contributory to the subsequent long interstate haul of lumber and that, therefore, the two operations should be considered together and the carriers were not entitled to contest the intrastate log rates without showing the results of the whole carriage before and after metamorphosis. This was held to be a fundamental error. The carrier cannot justify intrinsically excessive interstate rates on lumber because of losses on intrastate rates on logs, nor can it be required by the state to haul the logs at inadequate compensation because of the possibility of recoupment from the interstate rates on lumber. The methods by which the commission reached its conclusion were declared by Mr. Justice Butler to be arbitrary and to constitute a denial of due process of law. The Interstate Commerce Commission had permitted but not commanded the reduction of the interstate rates on logs. The state commission's command to make corresponding reduction of the intrastate rates was criticised because of its effect in destroying the relation between intrastate and interstate log rates in the same territory.

No decision on the merits was rendered in Pacific Telephone & Telegraph Co. v. Kuykendall in which the district court was reversed for denying an injunction on the disapproved finding that the petitioner had not exhausted its administrative remedies, and the case was sent back for hearing on the sub-

\[265\] U. S. 196, 44 Sup. Ct. 553 (1924).
stantive issue. Mr. Chief Justice Taft states that the averments of the bill show a clear case of confiscation. These include allegations that the “fair and reasonable value” of the property was some $35,000,000, with no inclusion of anything for franchises or for “going concern,” that the company was entitled to eight per cent as a fair return on this value, and that the highest returns under the rates complained of were 4.97 per cent on cost and 3.67 on present fair value. The opinion includes no statements as to actual returns, or methods of computing expenses or depreciation.

In the companion case of Home Telephone & Telegraph Co. v. Kuykendall the allegations are of a cost of over $4,000,000, a present value of $5,710,684, a necessary return of 8 per cent, and an actual return in the best year of 3.07 per cent on cost and of 2.28 per cent on “fair value.” In this case, too, the decree denying an injunction was reversed and the cause remanded for hearing on the merits.

The facts in Smith v. Illinois Bell Telephone Co., as conceded by motion to dismiss, showed deficits of $48,000 and of $65,000 for the past two years, after paying operating expenses and taxes and with no deduction for depreciation. The alleged fair value of the property, including working capital and going value, was $3,800,000. The district court had enjoined the commission from the further enforcement of the existing approved schedule of rates and from taking any steps against the company by reason of the collection by it of rates under a higher proposed schedule. This was affirmed by a unanimous court, Mr. Justice Stone not sitting. The opinion of Mr. Justice Sutherland is concerned with the question whether the complainant had exhausted its legislative remedies before appealing to the court. Long delay by the commission in passing upon the proposed new schedule was held to be a sufficient reason for seeking judicial relief without further poking at administrative procrastination.

41 270 U. S. 587, 46 Sup. Ct. 408 (1926).
42 At the succeeding term of court another controversy between the same parties with respect to rates in the Chicago district was reviewed by Mr. Chief Justice Hughes in Smith v. Illinois Bell Telephone Co., 282 U. S. 133, 51 Sup. Ct. 65 (1930), and the injunction granted by the court below was set aside and the case remanded with direction to make more specific findings as to annual depreciation, apportionment of interstate and intrastate operations, and the fairness of contracts
No details of valuation are given in the opinion of Mr. Justice McReynolds in *Ottinger v. Consolidated Gas Co.*\(^4\) which affirmed the district court in enjoining as confiscatory a rate of $1 per thousand feet for gas of 650 British thermal units. This rate had been fixed by statute after the commission had fixed a rate of $1.15 per thousand for gas of 537 thermal units, following a Supreme Court decision declaring confiscatory the further application of an old statute prescribing an eighty-cent rate. The commission accepted the district court’s decision denouncing the new legislative dollar rate, and did not appeal. The state attorney general took an appeal, apparently contesting the judgment that the rate was confiscatory. Mr. Justice McReynolds says that the master took evidence and reported on valuation and expenses and concluded that the new rate would yield less than six per cent on the value, and was therefore confiscatory. To this he adds that the district court agreed with the master and that the attorney general offers nothing in argument to justify the reversal of the decree so far as it directs appropriate injunctions. Since, however, the finding of confiscation was sufficient to dispose of the quarrel, the decree of the district court is modified to confine it to the enforcement of the rate against the complainant without enjoining enforcement generally or without decreeing that the acceptance by the company of an earlier rate constituted a binding agreement between it and the state. Mr. Justice Brandeis confines his concurrence to the result.

This decision was followed in *Ottinger v. Brooklyn Union* for supplies and service between the company and its affiliates in the American Bell system. While the Chief Justice says nothing which explicitly indicates disapproval of criteria laid down in previous decisions, the general tenor of his opinion seems less lenient toward company claims than were the opinions and the decisions of the majority of the court during the eight years prior to his return to the bench. Thus, though he recites the previous ruling that property acquired by use of reserves for depreciation is to be included in the rate base, he adds that “the recognition of the ownership of the property represented by the reserve does not make it necessary to allow similar accumulations to go on if experience shows that those are excessive.” Quite immaterial from the standpoint of the reproduction cost of the property at present prices is the further statement that “the record of the Illinois Company shows that for many years it has been able to expand its business so as to meet increasing demands, to pay its operating expenses including interest on money borrowed, to pay dividends of eight per cent upon its capital stock, and to accumulate a surplus.”

\(^4\) 272 U. S. 576, 47 Sup. Ct. 198 (1926).
Gas Co., \textsuperscript{44} in which the only difference was that in the case of the companies here involved the master found that the dollar rate would yield a return of less than five per cent on the value. According to Mr. Justice McReynolds the records in these cases were voluminous, but we are left without recital of anything but the master's conclusions. Evidently the master irked him a little, for he calls his report "too much burdened with unimportant dissertations" and "somewhat oracular—as in the lines which make solemn declaration concerning the position which this court must ultimately take regarding valuations in rate cases."

A decree of the district court, which enjoined the further enforcement of a five-cent fare on the New York subways and affiliated elevated lines, was reversed in \textit{Gilchrist v. Interborough Rapid Transit Co.} \textsuperscript{45} on the ground that the complainant had not exhausted its administrative remedies and for the further reason that the issue whether the company was restricted by contract to a five-cent fare depended upon intricate questions of state law which the federal courts should not attempt to pass upon in advance of a determination by the state court. The claim that the five-cent rate is confiscatory depended upon the assumption that the subways and the elevated lines are to be treated as a unit. The subways were owned by the city. The elevated lines were privately owned and were leased to the company operating the subway. Mr. Justice McReynolds says that on the record before the court it cannot be assumed that subway and elevated operations must be regarded as a unit. The income of the elevated above operating expenses and taxes was about $4,000,000, and the payment due from the lessee to the lessor under the lease was about $8,000,000, so that the five-cent fare on the elevated was clearly confiscatory so far as the lessee was concerned. The opinion does not disclose whether the court thinks that the issue of confiscation should be determined upon the basis of the contract situation of the operating company or upon the valuation of the leased lines.

\textsuperscript{44} 272 U. S. 579, 47 Sup. Ct. 199 (1926).
\textsuperscript{45} 279 U. S. 159, 49 Sup. Ct. 282 (1929), considered in 30 Colum. L. Rev. 527; 4 Notre Dame Law 564; and 4 St. Johns L. Rev. 76. For discussions prior to the Supreme Court decision, see John Bauer, "The New York Rapid Transit Contracts Before the Supreme Court," 7 N. Y. Univ. L. Rev. 120; and notes in 28 Colum. L. Rev. 812; 17 Nat. Mun. Rev. 348, 703; and 18 Nat. Mun. Rev. 47.
It observed that the present value of the elevated lines "is very large, but to determine this with fair accuracy would be exceedingly difficult." From the operation of the subways the company was realizing some $17,000,000 annually. It claimed that it was entitled to an eight per cent return on their value estimated at $600,000,000, or $240,000,000 over their cost. These subways are the property of the city and are declared by statute to be public streets. The claim that their value should be taken as the basis for estimating the return, said Mr. Justice McReynolds, "is unprecedented and ought not to be accepted without more cogent support than the present record discloses." The only property connected with the subways to which the lessee had title was operating equipment costing some $60,000,000, real estate valued at $300,000, and some office equipment of small value. In addition it had advanced under the contract $58,000,000 toward the construction. So far as appears, it could claim no return on this except under the contract. These comments of Mr. Justice McReynolds on the separate identity of elevated line and subways and on the property of the company in the subways on which it is entitled to a fair return do not constitute adjudications, but they suggest the interesting predicament in which the company might find itself if it should ever be held that the fare contract had been abrogated, that the elevated was an enterprise distinct from the subway, and that the fair return on the subway was to be based on the property owned by the company. No increase in rates would be likely to make the elevated remunerative to the lessee, and the loss of the high profits on subway operations by reduction of the subway rates would end the surplus that may now compensate for the elevated deficit. It may well be that the contract that fixes a five-cent fare is one that the company has reason to be grateful for. The injunction against the five-cent fare, which the district court had granted, was an interlocutory one. The Supreme Court granted a stay which kept the five-cent fare in operation. After a re-argument, the decree of the district court was reversed. Without revealing their reasons, Justices Van Devanter, Sutherland and Butler dissented.

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(To be continued.)