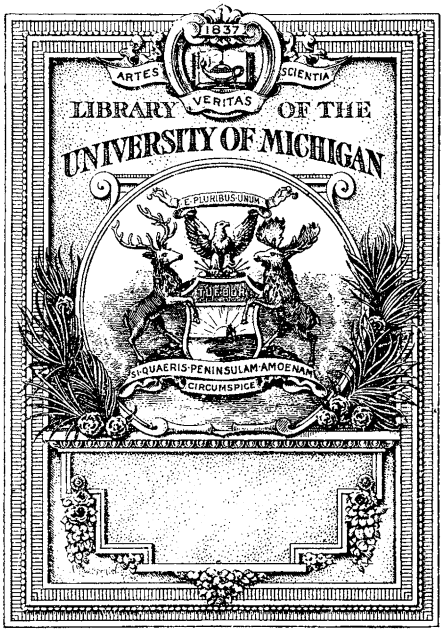
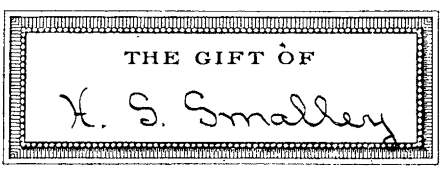



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RAILROAD RATE CONTROL

IN ITS LEGAL ASPECTS

A STUDY OF THE EFFECT OF JUDICIAL DECISIONS UPON PUBLIC REGULATION OF RAILROAD RATES.

BY

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1905.

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INTRODUCTION.

The following chapters are devoted to one of the phases of the railroad problem. Their purpose is to disclose the relation which has come to exist in this country between the courts and the railroad commissions. To this end they attempt to trace the development of what is termed the doctrine of judicial review—the principle that the courts have jurisdiction to review rates made by commissions and to restrain the enforcement of such as may be found unreasonable. They next endeavor to determine how seriously this doctrine, in its practical application, has affected the efficiency of such commissions as are empowered to establish schedules of railroad rates. And finally, from the difficulties thus disclosed, they venture to point out the possible avenues of escape.

Manifestly the discussion of a subject which involves but one phase of a problem, cannot appear in its proper light without some preliminary exposition of the problem as a whole. Yet so thoroughly familiar are most of the aspects of the railroad problem that their extended treatment must be entirely unnecessary. Accordingly the author has confined himself, in the first chapter, to a portrayal in barest outline of the historical back ground of the problem and of its basis in economic theory. Only those matters which bear a very important relation to the particular question discussed in the later chapters, are subjected to comment of any length. Indeed the whole purpose of the preliminary chapter is to cast the light of history and of theory upon the problem of judicial review, in order to discover its significance, and to determine the point of view from which it should be regarded.

It will be noticed that throughout the work reference is made only to rates established by state commissions, and to the judicial doctrine pertaining thereto. That doctrine, as will be shown, is based upon the Fourteenth Amendment to the Federal Constitution, which forbids each state to deprive any person of property without due process of law, or to deny to any person within its jurisdiction the equal protection of the laws. Up to the present time, therefore, the judicial doctrine has operated only as a restraint upon state railroad control. But the significance of the doctrine is much broader than that fact would imply. For the Fourteenth Amendment, in so far as it attempts to preserve the rights of private property from invasion by the states, has a counterpart in the Fifth Amendment, which forbids the national government to take property without just compensation and without due process of law. It is evident, therefore, that should the federal government ever attempt to fix railroad rates the doctrine of judicial review would be extended to embrace such regulation.

At the present writing (April 14, 1906) it seems probable that before long Congress will enact a rate regulation law, and should that event occur the matter will at once become of great importance. For even if an amendment providing specifically for judicial review should not be incorporated in the act, the courts would nevertheless possess that right just as fully as they now do in regard to state control. Even a provision for judicial review to determine whether rates are "fairly remunerative" would not change the scope of the judicial investigation, for that, as will be seen, is the purpose of judicial review under the Constitution. Thus the courts would assume the same relation to the Interstate Commerce Commission that they now maintain toward the state commissions, and consequently the same serious difficulties which

now confront the states would await the agencies of national control.

But the doctrine of judicial review is of even wider importance, in that it applies not only to the regulation of railroad rates, but to public control of charges in other lines of business as well. Whether the doctrine elaborated in railroad cases is to govern the courts in passing upon charges prescribed by the legislatures for *private* industries which have become so far affected with a public interest as to be subject to government control of their rates—such as warehouses and stock yard companies—is not clear, especially in view of such cases as Budd vs. New York, Brass vs. Stoeser, and Cotting vs. Kansas City Stock Yard Company. Mr. Justice Brewer's remarks in the last named case, though uttered *obiter,* are interesting because of their suggestion of a different form of review in cases involving industries of this kind. However that may be, there is no doubt that the doctrine of judicial review worked out for railroads applies also to the regulation of other forms of *public* business. And so the same restraints placed upon government control of railroads exist in the case of all public service or quasi-public corporations, limiting, for example, the public regulation of street railway fares, and of gas and water rates. These facts lend additional interest to the following inquiry as to the limits which the courts may set, under our Constitution, to public control of railroad rates, and as to the justice and expediency of such limitation.

CHAPTER I.

PUBLIC REGULATION OF RATES.

Public control of railroad rates has existed in this country for hardly more than a third of a century. Prior to about 1870 it was the policy of our governments, both state and national, to let railroad traffic matters alone. Indeed, with the exception of a few statutory provisions designed to promote security of life and limb in the operation of railroads, no public regulation of any kind was attempted. On the contrary, the American governments very generally encouraged and supported railroad enterprises through substantial grants of land and money. That railroad companies would ever require any considerable measure of restraint or control was not at first imagined, for they were regarded as public benefactors. And that there could be anything hostile between their interests and those of the public was not apparent until many years had passed and our railroad system was fairly well developed. When the fact did appear, however, many of the states were not slow to adopt a definite policy of regulation, in which lead they were followed in 1887 by the Federal Government. The initiation of this policy, then, was not the result of speculations concerning the proper functions of the state, but on the contrary was caused by the appearance of serious abuses in railroad management, and by the realization that they were the inevitable consequence of unrestricted private control. What these abuses are, and in what characteristics of the railroad industry they have their origin, it is important to observe in order to appreciate the significance of those measures which the public has adopted for their correction.

In any statement of railroad evils attention is most naturally directed first to unjust discrimination, as the most serious of all. "Discrimination" is a term which, as applied to railroads, embraces, if it does not cover, a multitude of sins. The forms which unjust discrimination may take are myriad. There may be undue preferences in rates as between persons, or communities, or commodities, or connecting lines. Again, the preference may be involved, not in the rates themselves, but in personal favors to the fortunate shipper, or in the character of the service rendered, as in a most abundant car supply, or more expeditious carriage. When involved in the rates, however, the discriminations may be effected through differences not only in the charges for carriage, but in the charges for other services, such as loading, switching, storage, and demurrage. Discriminations in rates may be public, appearing in the printed schedules of the company, but in the vast majority of cases they are privately made. When so made they most commonly take the pernicious form of secret rebates, though not infrequently they are effected through the equally vicious practice of false billing. But there are innumerable other ways. Quite recent investigation has brought to light the discriminations concealed by the incorporation of the so-called "industrial roads." "Midnight schedules" are also a late discovery—so far as the public is concerned—and the private car abuses are also fresh in mind. So far as passenger traffic is concerned, the connivance of railroads with scalpers has long been a familiar story. In these, then, and many other ways do the railroads too frequently succeed in evading their duty as common carriers to serve all on equal and reasonable terms.

The mere enumeration of these practices, however, is sufficient to prompt the inquiry as to why railroad man-

agers are disposed to indulge in them, since they must mean in many cases a reduction in revenue, and in all cases must tend to complicate the already difficult administration of the property. In reply it may be said that railroad managers do not often desire to discriminate, that on the contrary they are usually loath to do so, but that they are driven to that course whether they will or no. Under the conditions of competition as it prevails among railroads, there is no alternative except between discrimination and speedy insolvency.

The explanation of this fact is found in one of the characteristic features of the railroad industry, namely, the relation between expenses and volume of traffic. Expenses increase but slightly when traffic increases greatly. This is true not only because the fixed expenses of any railroad company are so large a proportion of the whole, but because even the variable items of expenditure do not begin to keep pace with the growth of traffic. These facts lead to two important immediate results. In the first place, railroad managers are under a constant and powerful incentive to get business even at reduced rates. They realize that an increase in traffic means a much more than proportional increase in net earnings; in other words, augmented business means a decided reduction in the cost of carrying each unit of traffic. Since this is so, they are not only inspired to seek customers in all the commercial highways and hedges, but they are also strongly tempted to accept traffic at reduced rates—indeed to offer reduced rates in order to secure it. But now a second consequence of this peculiar relation between expenses and volume of traffic is, that it is utterly impossible to determine what any given service will cost the company.[1] A traffic manager, therefore, tempted as

[1] It is not only impossible to determine in advance the cost of rendering any particular service, but it is impossible to discover what that cost has been even at the end of the year when all accounts are

he is to accept each item of traffic if need be at a reduced rate is entirely without data which would enable him to fix the point below which a rate would be unremunerative. Such being the case, his conduct under the stress of competition is most natural. He offers whatever rate is necessary to get the business away from his rivals, devoutly hoping all the time that the rate will not prove injurious to his road, but utterly without means of judging its effect. The outcome is that traffic managers are swayed by an impulse to accept traffic at almost any rate, if compelled to do so by competition. "Get business" is their motto. "Get it at a high rate, if possible; at a low rate if necessary; but *get* it."

The consequences of this fact are familiar to all. Competition between railroads is fierce and intense, and constantly tends to develop into the "cut-throat" variety, ending perhaps in the all too familiar "rate wars." Dominated by the passion for traffic, eager to snatch it from competing lines, each road cuts rates wherever necessary, or offers other advantages to get the traffic for itself. And thus swarm into industrial life that horde of evils to which allusion has been made—the evils of unjust discrimination. Thus are railroad managers compelled by the exigencies of their business to wield unceasingly a tremendous power through which one man, one industry, one town may be built up, while others are crippled or destroyed. Of course it may happen that a powerful industry may secure such an influence in the control of a railroad that discriminations may intentionally be

in. It is practically impossible to apportion the total expenditures among the various kinds of traffic—freight, passenger, milk, express, and mail. And even if the freight expenses could be determined, it would be impossible to apportion them among the various individual items, so as to determine cost of carriage, terminal expenses, etc., of each, or even the total cost of each. Cost keeping is impossible in the traffic department of a railroad.

made for the purpose of crushing the former's rivals; but even where this element is lacking, unjust discrimination is not only a possibility in railroad management—it is a natural and inevitable consequence of all unrestricted railroad competition. Railroads do not usually wish to discriminate, but they are compelled to do it. Discrimination *may* drive them into bankruptcy, but abstinence from it is *sure* to do so, so long as competition persists. They discriminate in order to live—though their discrimination may sometimes kill them.

A second railroad evil hardly less serious than that just considered, and certainly no less the outgrowth of causes inherent in the business, is extortion. The imposition of exorbitant charges is in large measure a consequence of monopolistic elements in the railroad industry. Many communities enjoy the services of but one railroad, and of no other means of transportation; and while the number of such places is at present slowly diminishing, there is no doubt that to the end of time the number will continue large. Of course as to such points there can be no competition at all. Even potential competition almost wholly fails as a restraining force, because of the immense cost of duplicating a railroad's plant and equipment, and because of the long time which the process of duplication must consume. The railroads are consequently free, in the absence of government control, to fix rates on the monopoly principle of maximum net return. The only practical limitation upon their power is that which arises from the influence of rates at competing points upon rates at intermediate points, but even this, as experience has abundantly shown, is wholly inadequate. Extortion may exist, moreover, even in the presence of competition. The nominal, or public rates applying to competing points may themselves be exorbitant. Of course discriminations, as already explained, result in a lower charge being

exacted from most shippers, but the small or innocent shipper may very likely have to pay the scheduled rate. And of course arrangements such as pools, consolidations, or communities of interest, may be made which destroy competition in whole or in part, temporarily or permanently. To the extent to which such arrangements are effective, rates are subject to the arbitrary control of the railroads. The public has no guarantee of reasonable charges.

A third evil of private railroad management is instability in rates. The industrial interests of every community demand that railroad charges shall be stable. The transportation factor is an essential one in all industries, and accordingly an element of transportation expense is present in the cost of practically every commodity. For railroad rates, therefore, to be unstable is to introduce an element of serious uncertainty into all business. That this is a highly undesirable thing needs no argument. Yet the fact that the public interest demands stability in rates is not always a conclusive argument with the traffic manager. Private railroad management furnishes no guarantee that rates, once established, will remain unaltered until changing industrial conditions demand their alteration.

Such are the principal evils so far as rates are concerned, which have grown up with the development of the railroads, and against which legislation has been directed.[2] Through just what measures the public has endeavored to abate these mischiefs, it is now appropriate for us to inquire.

[2] Certain other evils, such as the granting of free passes to public officers; attempts to evade or limit liability; and incompetent or negligent maintenance and operation of roads, are not dealt with here, as they are not of importance in connection with the subject of this work.

Legislation designed to prevent unjust discriminations has, up to the present time, taken chiefly the form of prohibitions against such practices, coupled with penalties for infraction of the law. In many states railroad comsioners have been charged with the duty of discovering violations of the law, and of directing against the guilty parties the prosecuting agencies of the government, but in many other states these agencies have been left without special assistance in this work. Leaving out of account a few minor provisions of law, our governments, both state and national, have rested content with this merely prohibitory legislation.

Against extortion also have been leveled prohibitory statutes, reinforced with penal provisions. To these have been added other laws forbidding the merger or consolidation of competing railroad companies, and declaring that no arrangements in the nature of a pool shall be enforcible at law. These provisions have been designed to preserve competition wherever it exists, thereby preventing the companies from fixing monopoly rates. In addition to these two classes of laws, a number of states, as well as the United States, have endeavored to solve the problem through the appointment of railroad commissions invested with a general authority to supervise railroad companies, and, among other things, to advise with them in regard to their rates. The majority of states, however, which have established commissions, have gone further than this, and have empowered their commissions actually to fix rates for the railroad companies. In some instances the legislatures have themselves exercised this power and have passed maximum rate laws. Thus it is seen that the states have resorted to several expedients to obviate the danger of exorbitant railroad charges.

The measures which have already been mentioned are also designed to secure stability in rates. Laws against

unjust discrimination and extortion, insofar as they are successful, must necessarily prevent those disturbances in schedules which are so injurious to all business. And especially effective in producing this result must be the public regulation of rates. No further measures, therefore, peculiar to this difficulty, have been alopted by the states.

In these various ways, then, have our governments endeavored to correct the evils of private railroad management. How, now, let us ask, have these attempts at control been regarded by the companies? To which, if any, have they offered resistance in the courts?

While railroad companies have no doubt often felt that they were being much abused, they have made no serious effort to disprove the validity of certain laws. Thus those general provisions requiring reasonable rates and service, forbidding unjust discrimination and extortion, have been generally recognized as within the proper scope of legislative power. So also anti-pooling and anti-consolidation clauses, being no more than adaptations to modern conditions of the old common law rule on restraint of trade, are generally acknowledged to be valid. Even an advisory commission empowered to recommend changes in rates is conceded to be a proper creature of the police power. Such methods of control as these, railroads have as a general rule refrained from resisting in the courts. They have rather exercised their ingenuity to discover methods of rendering them nugatory in practice.

But the case has been entirely different with statutes fixing rates or establishing commissions with power to fix rates, From the very beginning of railroad control the companies have resisted such laws with tireless energy. Case after case has been started, and very few which in the trial courts have been decided adversely to the roads,

have been abandoned until a ruling has been obtained from the Supreme Court of the United States. Every argument has been used to defeat these measures of public regulation, and the ablest counsel in the country has been employed in the attempt to accomplish that end.

The grounds upon which the resistance of the railroads has been based are four in number:

1. That the legislature has no right to fix rates.

2. That, even conceding that right to the legislature, some of the state laws have been void insofar as they have attempted to regulate interstate commerce.

3. That, again conceding the legislature's power, the charters of some companies exempt them from its exercise.

4. That, still conceding the legislature's right, its power is not absolute, but the rates are subject to review by the courts. Rates ought to be reasonable, even if made by the state, and whether they are or not is a judicial question, and cannot be conclusively determined by the legislature.[3]

Let us examine each of these contentions, and the reply which has been made to it by the Supreme Court of the United States.

I. It was most natural that railroad rate regulation should first be most vigorously resisted on the broad ground that the legislature is without constitutional power to fix rates, directly or indirectly. The spirit of our institutions—legal, political and economic—contemplates the widest possible freedom of individual action in industry, and limits the play of government interference within very strict bounds. Especially are prices, rates, and

[3] In addition to these objections it will be recalled that the power of the Interstate Commerce Commission to fix rates was successfully resisted on the ground that Congress never intended to confer it upon the Commission. See I. C. C. v. C. N. O. & T. P. Ry. Co., 167 U. S. 479.

so forth left to the determination of competitive forces. But this is not all. The constitution of the United States contains in unmistakable terms a guarantee of the rights of liberty and property, as against both the federal and state governments. In view of the former fact it is not altogether surprising that the railroads should have at first regarded governmental control of rates as a denial of fundamental rights which have been the product of centuries of Anglo-Saxon history. In view of the latter fact, it was inevitable that they should promptly call in question the constitutionality of such measures of control. In the first cases which arose, therefore, this argument was pushed to its farthest limit, and the question was thus squarely presented as to whether rate control is an infraction of the Constitution, or, on the other hand, is a proper exercise of the recognized police power of the states.

The so-called " Granger-Cases " were the first in which this question was at issue, and were the cases in which it was definitely determined.[4] In those cases the right of the legislature to regulate rates was firmly established, and in those and succeeding cases the basis on which that right reposes was clearly stated. The railroad business is essentially a public business, and, therefore, railroad companies, though private corporations, have devoted their property to public use and are discharging a public function. This being the case, it naturally follows that in the employment of their property, in the conduct of their business, railroad companies must be subject to pub-

[4] The " Granger Cases " were eight in number, and all arose under the " Granger Laws " which had been passed in Illinois, Iowa, Wisconsin and Minnesota. The leading case, Munn v. Illinois, involved the validity of a statute fixing maximum rates for the storage and handling of grain in public warehouses, but all the other suits dealt with railroad laws. See table of cases for their titles. All of the cases ultimately reached the federal Supreme Court and were decided in 1876. They are reported in 94 U. S. 113, *et seq.*

lic control. It would be intolerable that the management of a public industry, and especially rates to be charged by it, should be left to the ungoverned whim of private parties, to whom the state had delegated its function in order that the public might be served. The right of the state to control rates, therefore, flows from the very nature of the railroad industry.

That the railroad business is public in character is a proposition which the Supreme Court has maintained upon three separate grounds, each of which would seem to be sufficient in itself. In the first place a railroad company is a common carrier, and, as was said by Mr. Chief Justice Waite, "common carriers exercises a sort of public office, and have duties to perform in which the public have an interest."[5] In another of the Granger cases he added: "Railroad companies are carriers for hire. They are incorporated as such, and given extraordinary powers in order that they may better serve the public in that capacity. They are, therefore, engaged in a public employment affecting the public interest and (are) subject to legislative control as to their rates of fare and freight."[6] And this control of the rates of common carriers, as the Chief Justice pointed out, was exercised as long ago as the third year of the reign of William and Mary.[7]

In the second place a railroad is a public highway, and it has always been recognized that the creation and maintenance of public highways is a function of the state. A railroad company, therefore, is engaged in a public business. "A railroad is a public highway," declared Mr. Justice Harlan in Smyth v. Ames, "and none the less so because constructed and maintained through the agency of a corporation deriving its existence and powers

[5] Munn v. Illinois, 94 U. S. 130.

[6] C. B. and Q. Rd. Co. v. Iowa, 94 U. S. 164.

[7] 3 W. & M., c. 12, Sec. 24.

from the state. Such a corporation was created for public purposes. It performs a function of the state." [8]

In the third place, the grant of the right of eminent domain and its use by railroad companies is incontestable proof of their public character. A fundamental principle of the law of eminent domain is that the power shall be exercised for a public purpose and for a public purpose only.[9] The grant of that power to a railroad is therefore tantamount to an assertion by the state that a railroad's business is public—that its property is devoted to a public use—and the acceptance of the power by the company is likewise equivalent to a confession of that fact. Were it not so the exercise of the power by the railroads would be wholly unjustifiable.[10] Closely allied to this consideration is another. In this country railroads have been the beneficiaries of much public aid. In many places taxes were once levied to assist the companies in the construction of their roads; and whatever may be said as to the wisdom of this policy, the validity of these taxes, in the absence of special constitutional restraint, is beyond doubt. Yet it is also a fundamental rule of the law of taxation that the power shall be used only for a public purpose. Therefore it may be said here, as was said of the eminent domain, that the levying of the taxes was an assertion by the state, and the acceptance of their benefits an admission by the railroads, that the industry is public.

But while we have here three grounds on which it is possible to argue that the railroad business is public, it will be observed that there is an important distinction between the first two and the last. The first two are

[8] 169 U. S. 544. See also Lake Shore, etc., Ry. Co. v. Smith, 173 U. S. 690.

[9] Cooley; Constitutional Law, 3rd ed., p. 366.

[10] See Smyth v. Ames, 169 U. S. 544.

causes of the public character of the industry; the last is a consequence of it. Railroads are public because the roads are public highways and the companies common carriers; but they are not public because the powers of eminent domain and taxation have been exercised for their benefit. In other words, the exercise of these powers has not created publicness in the industry, for they cannot lawfully be used except for a purpose that is already intrinsically public. Their exercise, therefore, is not the cause of publicness, but rather a test or proof of it. And it furnishes a good argument for the validity of government control, for the railroads, having received the benefit of these important sovereign prerogatives, are forever estopped from denying the public character of their business—a character but for which the use of these powers would have been unlawful.

The railroad industry is therefore a public industry,[11] and because of that fact it is subject to legislative control as to its rates. This legislative power extends of course to all business of a public character, and therefore applies not only to railroads but to all public service corporations, such as other common carriers, municipal lighting, water and street railway companies, and so forth. It is well established, however, that the right of a legislature to regulate rates and prices extends not only to such industries as these, but to others which are not public in character as well. This fact and the reason for it, have frequently tended to produce confusion of thought as to the real legal basis of railroad control. At the risk of a digression, therefore, it seems advisable to inquire into the ground upon which the Supreme Court sustains a legislature's right to fix prices for a non-public industry, in order that the ground upon which railroad control is based may be clearly distinguished.

[11] See Lake Shore, etc., Ry. Co. v. Smith, 173 U. S. 690, 696.

The general doctrine of the Court is that when property is "clothed with a public interest," or "devoted to a use in which the public has an interest," it becomes subject to legislative control as to its price, or as to the rates for its use. The doctrine in this form has been vigorously assailed, as far too sweeping and as lacking in definiteness. What is to limit the discretion of the legislature? the opponents of the doctrine inquire. Is it not true that almost *all* business is affected with a public interest? What industry is there in which the public has not some measure of concern? Yet must all prices be liable to variation at the whim of a legislature? Such questions suggest the criticisms which have been made again and again and which have come from members of the bench as well as from the general public. Mr. Justice Brewer, for example, while upholding in no uncertain terms the power of a state to control public industries, such as railroads, submitted a most spirited dissent from the opinion of the Court in Budd v. New York [12]—a case in which a statute imposing rates of charge for warehouses was upheld by the majority of the court.

But in spite of criticism, the doctrine as a general proposition has become firmly established. It is subject, however, to considerable limitation. Not all business which is clothed with a public interest is subject to legislative control of its rates—but only such industries as exhibit qualities or peculiarities which mark them as fit subjects for public control. But what are the characteristics which will have this effect? This question cannot be answered with perfect definiteness, for the Court has never marked out clearly all of the limitations of its doctrine. Certain general ideas are involved in its decisions, however, and may be stated, There can be no doubt whatsoever that if an industry is public in char-

[12] 143 U. S. 517.

acter it is "affected with a public interest" in a sense which completely justifies public control. This is doubtless the most intense form which the public interest can assume. But a less intense interest, that is, interest in a non-public business, may also be sufficient. Thus in Munn v. Illinois, a statute fixing the charges for warehouses was sustained. The warehouses concerned were held to have become sufficiently "clothed with a public interest," apparently for two reasons: first, because of the general use and great importance of their service, and secondly, because they presented the case of a "virtual monopoly." A third consideration may be found, for example, in the regulation of rates for hacks and carriages, namely, a grant by the government of special privileges. So also a long standing custom of fixing prices of a certain sort may be deemed to impart a sufficient element of public interest, and to justify a continuance of the practice. It will not do to take any of these considerations in its full meaning, however. None of them will *always* be sufficient to justify public control. Thus the mere fact that an industry is of use and great importance is not sufficient, or our legislatures would be fixing the price of coal, ice, food, clothing, steel, and a score of other commodities, as well as rents. Nor have we any reason to believe that a "virtual monopoly" will under all circumstances subject an industry to price control. Were that so, our legislatures would possess a more powerful weapon against the Trusts than they now seem to suspect. Nor, again, can the grant of a special privilege be always sufficient—otherwise all corporate charters, at least all special charters, would imply a power in the state to fix prices for the corporation. It is not even certain that the dignity of age will always justify a continuance of legislative price making. It is more than possible that an effort to fix the price of bread, formerly

a common practice, could now be successfully resisted. Thus it seems evident that no hard and fast rule can be laid down as to the potency of any of these elements to create a public interest sufficient to justify price control. All that can be said, therefore, is that the presence in an industry of one or more of these elements (and perhaps others not yet disclosed by the Court) will under certain circumstances and conditions,—to be judged of in each case by the Court—be deemed to have clothed the industry with a public interest, sufficient to subject it to public control. Thus the class of industries so subject is not a definitely determinable one, but must gradually change with the evolution of industry.[13]

But whatever uncertainty may attach to the control of prices in industries private in character, and however difficult it may be to define the exact grounds on which such control is based, no suspicion of uncertainty or difficulty appears in the regulation of railroad rates. The public nature of the railroad industry is a full and sufficient justification of the control. True it is that in that industry there are other features of public interest besides its public character: the elements of monopoly, of general use and importance, and of special privileges

[13] As said Mr. Chief Justice Waite in speaking of warehouses: "Certainly if any business can be clothed 'with a public interest and cease to be *juris privati* only,' this has been. It may not be made so by the operation of the Constitution of Illinois, or this statute, but it is by the facts. . . . Neither is it a matter of any moment that no precedent can be found for a statute precisely like this. It is conceded that the business is one of recent origin, that its growth has been rapid and that it is already of great importance. And it must also be conceded that it is a business in which the whole public have a direct and positive interest. It presents, therefore, a case for the application of a long-known and well established principle in social science, and this statute simply extends the law so as to meet this new development of commercial progress." Munn v. Illinois, 94 U. S. 132, 133.

from government are all present. But these additional factors simply add strength to the basis of railroad control, and do not in any sense subject it to the uncertainty which is characteristic of the control of private industries, in which these factors are the only ground of regulation. The controlling consideration in railroad control is the public character of the business.[14] So true is this that even those who deny the potency of any argument to justify price control in private industries, do not often question the judicial doctrine of railroad regulation. Indeed, no more forceful exposition of that doctrine can be found than that given by Mr. Justice Brewer, in an opinion in which he denied the right of a legislature to fix charges for *warehouses:*

" The creation of all highways is a public duty. Railroads are highways. The State may build them. If an individual does the work he is *protanto* doing the work of the State. He devotes his property to a public use. The State doing the work fixes the price for the use. It does not lose the right to fix the price because an individual voluntarily undertakes to do the work." [15]

It is settled law, therefore, that a state may regulate railroad rates.[16] But while the courts rest this authority

[14] The statement that a public industry is subject to legislative control as to its prices, does not, of course, imply that the list of public industries is made up and is forever unchangeable. Here, as in the case of the peculiar class of private industries just mentioned, historical development necessarily works gradual changes. Thus we find the Supreme Court saying in San Diego Land and Town Co. v. National City: " That it was competent for the State of California to declare that the use of all water appropriated for sale, rental or distribution should be a public use and subject to public regulation and control, and that it could confer upon the proper municipal corporation power to fix the rates of compensation . . . is not disputed, and is not, we think, to be doubted." 174 U. S. 753.

[15] Budd v. New York, 143 U. S. 549.

[16] It has never been doubted by the courts that this power of regulation may be exercised either by the legislature, or by a commission to which the legislative power is delegated. See Tilley v. Railroad Co., 5 Fed. Rep. 641; Railroad Commission Cases 116 U. S. 307.

upon a purely legal basis—to be found in the public character of the road as a public highway, and of the company as a common carrier—it is also possible to further justify and sustain the judicial position by convincing arguments of an economic character. The monopolistic elements in the railroad industry, the nature of railroad competition, and, in general, the extensive economic, social and political significance of railroads, and hence the power of railroad managers, are considerations effective in strengthening the conviction that the courts are justified in sustaining public regulation of rates.

But what, it may be asked, is the precise significance of the term "regulate." Does it include a power to establish absolute rates, from which a railroad may be forbidden to vary, or is the power confined to merely maximum rates? This question has never been conclusively determined by the Supreme Court for the reason that it has never been directly at issue in any case. In spite of this fact, however, the answer has practically been given, for the Court, in asserting and describing the legislative power, has repeatedly used the term "maximum", or an equivalent.[17] It has, therefore, all but committed itself to that view of the case. On principle, also, that would seem to be the proper view. The Fourteenth Amendment operates to impose reasonable re-

[17] For example: "It has been customary from time immemorial for the legislature to declare what shall be reasonable compensation, or perhaps more properly speaking, to fix a maximum beyond which any charge would be unreasonable." 94 U. S. 133. "The right to establish a maximum of charge . . ." 94 U. S. 134. "The state may limit the amount of charges by railroad companies." 94 U. S. 176, and 116 U. S. 325. "The legislature of a state, having power to fix maximum rates and charges . . ." 173 U. S. 690. For other examples see 94 U. S. 125, 162, 179; 116 U. S. 330, 335; 173 U. S. 687, 694; 186 U. S. 261. No case, so far as I can discover, has ever held that rates may be absolute.

straints on the police power of the States. It does not prevent the imposition of reasonable maximum rates, nor the prohibition of rate cutting which amounts to unjust discrimination, for the high interests of the public demand that it be protected from extortionate and preferential railroad rates. But it would be hard to imagine public policy demanding a prohibition of all reduction in rates, reasonable as well as unreasonable. The repeated dicta of the Court, then, seem to find support in the merits of the question. It need hardly be added that the view of the federal Supreme Court is controlling in this matter, the question being one under the Constitution of the United States.

Thus has been established the right of the legislature to establish rates for the railroads within its jurisdiction. And as this doctrine was clearly enunciated in the first rate cases, the prime defence of the companies against public control at once broke completely down. We have now to consider the other arguments which they have brought to their aid. Two are not of much importance for our present purpose and may be briefly mentioned.

II. In some of the Granger Cases objection was raised to the laws involved, on the ground that they affected interstate commerce, and hence were void at least insofar as they applied to commerce not strictly infra-state. This objection was met by the Court with the distinct assertion that in the absence of Congressional action each state might regulate such interstate commerce as affected its own citizens. This was the law until 1886, when a divided Court overruled this feature of the Granger Cases.[18] The rule as then announced—that the

[18] Wabash, etc. Rd. Co. v. Illinois, 118 U. S. 557. It will be remembered that this case had an important influence in hastening federal legislation. The Interstate Commerce Act was passed at the next session of Congress.

states can regulate only such commerce as is purely infra-state—has since remained undoubted law.

III. In many of the earlier cases, also, the railroads sought exemption from the operation of the laws, on the ground that their charters exempted them from public control of their rates; but the answer of the Court brought them small comfort. In this matter the Court simply applied the old rule regarding grants—particularly grants of immunity—by the state. In no case, said the Court, is it to be presumed that a charter confers exemption from legislative control. The presumption is all the other way, and to overcome it requires a clear indication of legislative intent. Thus even a clause in the charter conferring upon the company the right to fix its rates does not excuse the road from the rates made by the state. It is excused only if the charter, in addition to granting that power, contains expressly or by clear implication, a renunciation by the state of its right of regulation. Under such a doctrine, of course, no railroad incorporated under general laws, and almost none incorporated by special act could claim exemption from public control.[19]

A matter of some interest is suggested by the Court's assertion that immunity from rate control *may* be given in a railroad charter. It has always been said that the fixing of the rates is an exercise of the police power. Yet it is a well settled doctrine of the police power that a state cannot dispossess itself of that power,—cannot contract it away. It would seem, therefore, that rate regulation is not in reality a phase of the police power, but that it stands on a different basis. What that basis may be, is indicated by a further distinction which may be drawn between rate control and the ordinary forms of

[19] See Ruggles v. Illinois, 108 U. S. 541, and Stone v. Farmers' Loan and Trust Co., 116 U. S. 307.

police regulation. In general the police power is employed to control matters of private concern for the general good, but rate regulation is used to control matters of public concern. Is not the public character of the railroad business alone sufficient to justify public regulation? But whatever interest may attach to speculations of this character, there is no doubt that at present the courts declare the police power to be the basis of rate control.

IV. We come now to the fourth defence of the railroad companies, and the one with which the remainder of our work will be concerned. The railroads have contended that rates ought to be reasonable, by whomsoever made; that what is reasonable is a judicial question; and that therefore the courts are competent to review legislative rates in order to determine their reasonableness. Into the varying replies which the Supreme Court has made to this contention it is now our purpose to inquire.

CHAPTER II.

THE DOCTRINE OF JUDICIAL REVIEW.—I.

The argument that rates established by public authority should be subject to the scrutiny of the courts in order that their reasonableness may be judicially determined was advanced and urged with much force in the Granger Cases—the first cases involving the validity of railroad control. It was therefore necessary for the Supreme Court to consider the question and to pronounce upon it. It did so, and in its expressions upon the point there appears no lack of definite conviction. The power of the legislature was held to be complete and exclusive, subject to no restraint from the courts. The force with which this doctrine was enunciated may be indicated by quotations from the opinions of the Court, read by Mr. Chief Justice Waite. In the Munn case are found these words:

"It is insisted, however, that the owner of property is entitled to a reasonable compensation for its use, even though it be clothed with a public interest, and what is reasonable is a judicial and not a legislative question. As has already been shown, the practice has been otherwise. . . . We know that this is a power which may be abused; but that is no argument against its existence. For protection against abuses by legislators, the people must resort to the polls, not to the courts."[1] And again: "Of the propriety of legislative interference within the scope of the legislative power, the legislature is the exclusive judge."[2]

In the Peik case, counsel for the railroad argued that "the question of what is reasonable compensation is for

[1] 94 U. S. 133, 134.
[2] 94 U. S. 132.

judicial determination and cannot be decided by the legislature." [3] The reply of the Chief Justice to this contention was perfectly clear. He said: "As to the claim that the courts must decide what is reasonable, and not the legislature. This is not new to this case. It has been fully considered in *Munn v. Illinois*. Where property has been clothed with a public interest, the legislature may fix a limit to that which shall in law be reasonable for its use. This limit binds the courts, as well as the people. If it has been improperly fixed, the legislature, not the courts, must be appealed to for the change." [4]

Again, in the Ackley case the only matter which received mention in the opinion of the court was the question whether the railroad company could "recover for the transportation of property more than the maximum fixed by the Act of 1874, by showing that the amount charged was no more than a reasonable compensation for the services rendered." The question was answered by a decided negative. "The limit of recovery," said the court, "is that prescribed by the statute." [5]

It can be no misinterpretation of language here quoted to say that it indicated a deliberate judgment and a clear conviction on the part of the Court, as to the question discussed. However much that matter may have been overshadowed by the major question in the cases, it received attention at the hands of the Court, and was settled in no doubtful terms. When the Granger Cases had been decided, therefore, the law was that the reasonableness of rates is a purely legislative question, that neither the Common Law nor the Federal Constitution permits the railroads to seek relief in a judicial review of rates made by the legislature.

[3] 94 U. S. 167.
[4] 94 U. S. 178.
[5] 94 U. S. 179.

For a period of nine years this rule was sustained without modification and guided the judiciary in its treatment of railroad cases. An illustration of its application may be seen in the case of *Tilley v. Savannah, etc. R. Co.*,[6] decided in 1881. This case involved the power of the Georgia Railroad Commission to act under a statute authorizing it to fix railroad rates. Mr. Justice Woods, of the Supreme Court, who was then sitting on circuit, held that there was only one conclusive test of the reasonableness of rates—for the railroad to try them—and that its only remedy, should the commission's rates prove unreasonable, was to apply to that board or to the legislature. "My conclusion is," he continued, "that the Act of the Legislature of Georgia is not in violation of either the Constitution of the United States or of the state of Georgia . . . that it (the Legislature) may prescribe rates, either directly, or through the intervention of a commission, and that the question whether the rates prescribed by the legislature, either directly or indirectly, are just and reasonable, is a question which the Legislature may determine for itself." [7]

After nine years of unqualified acceptance, however, a modification of this rule was introduced in the opinion of the Court, read by Mr. Chief Justice Waite, in the Railroad Commission Cases,[8] which were suits in equity brought to restrain the Mississippi Railroad Commission from establishing rates, on the ground that the charters of the companies exempted them from public control of their charges. In determining that the charters afforded no such exemption the court reaffirmed the right of the

[6] 5 Fed. 641.

[7] 5 Fed. 664. See *Ruggles v. Illinois*, 108 U. S. 526, and concurring opinion of Mr. Justice Field on p. 541; also *Spring Valley Water Works v. Schottler*, 110 U. S. 347.

[8] Stone v. Farmers' Loan and Trust Co. and two other cases, (1886) 116 U. S. 307, 347, 352.

legislature to regulate railroads, but in the midst of the opinion are found these significant words:

"From what has thus been said it is not to be inferred that this form of limitation or regulation is itself without limit. This power to regulate is not a power to destroy, and limitation is not the equivalent of confiscation. Under pretence of regulating fares and freight, the State cannot require a railroad corporation to carry persons or property without reward; neither can it do that which in law amounts to a taking of private property for public use without just compensation or without due process of law."

Continuing, the Chief Justice said: "What would have this effect we need not now say, because no tariff has yet been fixed by the Commission, and the statute of Mississippi expressly provides 'that in all trials of cases brought for a violation of any tariff of charges so fixed by the commission it may be shown in defence that such tariff so fixed is unjust.'" [9]

Thus the suggested modification remained, in this case, merely an obiter dictum, but its importance lay in the fact that it was the first hint in any prevailing opinion of the court that the legislative power of control was subject to limitations other than those which might be imposed through popular suffrage. The dictum did not go so far as to describe the nature and extent of those limitations, nor to state through what agencies they could be enforced. It was simply a declaration in general terms that the railroads possessed rights of property which were secure even from the legislative power of regulation.

Three years later Mr. Justice Gray, in his opinion in a rate case, remarked that "the general rule of law that governs this case has been clearly stated and developed in opinions of this Court delivered by the late Chief Justice."[10] The fact is, however, that at that time the

[9] 116 U. S. 331.

[10] Dow v. Beidelman, 125 U. S. 680, 686.

Court was anything but clear upon the subject. For a period of five years after the Railroad Commission Cases the law was in a very unsettled condition, and for this the dictum of Mr. Chief Justice Waite was wholly responsible. It is idle to speculate as to what effect he would have given to his words had he been spared to share in the trial of later cases. His death left their full meaning undetermined, and until 1890 no authoritative decision was reached. During that time his colleagues on the Supreme bench and other jurists as well speculated upon his dictum, in attempts to discover its proper implications and applications, but without complete definiteness or harmony of conclusion.

Thus, in the opinion of the Court in *Dow v. Beidelman,* a case in which the railroad claimed that the passenger rates fixed by an Arkansas statute would reduce its net yearly income to less than 1½% on the "original cost of the road," and to only a little more than 2% on its bonded debt, Mr. Justice Gray cited several cases, quoting Chief Justice Waite's dictum, but after showing that the railroad had offered no evidence as to the cost of its bonds or the sum paid for its road, continued as follows:—

"Without any proof of the sum invested by the reorganized corporation or its trustees, the court has no means, *if it would under any circumstances have the power,* of determining that the rate fixed by the legislature is unreasonable. Still less does it appear that there has been any such confiscation as amounts to a taking of property without due process of law." [11]

In this case, then, it is evident that the Court was not free from doubt as to its power to test the reasonableness of rates. A more positive statement appeared in the opinion of the Court, read by Mr. Justice Field, only a few months later in the *Georgia Railroad and Banking Co. v. Smith.* After quoting from the Railroad Com-

[11] 125 U. S. 680, 690. The italics are mine.

mission Cases and *Dow v. Beidelman,* the learned Justice remarked:

"It has been adjudged by this court that the legislature of a state has the power to prescribe the charges of a railroad company for the carriage of persons and merchandise within its limits, in the absence of any provision in the charter of the company constituting a contract vesting in it authority over those matters, subject to the limitation that the carriage is not without reward, or upon conditions amounting to the taking of property for public use without just compensation; and that what is done does not amount to a regulation of foreign or interstate commerce." [12]

But as the only contention in this case was exemption by reason of charter provisions, no application was made of the dictum as to carriage "without reward or upon conditions amounting to the taking of private property for public use without just compensation."

The precise question, however, was directly involved in a suit which came before Mr. Justice Brewer, then a circuit judge, in 1888, after the Arkansas case, but before the Georgia case had been passed upon by the Supreme Court. Taking up the dictum of Chief Justice Waite and Justice Gray's holding in *Dow v. Beidelman,* the now eminent jurist interpreted them as establishing in a most thorough way the power of the courts to interfere in matters of railroad rates. The action [13] was for an injunction to restrain the Railroad Commission of Iowa from enforcing rates made under the authority of an Act of 1887. In his opinion Judge Brewer quoted from the opinions in the Railroad Commission and Dow cases, and then proceeded:

"It is obvious from these last quotations that the mere fact that the legislature has pursued the forms of law in

[12] 128 U. S. 174, 179.

[13] *Chicago and Northwestern R. Co. v. Dey,* 35 Fed. Rep. 866.

prescribing a schedule of rates does not prevent inquiry by the courts, and the question is open and must be decided in each case, whether the rates prescribed are within the limits of the legislative power, or mere proceedings which, in the end, if not restrained, will work a confiscation of the property of complainant. Of course some rule must exist, fixed and definite, to control the action of the courts, for it cannot be that a chancellor is at liberty to substitute his discretion as to the reasonableness of rates for that of the legislature. . . . The right of judicial interference exists only when the schedule of rates established will fail to secure to the owners of the property some compensation or income from their investment. As to the amount of such compensation, if some compensation or reward is in fact secured, the legislature is the sole judge. The question is one alone of policy. . . . The rule, therefore, to be laid down, is this: That where the proposed rates will give some compensation, however small, to the owners of railroad property, the courts have no power to interfere. Appeal must then be made to the legislature and the people." [14]

Here is a clear enunciation of the doctrine of judicial review from a lower court, and, what is more important, its practical application through the granting of an injunction against a railroad commission. In another case, also,[15] which he decided the same day, Judge Brewer issued an injunction restraining the Minnesota Commission from enforcing a certain switching charge, which the railroad claimed would prove unremunerative. These two cases could leave no doubt that in Judge Brewer's mind unremunerative rates were unreasonable, and unreasonable rates it was competent for the judiciary to suspend.

Some months later [16] the Supreme Court of Florida

[14] 35 Fed. Rep. 878, 879.

[15] Chicago, St. Paul, Minneapolis and Omaha R. Co. v. Becker, 35 Fed. Rep. 883.

[16] Pensacola, etc. R. Co. v. Florida, 25 Fla. 310.

had under consideration rates made by the state commission, which the railroad claimed and the commission admitted would not allow the road to pay its operating expenses. Reviewing the Railroad Commission, Dow, Georgia and Dey cases, with thorough approval of Judge Brewer's opinion in the last named case, the court declared that the enforcement of unremunerative rates is a wrong, for which there is no remedy but in the courts. Accordingly it adjudged the contested rates to be an attempt to take property without just compensation and without due process of law.

From this brief review of the suits which followed the Railroad Commission Cases, it is evident that in a very few years the Supreme Court had placed a broad interpretation upon Chief Justice Waite's dictum, while some of the lower courts had gone so far as to announce a definite theory of judicial control. The question had not been authoritatively determined by the Supreme Court because it had not been squarely presented, but such had been the tendency of judicial opinion since 1885, that one could have foretold the nature of Court's decision when a clear case arose. It was but a matter of time before the period of uncertainty would be ended by a definite recantation by the Court of the conviction so clearly expressed in the Granger Cases.

It was in 1890 that the test came. The case, the *Chicago, Milwaukee and St. Paul R. Co. v. Minnesota,*[17] originated in 1887, in a complaint made to the Minnesota Commission alleging the unreasonable character of certain milk rates charged by the railroad. The complaint was forwarded to the railroad and a date fixed for an examination. Upon that date both the railroad and the complainants appeared by attorney, and the Commission

[17] 134 U. S. 418.

"proceeded to investigate the complaint." Some weeks later the Commission served its decision upon the railroad with an order fixing new and lower rates. Upon the refusal of the railroad to put them in force, the Commission applied to the Supreme Court of the State [18] for a writ of mandamus to compel the adoption of the rates. On the hearing the railroad asked for a reference to take testimony regarding the reasonableness of the Commission's rates, but this application was denied upon the ground that the statute declared the Commission's rates to be conclusively reasonable, and, as decided in the Granger Cases, this legislative determination was binding upon the courts. The court, therefore, granted a peremptory writ of mandamus. The railroad company, however, sued out a writ of error to the Supreme Court of the United States, asserting its right to contest the reasonableness of the Commission's rates, under the Fourteenth Amendment to the Federal Constitution. The case was decided March 24, 1890, the opinion of the majority of the Court being read by Mr. Justice Blatchford.

In his opinion the learned jurist reviewed the facts of the case, and the decision of the Supreme Court of Minnesota, then discussed the question as to whether the railroad's charter exempted it from legislative control, and having decided that question in the negative, announced the important point to be whether the form of regulation adopted in this case was valid.

Launching into the discussion of this subject, he asserted the necessity of adopting the construction placed upon the Minnesota statute by the state court—that the Legislature intended the Commission's rates to be conclusively reasonable. Upon such a construction he declared the statute to be clearly invalid:

[18] 38 Minn. 281.

" It conflicts with the Constitution of the United States in the particulars complained of by the railroad company. It deprives the company of its right to a judicial investigation, by due process of law, under the forms and with the machinery provided by the wisdom of successive ages for the investigation judicially of the truth of a matter in controversy, and substitutes therefor, as an absolute finality, the action of a railroad commission which, in view of the powers conceded to it by the state court, cannot be regarded as clothed with judicial functions, or possessing the machinery of a court of justice."

Under the statute, said the Court, the Commission had but to " find " a railroad's rates unreasonable, adopt others, and notify the company of the fact.

" No hearing is provided for; no summons or notice to the company before the commission has found what it is to find, and declared what it is to declare; no opportunity is provided for the company to introduce witnesses before the commission,—in fact, nothing which has the semblance of due process of law; and, although in the present case, it appears that, prior to the decision of the Commission, the company appeared before it by its agent, and the commission investigated the rates charged by the company for transporting milk, yet it does not appear what the character of the investigation was, or how the result was arrived at." [19]

Continuing, Mr. Justice Blatchford called attention to another provision of the statute, requiring all railroad rates to be equal and reasonable. Nevertheless, although here the railroad alleged that the Commission's rates were not equal and reasonable, the statute did not permit them to show that fact in judicial proceedings. This restraint was clearly wrong: " The question of the reasonableness of a rate of charge for transportation by a railroad company, involving, as it does, the element of reasonableness both as regards the company and as regards the public, is eminently a question for judicial investiga-

[19] 134 U. S. 456, 457.

tion, requiring due process of law for its determination. If the company is deprived of the power of charging rates for the use of its property, and such deprivation takes place in the absence of an investigation by judicial machinery, it is deprived of the lawful use of its property, and thus, in substance and effect, of the property itself, without due process of law, and in violation of the Constitution of the United States, and in so far as it is thus deprived, while other persons are permitted to receive reasonable profits upon their invested capital, the company is deprived of the equal protection of the laws."[20]

From this argument the conclusion emerged that the issuing of a peremptory writ of mandamus by the state court was unlawful, because in violation of the Constitution of the United States. In its judgment, therefore, the Court remanded the case for further proceedings not inconsistent with its opinion, remarking, however, that unless the state court changed its construction of the statute so as to permit of judicial review of the rates, the only possible proceeding was to dismiss the application for the mandamus.[21]

The opinion of Mr. Justice Blatchford in this case has been described at length and many passages have been

[20] 134 U. S. 458. With this compare the following from the dissenting opinion of Mr. Justice Bradley: "No one questions the constitutionality or propriety of boards for assessing property for taxation, or for improvement of streets, sewers, and the like, or of commissions to establish county seats, and for doing many other things appertaining to the administrative management of public affairs. Due process of law does not always require a court. It merely requires such tribunals and proceedings as are proper to the subject in hand." 134 U. S. 464.

[21] On the same day the Supreme Court, through Mr. Justice Blatchford, handed down its opinion in the case of the Minneapolis Eastern R. Co. v. Minnesota, 134 U. S. 467. The Minnesota Commission had fixed a switching charge which the railroad refused to adopt. The Commission secured an alternative writ of mandamus, and in its reply the railroad asserted that the rate was unreasonable and would

freely quoted for several reasons. In the first place, because of the great importance of the case. It marks the turning point in American railroad law; it indicates the definite adoption by the Supreme Court of a policy fraught with tremendous consequences both to the railroads and to the people. In the second place, because the reasoning of the Court does not repose on its former decisions or opinions. In all that part of his opinion which deals with the question under discussion, Mr. Justice Blatchford cites no case or other authority except the obiter dictum in the Railroad Commission Cases. His doctrine was new law, freshly made out of whole cloth.

But still another reason for the extended discussion of his opinion is that it is not entirely easy to understand its reasoning. It must be confessed that the discussion is somewhat confused, and it is therefore difficult to satisfactorily digest its substance. The following, however, is believed to be a practically faithful statement of the doctrine of judicial review as it presented itself in this case:

Although railroad companies are quasi-public in character they are entitled to the protection of the Fourteenth Amendment. Therefore,

1. They cannot be deprived of property without due process of law. But since rates imposed by the state may deprive them of the lawful use of their property, and hence, in substance and effect, of the property itself, such rates must be enforced only after an investigation by judicial machinery, that is, after due process of law has been observed.[22]

deprive it of property without due process of law. Its request to make proof of these matters was, however, refused and a peremptory writ of mandamus issued. Upon its reasoning in the other case, and especially because no notice to the railroad or hearing had been granted before the charge had been fixed, the Federal Supreme Court reversed the judgment of the State Court.

[22] The statute in this case, however, did not provide nor require due process of law, nor did it appear that the commission employed it in fixing the rate.

2. They cannot be denied the equal protection of the laws. But if they are deprived of the lawful use of their property with due process of law, while other persons are not, they are denied the equal protection of the laws.[23]

This, then, is the doctrine of judicial review as it appeared when first authoritatively announced in 1890. It will at once be seen, however, that in this form, it was in but a crude and rudimentary state, and much litigation was needed to develop and refine it. As pronounced by Mr. Justice Blatchford, many questions of importance were left unsettled, and it is to the later decisions of the court that we must look for answers to these questions. The next two chapters will therefore be devoted to a study of the evolution of the doctrine up to the present time.

It remains now merely to remark that although the doctrine of this case was far from complete, the result of the case was clear and definite. The Court had executed a right-about-face. Mr. Chief Justice Waite's repeated assertion in the Granger Cases, that the judgment of the legislature binds the courts as well as the people was distinctly renounced. So far as those cases dealt with the relation of the courts to the legislature they were definitely overruled. The doctrine of judicial review was born.

Only three of the justices who decided the Granger Cases were on the bench when this Minnesota case was considered. Of these, Mr. Justice Field had dissented in the former cases and naturally agreed with the majority in their holding. But Mr. Justice Bradley delivered a vigorous dissent, asserting that the majority had practically overruled *Munn v. Illinois;* claiming that reasonableness is a legislative and not a judicial question; and deploring "an assumption of authority on the part of

[23] Such might have been the effect of the statute in this case.

the judiciary, which, it seems to me, with all due deference to the judgment of my brethren, it has no right to make."[24] In this dissenting opinion Mr. Justice Gray and Mr. Justice Lamar concurred.

The third surviving member of the Granger Court was Mr. Justice Miller, who concurred " with some hesitation " in the judgment of the Court. His brief opinion consisted of a series of propositions, which, in his judgment, embodied the rules of law applicable to such cases. It may be said that his views were largely adopted in subsequent decisions of the Court.

[24] 134 U. S. 462.

CHAPTER III.

The Doctrine of Judicial Review.—II.

We are now to consider the evolution of the doctrine of judicial review, from its crude condition in the Minnesota Case to the well-developed and somewhat complex form which it presents to-day. In pursuing this study, constant reference must be made to the important cases decided since 1890, and it therefore seems advisable to delay our analysis of the subject long enough to take a hasty view of those cases.

The first case upon our subject to come before the federal Supreme Court, after the Minnesota case, was the *Chicago and Grand Trunk R. Co. v. Wellman,*[1] which involved a Michigan statute fixing maximum charges. Finding that the evidence was insufficient to prove the rates unreasonable, the Court sustained the statute. On the same day on which this was decided, Mr. Justice Blatchford read the opinion of the majority of the Court in the curious case of Budd v. New York.[2] This was an action brought to test the constitutionality of a New York statute fixing rates of charge for warehouses, and as this was precisely the question involved in Munn v. Illinois, the case is of special interest. The opinion was definite in its conclusion—the statute was sustained—but for uncertainty of argument it would be hard to find its equal in all the books of law. At one point it states that "we must regard the principle maintained in *Munn v.*

[1] 1892. 143 U. S. 339. To be referred to hereafter as the Wellman case.

[2] 134 U. S. 517. To be referred to hereafter as the Budd case.

Illinois as firmly established, and we think it covers the present case." At another point it attempts to distinguish the Minnesota case, by asserting that the opinion there had reference only to charges fixed by a commission and was not concerned with rates fixed by a legislature. Then, as if fearing that this might imply a total lack of judicial control over legislative rates, it resorts to the hopeless uncertainty of *Dow v. Beidelmann,* and quotes the dubious clause, " if it (the Court) would under any circumstances have the power " of determining a legislative rate to be unreasonable. Under cover of this makeshift doctrine, the opinion goes on to show that the complaint in this case alleged no unreasonableness in the rates, and then repeats the words: " even if under any circumstances we could determine that the maximum rate fixed by the legislature was unreasonable."

It is, of course, hard to construe such an opinion as this, but a fair inference would seem to be that at this time there was some doubt in the mind of Mr. Justice Blatchford, if not in the minds of other members of the Court, as to whether the doctrine of judicial review should be extended to rates made directly by a legislature. That there was no such doubt, however, as to most of the justices, is evident from the fact that Mr. Justice Brewer's opinion in the Wellman case, read on the same day, and to which no dissent was offered, clearly asserted the right of the courts to review legislative rates. " The legislature," he said, " has power to fix rates and the limit of judicial interference is protection against unreasonable rates."[3]

Two years later the same jurist laid to rest as gracefully as was possible, any doubt that may have been raised by the Budd Case by saying that because the records in that case had not shown the rates to be un-

[3] 143 U. S. 344.

reasonable, " there was no occasion for saying anything as to the power or duty of the Court in case the rates as established had been found to be unreasonable."[4]

In the Reagan cases the doctrine of judicial review was reaffirmed and much elaborated. These important cases,[5] decided in 1894, all involved rates made by the Texas Railroad Commission. Injunctions to restrain the Commission from enforcing the railroads from operating the rates, had been sought in the Circuit Court and had been granted. Indeed so sweeping was the decree of that court that the Commission was forbidden to establish any rates whatever. This last feature of the decree was reversed by the Supreme Court, but so far as the decree restrained the enforcement of the rates already established, it was affirmed, the court finding, after investigation, that the rates were unreasonable.

On March 4, 1895, three suits were decided by the Supreme Court, speaking through Mr. Justice Shiras. The leading case was *St. Louis and San Francisco Ry. Co. v. Gill*[6] and the others[7] were settled upon the principles therein declared. It is interesting to note that these cases involved the same statute as *Dow v. Beidelman*—the Arkansas Maximum Passenger Rate Act of 1887. There was no longer, however, the uncertainty which characterized the utterances of the Court in that case. The right of the courts to test the reasonableness of legislative rates was clearly declared, although, because the evidence had not shown their unreasonableness, the rates were sustained.

[4] Reagan v. Farmers' Loan and Trust Co. 154 U. S. 398.

[5] Reagan v. Farmers' Loan and Trust Co., and four other cases, 154 U .S. 362, 413, 418, 420.

[6] 156 U. S. 649. To be referred to hereafter as the Gill case.

[7] St. L. & San F. Ry. Co. v. Stevenson, and same v. Trimble, 156 U. S. 667.

In 1896, in the case of the *Covington and Lexington Turnpike Co. v. Sandford,*[8] the Supreme Court elaborated the doctrine still further and employed it to restrain the enforcement of rates made by the Legislature of Kentucky for the turnpike company. And on March 7, 1898, was delivered the opinion of the Court in the great case of *Smyth v. Ames,*[9] which had been brought to contest the validity of the Nebraska Maximum Rate Law of 1893. The Supreme Court affirmed the decree of Mr. Justice Brewer in the Circuit Court, restraining the enforcement of the rates. The opinion of the Court, prepared by Mr. Justice Harlan, worked out our doctrine in great detail.

A variation on the usual form of question presented to the Court appeared in the *Lake Shore, etc. R. Co. v. Smith,*[10] in which was involved a Michigan statute requiring railroads to sell mileage books and fixing the price therefor. Although there was strong dissent, and although the reasoning of Mr. Justice Peckham's prevailing opinion is not at all clear, there can be no doubt that in the opinion of the majority the statute was "a violation of that part of the Constitution of the United States which forbids the taking of property without due process of law." It was therefore declared to be invalid.

Another variation of the question presented itself in *San Diego Land and Town Co. v. National City,*[11] which involved the power of certain local officers to fix water rates under the California Act of March 7, 1881. In

[8] 164 U. S. 578.

[9] 169 U. S. 466; see also 171 U. S. 361. To be referred to hereafter as the Smyth case.

[10] 1899. 173 U. S. 684. To be referred to hereafter as the Lake Shore case.

[11] 1899. 174 U. S. 739. To be referred to hereafter as the San Diego case.

1884, in the *Spring Valley Water Works v. Schottler,*[12] the Supreme Court, in pursuance of the principles of the Granger Case, had held that such regulations of water rates was a proper exercise of legislative power, and was not subject to judicial review. But in the San Diego case this view was abandoned. Citing the Wellman, Reagan, and Smyth cases, the Court asserted its right to test the reasonableness of the rates under the Federal Constitution. The rates were, however, upheld as valid.

The Chicago, Milwaukee and St. Paul R. Co. v. Tompkins [13] arose from a suit by the railroad to restrain the enforcement of a schedule made by the South Dakota Commission. The decree of the trial court was in favor of dismissing the bill and vacating the injunction, but, on appeal of the railroad, all proceedings were stayed in the lower court. The Supreme Court held that the decision of the trial court was based on an inadequate finding of fact, the cost of local business not having been determined, and it therefore reversed the decree and remanded the case to the lower tribunal with instructions to appoint a master to fully find the facts and then to proceed as equity might require. In pursuance of this decree the Circuit Court found the rates to be unreasonable and perpetually enjoined their enforcement.[14]

In McChord v. Louisville and Nashville R. Co.,[15] the railroad applied for an injunction to restrain the Kentucky Commission from fixing any rates whatever, on the ground of threatened multiplicity of suits and irreparable injury. The court, however, maintained the right of a commission to establish rates, stating that an

[12] 110 U. S. 347. Supra, p. 27, footnote.

[13] 1900. 176 U. S. 167. To be referred to hereafter as the Tompkins case.

[14] Chicago, Milwaukee and St. Paul R. Co. v. Smith, 110 Fed. Rep. 473.

[15] 183 U. S. 483.

injunction could be granted only when, after their establishment, they could be shown to be unreasonable.

A novel question was presented by the *Louisville and Nashville Railroad v. Kentucky,* decided in 1903.[16] The question involved was the power of the courts to review action taken by the Railroad Commission in pursuance of a statute authorizing it to exempt railroads from time to time from the operation of the "Long and Short Haul Clause." The railroad relied on the cases just reviewed, but the Supreme Court held that they applied only to rate-making, that in such a case as this no such matter was involved, and that the action of a commission was therefore final. It is difficult to perceive why a discretionary power to compel obedience to a Short Haul Clause is not one feature of the power of rate-making. Certainly through it the earnings of a company can be profoundly influenced. In this particular, however, the Supreme Court refused to extend the doctrine of judicial review.

The last Supreme Court case upon this subject is the *Minneapolis and St. Louis R. Co. v. Minnesota,* also decided in 1902,[17] in which was sustained a coal rate imposed by the State Commission.

Many other applications of the doctrine of judicial review may be found in the lower courts. A few only can be mentioned here. In the *Cleveland Gaslight and Coke Co. v. Cleveland,*[18] Mr. Justice Jackson, then a circuit judge, cited the Minnesota case as authority for granting an injunction to restrain the enforcement of a city ordinance fixing the price of gas. In 1894 Mr. Justice Brewer and Judge Dundy decided the case of *Ames v. Union P. R. Co.*[19] adversely to the Nebraska Maxi-

[16] 183 U. S. 503.

[17] 186 U. S. 257. To be referred to hereafter as the Minneapolis and St. Louis case.

[18] 1891. 71 Fed. Rep. 110.

[19] 64 Fed. Rep. 165.

mum Rate Law, its decree being affirmed by the Supreme Court in *Smyth v. Ames*. About a year later District Judge Clark enjoined the enforcement of gas rates fixed by the city of Memphis, citing as authority the Minnesota and Reagan cases.[20]

In the same year [21] Judge Wellborn, of the United States District Court asserted the right of the courts to review rates fixed by the Secretary of War, under provisions of an Act of Congress, for a railroad which had been incorporated and aided by the United States, although he declared the rates in controversy valid, inasmuch as no showing was made to the contrary.[22] And a few months later Mr. Justice McKenna, then Circuit Judge, restrained the enforcement of rates made by the California Commission.[23]

In these, and other cases, has the doctrine of judicial review been elaborated and authoritatively pronounced. With this cursory glance at the leading cases on the subject, we may now proceed to inquire their effect upon that doctrine.

No one can read the opinion of Mr. Justice Blatchford in the Minnesota case without being impressed by the emphasis there laid on the phrase "due process of law." Evidently he was profoundly impressed by the absence of provisions in the statute requiring formal procedure by the commission in the investigation and decision of rate cases. And no less was he impressed by the absence of evidence, upon the record, tending to show that the commission had actually employed those forms which have been "provided by the wisdom of successive ages

[20] New Memphis Gas and Light Co. v. Memphis, 72 Fed. Rep. 952.
[21] 1896.
[22] Atlantic and Pacific Rd. Co. v. U. S. 76 Fed. Rep. 186.
[23] Southern Pacific R. Co. v. Railroad Commissioners, 78 Fed. Rep. 236.

for the investigation judicially of the truth of a matter in controversy." "No hearing is provided for"; he complains of the statute, "no summons or notice to the company; . . . no opportunity provided for the company to introduce witnesses before the commission,—in fact, nothing which has the semblance of due process of law; and, although," he continues, "in the present case it appears that, prior to the decision of the commission, the company appeared before it by its agent, and the commission investigated the rates charged by the company for transporting milk, yet it does not appear what the character of the investigation was, or how the result was arrived at."[24]

On this point the suit of the Minneapolis Eastern Railway Co., decided on the same day, presented even a clearer case. Says Mr. Justice Blatchford, in his opinion in that case: "the commission states that it made its findings after due and careful inquiry and consideration; but it does not appear that the Minneapolis Eastern Railway Company had any prior notice of any hearing at which such finding was made, or any opportunity of being heard in regard thereto, while it does appear that it asked leave of the court to make proof of the matters set up in its return; and that its request was denied."[25]

The emphasis which is thus strongly laid in both cases upon the absence of formal procedure in the work of the commission might well justify the inference that it was because of this lack that the statute was found to be repugnant to the Constitution. It provided for no notice, or hearing, or opportunity to present evidence, in short, for none of the features of the procedure of courts:—the commission had but to "find" whatever it might

[24] 134 U. S. 456, 457.
[25] 134 U. S. 482.

choose to find. For that reason due process of law was denied to the railroads, in proceedings which might result in depriving them of property, and insofar as railroads were subjected to such treatment while other persons were not, they were denied the equal protection of the law. Such an interpretation of the cases seems not unfair, and might well prompt the conclusion that if statutes should require, and a commission employ, all of the forms of law, the rates made by the commission would be secure against judicial interference; that the most which the courts could do, should the rulings of the commission be appealed to them, would be to determine whether the necessary formalities had been observed. The rates might be absurdly low, but if the forms of law had been followed in their establishment, they could not be disturbed by the courts. We have, then, to consider whether this view is a fair inference from all the adjudications of the Court.

It must be said, in the first place, that although the question of procedure was the dominant consideration in these opinions of Mr. Justice Blatchford, there was one other idea, advanced in the Minnesota case, not wholly consistent with the inference suggested above. It will be remembered [26] that the learned justice contended that "the question of the reasonableness of a rate of charge for transportation by a railroad company . . . is eminently a question for *judicial* investigation." From this might possibly be drawn the conclusion that the reasonableness of rates is by nature a question for the *courts* to determine, and in which they cannot be bound by the decision of an administrative or, at most, *quasi*-judicial body. This is evidently the view which Mr. Justice Bradley attributes to the majority of his brethren. In

[26] Supra, p. 34.

his dissenting opinion he says: "It is urged that what is a reasonable charge is a judicial question. On the contrary it is preëminently a legislative one, involving considerations of policy as well as of remuneration. . . . This is just where I differ from the majority of the court. They say in effect, if not in terms, that the final tribunal of arbitrament is the judiciary; I say it is the legislature."[27]

Under such an interpretation of Mr. Justice Blatchford's language this phase of the doctrine of judicial review as announced in the Minnesota case, would present itself somewhat as follows:—

Rates made by the legislature or by a commission may be carried to the courts for two purposes, (1) to determine whether that due process of law commanded by the Fourteenth Amendment, has been observed in their formulation; (2) to secure a determination by the courts of their reasonableness, it being within the province of the courts, irrespective of the Constitution, to decide such questions.

In this form, the doctrine of judicial review would effectively preclude the idea that simply because a commission follows the forms of judicial procedure, its rates are exempt from judicial scrutiny and control. But it must be admitted that the doctrine as authoritatively enunciated by the Supreme Court has not taken this form. The theory of the inherently judicial character of the question of reasonableness has never been adopted by that court. Aside from the sentence already quoted from Mr. Justice Blatchford's opinion, in only one instance has any member of the supreme bench asserted that theory. In the Reagan cases Mr. Justice Brewer spoke as follows:—

[27] 134 U. S. 462.

"It has always been recognized that, if a carrier attempted to charge an unreasonable sum, the courts had jurisdiction to inquire into that matter. . . . The province of the courts is not changed, nor the limit of judicial inquiry altered, because the legislature, instead of the carrier, prescribes the rates."

Giving full weight to these dicta of Justices Blatchford and Brewer, it may nevertheless be safely said that their view as to the inherent competence of the courts in rate cases, irrespective of constitutional provisions, has not been adopted by the Court. It is at least certain that the Court has not felt that it could safely repose its authority upon the basis of the theory, and has sought for a firmer foundation. And indeed it must be admitted that the theory cannot command acceptance. It can hardly be maintained in the face of the historical fact that until very recent years it was never supposed that the judiciary could control the legislature in its regulation of quasi-public property. "As has been shown," said Mr. Chief Justice Waite in Munn v. Illinois,[28] "the practice has been otherwise." Rate-making is historically a legislative function, and there is much reason to agree with Mr. Justice Bradley that what is a reasonable charge is pre-ëminently a legislative question, "involving considerations of policy as well as of remuneration."[29] Moreover, it is far from conclusive to say that because the courts could restrain unreasonable rates made by a carrier to whom the legislature had permitted the privilege of making their own rates, they can also restrain rates when made by the legislature itself in pursuance of its undoubted power and in fulfillment of its duty to the people. The courts may control private citizens, especially in their enjoyment of a public privilege, where they may not control a co-ordinate branch of the government.

[28] 94 U. S. 133.
[29] 134 U. S. 462.

But whatever the considerations may be to which the Supreme Court has given weight, it is certain that it has never insisted upon the theory in question, and has not been content to rely upon it in working out the doctrine of judicial review. So solitary are the two utterances of Justices Blatchford and Brewer, and so entirely different is the basis upon which the Court has finally reposed, that it may be safely said that the theory of the judicial character of the question of reasonableness forms no part of the doctrine of judicial review.

This being true, the question recurs: Is a court limited in a rate case to an investigation of the procedure employed by the commission, and must it sustain rates, however low, if it finds that they have been established as a result of those formal proceedings which are contemplated by the phrase "due process of law?" Evidently this is not so. For the slightest study of rate cases reveals the fact that in almost every instance the investigation of the court has been directed not at the procedure of the commission, but at the reasonableness of the rates. The question then arises as to the theory upon which the courts base this broader authority. If, as we have just seen, they are not prepared to insist that reasonableness of rates is in its nature a judicial question, why may they nevertheless determine that question?

The answer to this query is to be found in a broader interpretation of the phrase "due process of law." To Justice Blatchford those words apparently suggested no more than the forms of judicial procedure. In other cases, however, they have been recognized as including the further idea of "just compensation." No state shall deprive a person of property without due process of law, but should a state, in taking private property, employ all the judicial procedure and machinery known to man, yet fail to return just compensation for that property, it

would not have used "due process of law." Just compensation, then, is an essential element in due process of law, and under the Fourteenth Amendment, therefore, the question is open for determination by the courts as to whether rates are such as to deprive of property, and whether, if so, just compensation is made for the property so taken. Moreover, if a railroad is in fact deprived of its property without just compensation, it is not only denied due process, but, since other persons receive just compensation for property appropriated by the state, it is also denied the equal protection of the laws.[30] Thus these two clauses of the Fourteenth Amendment are both violated.

Something akin to this idea has probably lain behind all of the decisions of the court within the last fifteen years, but it has not always been clearly stated. In the Minnesota case, for example, while Mr. Justice Blatchford gave no expression to such an idea, Mr. Justice Bradley clearly saw that the decision of the majority necessarily involved in it, and in his dissenting opinion he objected to it in decided language.[31] In other cases, however, the idea has been definitely approved. In 1897, for instance, an unequivocal enunciation of it was made in the *Chicago, Burlington, and Quincy R. Co. v. Chicago,* where we read these words:

"A judgment of a state court even if it be authorized by statute, whereby private property is taken for the state, or under its direction for public use, without compensation made or secured to the owner, is, upon principle and authority, wanting in the due process of law required by the Fourteenth Amendment of the Constitution of the United States, and the affirmance of such judgment by the highest court of the state is a denial by that state of a

[30] See remarks of Mr. Justice Brewer in the Reagan cases, 154 U. S. 399.

[31] See 134 U. S. 465.

right secured to the owner by that instrument." [32]

This, then, is the fundamental idea in the doctrine of judicial review. The Fourteenth Amendment prohibits the states from appropriating private property without just compensation. The constitutional questions presented by a rate case are, therefore, these:

1. Do the rates deprive the railroad company of property?

2. If so, has just compensation been made or adequately provided for?

Let us comment first on this second question, as it can be disposed of in a few words, thus leaving us free to examine the first, which will require a somewhat extended treatment.

There can be no doubt that a state's power to appropriate private property for public purposes is unlimited so long as just compensation is made to the owners. It is clearly within the power of the state, therefore, to reduce a railroad's rates to any extent whatsoever, provided only that it recompenses the company for whatever property may be taken by means of the imposition of rates. This course, however, has never been taken by any of our states. In other words, no state has yet made provision for payment from the state treasury of amounts required to compensate the railroads for losses due to legislative or commission-made rates. Accordingly this second question has never yet come before the courts. Should, however, a state adopt a plan of compensation and essay to make payment to the companies, there is no doubt that the question would still be open for the courts to decide as to whether the compensation was ample, or "just."[33]

[32] 166 U. S. 226, 241; and see Backus v. Union Depot Co., 169 U. S. 557, 565.

[33] The real meaning of the doctrine of judicial review has some-

But since no legislation has ever been enacted for compensatory payments the only question which has as yet been presented to the courts is the first of those just mentioned: Do the rates deprive the railroad company of property? To answer this question in any particular case requires an understanding of the broader question as to what amounts to a deprivation of railroad property through a reduction of rates. To the consideration of this question we must now devote ourselves.

To begin with, it may perhaps hardly be necessary to state that property, as the term is used in the Fourteenth Amendment to the Constitution, signifies more than mere tangible objects. Among other things it also embraces the fruits or income of property. To deprive a person of the fruits of his property is to deprive him of property within the meaning of the constitutional prohibition. This being true, the thought which most naturally arises is this: that any change in a railroad's rates which results in a reduction of its earnings must amount to a

times been obscured by a wrong use of the word "compensation." The word has been used occasionally in the sense of a railroad's earnings from operation. For example: "The state cannot withhold from the owners of private property just compensation for its use. That would be a deprivation of property without due process of law." San Diego Land and Township Co. v. National City, 174 U. S. 739. Again: "The corporation may not be required to use its property for the benefit of the public without receiving just compensation for the services rendered by it." Smyth v. Ames, 169 U. S. 546. These statements, of course, are not accurate. They are true only under the assumption that the state has made no provision for indemnifying the railroad for the property taken. While such an assumption is natural in view of the fact that no state has yet made provision for indemnification, this double use of an important word is nevertheless unfortunate, as it tends to confuse an already intricate subject. A railroad is not entitled to just compensation *from shippers for services rendered;* and it is entitled only to just compensation *from the state for property taken* through the medium of undue reductions in rates.

deprivation of property, for it has deprived the company of a part of the fruits or income of its property. This is certainly true in fact, but in contemplation of law it is not. Not even the most ardent exponent of the doctrine of judicial review has gone so far as to assert that all reduction in a railroad's earnings, without compensation, is a violation of the Constitution. In the view of the Supreme Court, the State is competent to reduce income to a certain point. Down to that point the reduction is not a deprivation of property; beyond that point, it is. What is the point? It is the point of "reasonable income." A railroad is entitled to a reasonable income from its business; all income above that amount the state may freely take; but the state cannot reduce its income below that amount without making adequate compensation.

From what has just been said it naturally follows that the question,—do the rates in any given case deprive of property?—resolves itself into two others:

I. What effect will the rates have on the earnings of the company?

II. Will the earnings allowed by the rates be a reasonable income?

These two questions a court must answer before it can dispose of a railroad rate case. Now it is easy to see that they are difficult to answer. By what methods is a court to determine the effect of any given rates on earnings? And on what principles is it to judge the reasonableness of a company's income? These are serious questions, presenting many difficulties, and we shall therefore consider them separately and in detail.

I. First, as to the methods of discovering the effect of rates on earnings. There is only one fairly satisfactory way of determining this—for the railroad company to put the rates in operation for a period sufficient to dis-

close their effect on its earnings. But this method, however excellent abstractly considered, is anything but satisfactory to the companies. For if, after the period of trial, it appeared that their earnings had been unduly reduced (i. e., below the point of "reasonableness") they would have no adequate means of recoupment. Their only remedy at law would be to sue each one of the shippers who had used the road during that period for the difference between the rate paid and the fair rate—in many individual cases a trivial sum, but all aggregating a considerable amount. Thus the railroads would have no recourse except to multitudinous and unprofitable suits. It is because of this inadequacy of the remedy at law that the companies early resorted to courts of equity, and that those courts have recognized their right to an injunction restraining the enforcement of rates which seem calculated to unjustly diminish their revenues. Indeed the almost invariable form of action employed to test the validity of rates is a bill in equity to restrain their enforcement.

But what does this use of the injunction mean? It means that the courts are required to determine, before the rates have been in force at all, whether they will so seriously affect the future earnings of the company as to be repugnant to the constitution. Thus a task of great difficulty is imposed on the courts. It would not, indeed, be a simple matter to discover the exact effect of the rates after they had been in force for a year or more; but to estimate with sufficient accuracy for judicial purposes their future effect, must necessarily be a matter of intricate and elusive character. Nor is the difficulty of the task lightened by the fact that upon that estimate depends the constitutionality of an act of legislation which bears directly upon the welfare of the public and the railroads, as well as upon the success of a great system of railroad

regulation. Constantly has the Court asserted the embarrassing character of this question, but none the less has it recognized its duty to face it squarely.

How, then may the future effect of rates upon earnings be determined? The starting point from which judicial calculations proceed is the assumption that the traffic of the company will continue to be the same that it was for a period of time prior to the establishment of the rates. The effect of the rates is, therefore, to be determined by applying them to the past business of the company. This method might, indeed, seem questionable, in view of the universally acknowledged fact that a decrease in rates almost always augments the volume of traffic; and it might therefore seem only fair to assume that the business under the commission's rates, if they were lower than those formerly in force, would be greater than the past business. This view is supported by a solitary passage in the Wellman case where Mr. Justice Brewer said: "may it not be possible,—indeed does not all experience suggest the probability—that a reduction of rates will increase the amount of business and, therefore the earnings?"[34]

This passage, however, stands alone in the decisions of the Supreme Court. Exactly the opposite assumption has formed the basis of the reasoning in every other case. And, indeed, no better expression of the view actually held by the Court can be found than in the words of Mr. Justice Brewer himself in the Dey case:

"It is said that it cannot be determined in advance what the effect of a reduction of rates will be. Often it increases business, and who can say that it will not in the present case so increase the volume of business as to make it remunerative, even more so than at present? *But speculations as to the future are not guides for judicial action:* courts determine rights upon existing facts."[35]

[34] 143 U. S. 343.

[35] 35 Fed. Rep. 881.

And, apparently, " existing facts " must be interpreted to mean the business which the company has handled for a reasonable period prior to the establishment of the rates, and which may be regarded as assured to it for the future with reasonable certainty.

If, therefore, the actual facts of the past, rather than the probable facts of the future, are to form the starting point of the calculation, how is the Court to proceed? Several ways at once suggest themselves. Obviously the earnings of the company under the new rates might be determined by applying the rates to the former traffic. That is, the number of ton miles actually hauled might be multiplied by the new rate, the product representing the gross earnings from operation possible under the new rate should business neither increase nor diminish. This would seem to be a fair and reasonable, as well as a simple method, but curiously enough, it has not received the sanction of the courts. There is some authority for a method which compares the new rate with the actual cost of the service to be performed. Thus in the Becker case,[36] where the Minnesota Commission had fixed a switching charge of one dollar per car and the company alleged that the cost of switching one car had been $1.14, it was held that the new rates would be unremunerative. So, also, in the Gill case, where the legislature of Arkansas had fixed a passenger rate of three cents a mile, the company claimed that the actual cost of carrying a passenger a mile was three and three-tenths cents; and, in sustaining the rate because of the inadequacy of the company's evidence, the Court took no exception to this mode of attempting to show that earnings would be cut down below expenses.

It is submitted, however, that such authority for this

[36] 35 Fed. Rep. 883.

method as may be found in these two cases (one of them a circuit court case) is not sufficient to establish it as one to which the Supreme Court has lent its sanction. And in this conviction one is strengthened by the reflection that it is necessarily an erroneous method, inasmuch as it is utterly impossible to determine the cost of any particular service in the railroad industry, even when proceeding upon the basis of past business.

In every case in which the effect of rates upon earnings has been calculated, the Supreme Court has always employed a third method—one which requires a determination of the reduction made by the new rates in the schedules formerly in force. The percentage of reduction in gross earnings will, in contemplation of the courts, be equal to the percentage of reduction in the rates. Thus, in the Smyth case, as we shall presently see, it was found that the law reduced the rates formerly charged by twenty-nine and one-half per cent., and it was therefore held that the law would diminish *gross earnings* by twenty-nine and one-half per cent.

This is unquestionably the method approved by the Court, and employed in the great cases. It is clearly illustrated in the Dey, Covington, and Smyth cases. In the Reagan cases the same general idea was employed, though it was not asserted, because it was not necessary to assert, that the reduction in earnings would be in exactly the same proportion as the reduction in rates. And in the same proportion as the reduction in rates. And in the Minnesota Eastern case the method was impliedly approved, though it was not necessary to the decision of the case.

Since, then, the basis of the calculation as to whether the new rates will be remunerative, must be the former earnings, the former rates and the former expenses of the company, a further question becomes pertinent. When

the company presents evidence as to these matters, how long a period of time must the evidence cover? Must it show the earnings, expenses, and rates for one, two, three, or more years? This question has never been discussed by the Court, and, therefore, has not been authoritatively answered. The time covered by the evidence in actual cases has varied greatly. In the Dey case, it was one year. In the Wellman case the offering was again for one year, and although the suit went against the railroad it was not because of the short period covered by the evidence. In the Covington case, the business of the road "for a number of years last past" formed the basis of the contention; while in the Smyth case the term was three, and in the Reagan cases, a little more than three years. In the final disposition of the Tompkins case, evidence for one year only was held sufficient. It is evident, therefore, that three years are adequate, and it is probable that one would be regarded as sufficient, unless it could be shown to have been an exceptional year.

It may now be advantageous to illustrate this judicial method of determining the effect of rates on earnings by describing the process employed by the Supreme Court in an important and typical case. *Smyth v. Ames* furnishes excellent material for the purpose of such an illustration. That case involved the Nebraska Maximum Freight Rate Act of 1893, which contained a classification of freight and prescribed a general schedule of rates. Seven railroads were involved in the suit, and the problem before the Court was to determine the effect of the legislative rates on the earnings of those companies.

The Court approached the problem by approving the railroad's contention that a proper method of testing the legality of the rates would be to determine their effect had they been in force during the three years preceding their promulgation. Its next step was to announce as a

conclusion from the evidence that the act reduced the rates in force by 29.5 per cent., that is, that the legislative rates were on the average only 70.5 per cent. of the rates which were being operated in 1893 and had been operated for some three years or more as a result of voluntary action on the part of the roads concerned. These preliminary points determined, the way was open to attack the main problem.

The Court next presented a number of tables containing statistics regarding the affairs of the seven roads during the three years under discussion. From these tables the items of essential importance have been taken and are reproduced in the table below. It will be seen that in the first column is given the gross receipts from local, or infra-state freight received by each road each year. In the second column is given the amount of reduction which would have resulted from the Act had it been in force during each of the years. This, of course, is 29½ per cent. of the actual receipts—since it had already been decided that the rates were reduced 29½ per cent. by the Act. The third column consists of the remainders left after subtracting the amounts in the second from those in the first column, and shows the amounts which would have been received had the Act been in force. The next column gives the gross operating expenses incurred in handling the local freight. The last two columns are a result of comparing the third and fourth, and show the amounts which the companies would have gained or lost, so far as local freight is concerned, had they been operating the rates fixed by the Act.

1891	Gross receipts from local freight	Amount of reduction by Act—20½ per cent.	What would have been received under rates fixed by Act	Total expense of local business	Gain	Loss
Burlington Road	$1,066.871	$314,726	$752,145	$813,382		$61,237
St. Paul Road	110,933	32,725	78,208	89,611		11,403
Fremont Road	348,408	102,780	245,628	288,591	$37,087	
Union Pacific Road	278,211	82,072	196,139	219,619		23,480
Omaha Road	75,581	22,296	53,285	98,451		45,166
St. Joseph Road	21.817	6,436	15,381	23,221		7,840
Kansas City Road	6,732	1,985	4,747	7,374		2,627
1892						
Burlington Road	1,237,884	365,175	872,709	918,881		46,172
St. Paul Road	123,033	36,294	86,739	93,455		6,716
Fremont Road	336,714	99,330	237,384	271,761		34,377
Union Pacific Road	398,262	117,487	280,775	264,605	16,170	
Omaha Road	88,335	26,058	62,277	91,090		28.813
St. Joseph Road	31,004	9,146	21,858	26,114		4 256
Kansas City Road	6,630	1,955	4,674	5,648		974
1893						
Burlington Road	1,242,416	366,512	875,904	938,147		62,243
St. Paul Road	142,542	42,049	100,493	106,307		5,814
Fremont Road	424,437	125,208	299,229	270,193	29,036	
Union Pacific Road	413,714	122,045	291,669	283,435	8,234	
Omaha Road	80,519	23,753	56,766	83,851		27,085
St. Joseph Road	33,802	9,971	23,831	24,354		523
Kansas City Road	9,445	2,786	6,659	8,169		1,510

A word should perhaps be added as to the method of estimating the total cost of local freight business. Taking all business, the percentage of actual gross expenses to actual gross receipts was found for each company. It was then decided, on the basis of evidence submitted, that the percentage of operating expenses to earnings is, in general, fully 10 per cent. higher on local traffic than on all the business of a company.[37] The first percentage found was therefore increased by ten to get the percentage of expenses to earnings on local business. This percentage was then taken of the gross receipts from local freight. The result was the cost of the local freight business. For example, it was found that in 1891 the

[37] In other cases the Court has recognized the higher cost of local business above interstate or through business. "That there is a difference is manifest, and upon such difference the opinion of experts familiar with railroad business is competent testimony and cannot be disregarded." Chicago, Milwaukee and St. Paul Ry. Co. v. Tompkins, 176 U. S. 179. Because of this difference in cost the sum of two local rates conceded to be reasonable is not necessarily a reasonable through rate. Minneapolis and St. Paul R. Co. v. Minnesota, 186 U. S. 262.

percentage of expenses to earnings on all the business of the Burlington road was 66.24. The percentage of expenses to receipts on local business alone was accordingly held to be 76.24. But now, as appears from the table above, the earnings of the Burlington from local freight in 1891 were $1,066,871. The expenses of that freight were therefore 76.24 per cent. of $1,066,871, or $813,382. Similar calculations were made in each of the other cases.

Before concluding our remarks on the method of determining the effect of rates on earnings it is necessary to notice one further matter. A study of the illustrative case just described naturally prompts the following query. The doctrine of judicial review forbids a state to deprive a railroad of the reasonable income on its property without just compensation; yet in this case of *Smyth v. Ames* inquiry was not made as to the effect of the rates on the earning power of each company; the effect of the rates on earnings from *local freight only* was considered. But now, might it not be possible that the small loss on local freight business might not seriously affect the total earnings of the company from all sources—inter-state as well as local; passenger, express, etc., as well as freight? In other words, might not the company still be able to earn a reasonable income from its business in spite of this loss on local freight in Nebraska? And if so, why should the Nebraska Act be held to be repugnant to the Constitution?

This question was squarely presented in *Smyth v. Ames* and so far as questions of inter-state and local business are concerned was answered by the Court in the following language: "The reasonableness or unreasonableness of rates prescribed by a State for the transportation of personal property within its limits must be determined without reference to the interstate business done by the car-

rier, or to the profits derived from it. The State cannot justify unreasonably low rates for domestic transportation, considered alone, upon the ground that the carrier is earning large profits on its inter-state business. Nor can the carrier justify unreasonably high rates on domestic business upon the ground that it will be able only in that way to meet losses on its inter-state business."[38]

Continuing, the Court explained more definitely the reason for this view by quoting from the opinion of Mr. Justice Brewer rendered when the case was in the Circuit Court. " It may be as stated by counsel," that jurist had said, " that the annual earnings of the Chicago, Burlington and Quincy Co. are $27,916,128, and that the total amount of reduction[39] is only $365,175; . . . but the entire earnings of the Chicago, Burlington and Quincy are more than twenty times the receipts from local freight in Nebraska, and to reduce such earnings by twenty times $365,175, would make a startling difference in their amount. The fact that the State of Nebraska can reach only one-twentieth of the total earnings gives it no greater right to make a reduction in regard to that one-twentieth than it would have, had it the power over the total earnings and attempted in them a like per cent. of reduction. If it would be unreasonable to reduce the total earnings of these roads twenty-nine and a half per cent., it is, prima facia, at least, equally unreasonable to so reduce any single fractional part of such earnings."

From these quotations the relations of interstate and local traffic to the case are perfectly clear. A single state controls only part of the business of a road; as to that business it can reduce earnings only in a proportion which would be fair if applied to all earnings of the company—because, of course, it is only by means of this

[38] 169 U. S. 541.
[39] Caused by the Act.

principle that other jurisdictions to which the company is subject, can exercise an equal power of control. But there is another aspect of the question which is not at all clear. What may be said in regard to the purely local traffic which the State exclusively controls? That traffic consists of various elements—freight, passenger, milk, express and mail. Can the state justify an unreasonable reduction in earnings from freight [40] on the ground that the reduction caused thereby in the *total* local earnings is no more than reasonable, because of large earnings permitted on passenger and other traffic? Can a state, in other words, justify its conduct in controlling railroads, by showing that it permits a reasonable income from *all* of the business subject to its control—although the various elements in that business may be very unequally treated?

No explicit answer to this question can be found in the opinions of the Supreme Court. A fair inference, however, from the opinion in *Smyth v. Ames* seems to give a negative reply. From what is there said, it seems fair to conclude that the percentage of reduction in earnings from *each separate class* of *local* traffic must not be greater than would be reasonable were it applied to *all* the business of the company. It is true that some doubt is thrown on the matter by the last sentence in the quotation last given from Mr. Justice Brewer: "If it would be unjust to reduce the total earnings of these roads twenty-nine and a half per cent., it is, prima facia, at least, equally unreasonable to reduce any single fractional part of such earnings." The words, "prima facia, at least," are the significant ones. They imply that it is a presumption which may possibly be rebutted. Nevertheless Mr. Justice Brewer had himself just declared, in regard to

[40] That is, a percentage of reduction which is applied to all the earnings of the company would be unreasonable.

the evidence that the rates would reduce earnings by twenty-nine and a half per cent.: "The effect of this testimony is not destroyed by the table offered of the percentage of reduction on the total amount of business done by these companies in the state." And in the table referred to, "the total amount of business done by these companies in the state" meant the gross earnings from passengers and freight, both through and local, carried in Nebraska. All this would seem to imply that the compensatory effect of large passenger earnings would not be considered, and that the public regulation of each class of traffic must stand or fall by itself. This is only an inference, however, and in the absence of a direct decision on the point, no positive statement can be offered with confidence.

One or two other questions have arisen as to the earnings which should be considered when estimating the effect of rates established by a state. In the Gill case it was held that they should be the earnings from local business on all the line of company within the state, and not on any one part of it.[41] The Supreme Court has also recently held that a commission may impose very low rates on isolated articles of freight; and that it is not good defense for a railroad to show, in such a case, that the same rates applied to all classes of freight would prevent it from earning a reasonable income. The rates may be justified, if the company can recoup its loss on the particular articles from gains on other parts of its local business, so that a "reasonable income" is still earned. But whether the recoupment must come from gains on local *freight*, or whether it may come from gains on *all* local business is not clearly disclosed. It seems probable, however, that the former is the rule.

[41] 156 U. S. 666.

Let us now summarize the decisions as to the earnings which should be considered. That they should be the earnings from purely local, and not from inter-state business is certain; that they should be the earnings from the local business on the entire road of the company within the state is also certain; that they should be the total earnings from local freight if rates on a few articles only are concerned is probable, though not certain; and that they should be the total earnings from local freight if freight rates are concerned, from passenger traffic if passenger rates are concerned, and so forth, is also probable, though not certain. But for these uncertainties, then, it could be said that the earnings to be considered are the total local earnings from the class of traffic affected by the rates in question.

II. We have now discussed the judicial methods employed in determining the effect of rates upon earnings. This question answered, however, the work of a court in any case is but partly done. Before a reply can be made to the initial query—do the rates deprive of property?—a further inquiry is necessary. The court must ask whether the earnings permitted by the rates can fairly be called a "reasonable income" from the railroad's business.[42] If they can, then the rates do not deprive of property; if they cannot, the reverse is true. But now upon what principles is a court to determine what income is "reasonable?" This question we must now examine; and accordingly the next chapter will be devoted to its discussion.

[42] Supra, p. 54.

CHAPTER IV.

The Doctrine of Judicial Review.—III.

What are the principles by which the " reasonableness " of railroad earnings may be judged? The vagueness of the term " reasonableness " at once suggests the difficulty of the question. It is hard indeed to determine the principles; and harder yet to apply them in a concrete case. Yet the task of doing both of these things has fallen upon the courts, and consequently an attempt may be made to gather from their dicta and from their acts an idea of what, in judicial contemplation, the word " reasonableness " implies.

In pursuing this inquiry we have not the advantage of perfectly consistent expressions of opinion by the various courts, nor even by the several members of the Supreme Court, and an entirely satisfactory result is therefore impossible. The form of the problem confronting the judiciary, nevertheless, is evident. Are earnings reasonable if sufficient to pay only operating expenses? Or must they also cover fixed charges? May it even be true that beyond this they must provide a dividend upon the stock of the corporation? And, if so, how large a dividend is to be regarded as reasonable?

The difficulty of determining with precision the judicial attitude on these questions is enhanced by the fact that very much that has been said upon them has been of the nature of obiter dicta. Caution, of course, demands that proper discrimination be made between such dicta and principles which were, so to speak, essential in the decrees of the court. And a final construction of the judicial

doctrine on this point must necessarily give more weight to the latter than to the former.

A brief attention to some of the principal cases will best serve to introduce this subject. In the Dey case the railroad alleged that the reduction in the schedules would decrease earnings by a sum exceeding the amount paid out in dividends in each of the three preceding years, and that the effect would be to prevent the railroad from declaring any dividend at all. There being no evidence from the state to the contrary the enforcement of the rates was enjoined. In his opinion Judge Brewer declared what, in his judgment, constituted a reasonable income, stating it to be such as would cover all operating expenses, all fixed charges, and some dividend, however small, the size of the dividend being purely a matter for legislative discretion.[1]

In the Reagan cases a number or railroads were involved. All of them were in anything but a prosperous condition; some had never paid operating expenses, to say nothing of fixed charges and dividends. The best of them had not for three years been able to meet all of their fixed charges. It was shown that the rates imposed by the Texas Commission were lower than those formerly in force, and this, according to the theory of the courts already mentioned, was conclusive evidence that earnings would be reduced by them, The rates were accordingly suspended, the Supreme Court holding that because the roads had been operated in the past at a loss to the owners it was not just to so reduce rates as to increase the amount of that loss.[2]

In the Covington case the turnpike company set up that for a number of years last past its operating expenses had averaged about one-half of its earnings, that inasmuch as

[1] 35 Fed. Rep. 879.
[2] 154 U. S. 419.

the legislative act reduced the tolls about fifty per cent. its future earnings would barely cover ordinary expenditures; and that, moreover, certain extensive repairs would be imperatively necessary in the near future. The Supreme Court thereupon suspended the rates, stating that they were so low as to prevent the company "from maintaining its road in proper condition for public use, or from earning any dividends whatever for stock holders."[3]

In the Smyth case, as we have already seen,[4] the court determined that, generally speaking, the earnings permitted by the legislative rates would not cover operating expenses. It is true that in four out of the twenty-one cases presented in the table, some excess over expenses appeared, but as to those exceptional cases the Court held that "the receipts or gains above operating expenses would have been too small to affect the general conclusion that the act, if enforced, would have deprived each of the railroad companies involved in these suits of the just compensation secured to them by the Constitution."[5]

In the final disposition of the Tompkins case the Commission's rates were suspended because it was found that, while the earnings under the rates would be sufficient to pay all operating expenses, the balance left would not be sufficient to pay the proportion of the interest on the bonded debt properly chargeable to local traffic.[6]

The inference to be drawn from what has so far been said is that earnings, to be reasonable, must cover all operating expenses and fixed charges, and must even allow some dividend upon stock. In the Dey case, as we have just seen, Mr. Justice Brewer held that rates permitting any dividend, however minute, are fair, but a few

[3] 164 U. S. 592.
[4] Supra, p. 61.
[5] 169 U. S. 547.
[6] Railroad Co. v. Smith, 110 Fed. Rep. 473.

years later, in his opinion in the Wellman case, we find him implying, though not asserting, that the dividends ought to be "reasonable." "The courts," he declared, "should be fully advised as to what is done with the receipts and earnings of the Company, for if so advised it might clearly appear that a prudent and honest management would, within the rates prescribed, secure to the bondholders their interest and to the stockholders reasonable dividends." [7]

In regard to the size of the dividends to be allowed, some of the lower courts have gone even further than this. Thus, in the *New Memphis Gas and Light Co. v. Memphis*,[8] District Judge Clark held that the dividends to which a quasi-public corporation is entitled while under public control should "correspond to the ruling rate of interest." And in the Southern Pacific Railroad Co. v. Railroad Commissions [9] Mr. Justice McKenna, then a circuit judge, denounced the idea that a railroad company should be compelled to accept a "microscopical profit." In his view dividends ought to be adequate in every case —though what "adequate" might mean is not disclosed.

It is safe to say, however, that the Supreme Court has not indorsed these extreme views. On the contrary, it has been gradually assuming, in its dicta at least, a much more conservative attitude. The general principle which the Court seems to have adopted is this: that a railroad company is entitled to earnings sufficient to pay operating expenses, fixed charges, and some dividend—a reasonable dividend. But it has repeatedly declared that this is only a general proposition and that it may have many exceptions. That is to say, there may be cases in which earnings not sufficient to pay dividends, or not even sufficient

[7] 143 U. S. 345.
[8] 72 Fed. Rep. 952.
[9] 78 Fed. Rep. 236.

to pay all expenses and fixed charges will be held to be reasonable.

Thus in the Reagan cases it was said:

"It is unnecessary to decide, and we do not wish to be understood as laying down as an absolute rule that in every case a failure to produce some profit to those who have invested their money in the building of a road is conclusive that the tariff is unjust and unreasonable. . . . There may be circumstances which would justify such a tariff." [10]

Fully as pointed are the remarks of Mr. Justice Harlan in the Covington Case:

"It cannot be said that a corporation is entitled, as of right, and without reference to the interests of the public, to realize a given per cent. upon its capital stock. . . . The public cannot properly be subjected to unreasonable rates in order simply that stockholders may earn dividends. . . . If a corporation cannot maintain such a highway and earn dividends for stockholders, it is a misfortune for it and them which the Constitution does not require to be remedied by imposing unjust burdens upon the public." [11]

This same general idea was restated with much force by the same learned justice in *Smyth v. Ames,* and has received confirmation in other cases. In fact the Supreme Court, by oft-repeated dicta, has practically committed itself to the doctrine that, although as a general proposition, a railroad is entitled to earn reasonable dividends, that right is not absolute, but is subject to limitations.[12] Conditions may exist and circumstances arise which would justify the state in imposing rates under which earnings would be reduced to or below the dividend paying point. While but very few of these conditions have ever been present in any case in such a way as to affect the decision, and are therefore entitled to rank as precedents, many

[10] 154 U. S. 412.

[11] 164 U. S. 596, 597.

[12] See San Diego, etc. Co. v. National City, 174 U. S. 757.

others have been stated and some often restated as obiter dicta, and are therefore entitled to some consideration. We have, now, therefore, to inquire what those circumstances and conditions are which may in some cases justify rates too low to be profitable to the railroad, and which ,moreover, when a dividend is allowed, must enter into the determination of the question as to whether that dividend is reasonable. Throughout the discussion it should be borne in mind that *obiter dicta* alone are being dealt with, except where the contrary is specifically stated.

The circumstances recognized in the opinion of the Supreme Court may be classified under four heads—those affecting the base upon which the rate of profit should be reckoned; those which have to do with the management of the road; those which have to do with the rights of the public; and those which have to do with the industrial condition of the community traversed by the road. Let us consider these in order.

I. In the first place it has been held that what a company is entitled to demand is no more than a " fair return on the *reasonable value* of the property at the time it is being used for the public."[13] The rate of profit which should be secured by the rates must therefore be reckoned not on the capitalization of the company, but upon the " reasonable value " or " fair value of the property used by the railroad for the public convenience."[14] As a result of stock watering, or otherwise, the face value of the bonds and stocks may exceed this " fair value"; nevertheless earnings no more than a fair return on the real value need be allowed by the rates for distribution among the security holders. " If a railroad corporation has bonded its property for an amount that exceeds its fair value, or if its capitalization is largely fictitious, it may not impose

[13] San Diego Land and Town Co. v. National City, 174 U. S. 757.
[14] Smyth v. Ames, 169 U. S. 546.

upon the public the burden of such increased rates as may be required for the purpose of realizing profits upon such excessive valuation or fictitious capitalization."[15] The elements to be considered in determining the " fair value " of the property have of course been recognized as multitudinous, but in *Smyth v. Ames* the following enumeration was given to suggest such as are of special importance.[16]

1. The original cost of construction.

2. The amount expended in permanent improvements.

3. The present as compared with the original cost of construction.[17]

4. The amount and market value of the stocks and bonds.

5. The probable earning capacity of the road under the rates in question.[18]

6. The amount of operating expenses.[18]

7. Whatever other matters may be properly considered.

In the Reagan cases additional emphasis was laid on the third of these considerations. In its opinion the Court remarked that the construction of a road might

[15] Smyth v. Ames, 169 U. S. 544, and see San Diego, etc. Co. v. National City, 174 U. S. 757-8.

[16] 169 U. S. 547.

[17] It is not certain whether this means "present value" or "present cost of duplication" as compared with the original cost of construction.

[18] It is difficult to see what the fifth and sixth consideration have to do with this immediate question. The problem is to find the fair value of the property, in order to get a base upon which to reckon the percentage of profits which the tariff in question will yield. The *amount* of those profits is no doubt to be largely determined by the earning capacity of the road under the tariff, as compared to its operating and other expenses. If earning capacity and expenses are considered in discovering this amount of profits, it would of course be a mistake to consider them in determining value of the property to which that amount is to be referred in order to arrive at the per centage of profit.

have been at a time when material and labor commanded a high price, the actual cost of the road therefore exceeding its present value; and that, moreover, there might have been extravagance or needless expenditure of money on the railroad.[19] The actual outlay of money is not, therefore, in such cases, a test of the " fair value " of the property, and if securities had been issued to cover this outlay, they should not be taken as the base upon which to reckon profits. The same principle was later laid down with added force in the San Diego case.[20]

II. In the second place it has been held that unless the administration of a road has been economical and honest, the company's defense against legislative control is weakened. If its earnings have been reduced by its own imprudent or dishonest management, it cannot always successfully resist a reduction in rates on the ground of its already scanty revenue. Thus in the Reagan cases it was declared that if there has been waste in the management of a road, if the company has been paying " enormous salaries " or has been indulging in " unjust discriminations resulting in general loss," it cannot use the practices as a defense against legislative reduction in rates.[21] The legislative rates will be sustained if they would permit a reasonable income to a company which would abstain from such practices.

This general principle, moreover, is not supported by obiter dicta alone. In the Wellman case it was to a certain extent involved in the disposal of the suit. One of the grounds on which the Court sustained the rates was that the railroad had made no showing as to what had been done with its earnings. The court declared that it should be fully advised on this point, " for if so advised,

[19] 154 U. S. 412.
[20] 174 U. S. 757-8.
[21] 154 U. S. 412.

it might clearly appear that a prudent and honest management would, within the rates prescribed, secure to the bondholders their interest and to the stockholders reasonable dividends." [22]

III. In the third place, the Court has repeatedly declared that the railroad's right to earnings is further circumscribed by considerations relative to the rights of the public. In the Minnesota case[23] Justice Blatchford stated that the question of the reasonableness of a rate involved the element of reasonableness as regards the public as well as the railroad, and in his concurring opinion Justice Miller denied the right even of the legislature to make rates "in utter disregard of the rights of the public." [24] Again, in the Reagan cases,[25] in concluding his statement of limitations upon the right of railroads to profits, Justice Brewer said that there were doubtless many other matters affecting the rights of the community in which the road is built. The idea was expressed with much more force and elaboration in later cases. We have already had occasion to quote some of Mr. Justice Harlan's utterances on this point in the Covington case.[26] Again, speaking for the Court in the Smyth case, he referred to the railroads' contention that rates ought to permit the payment of dividends as well as all expenses, commenting upon it in these words:

"In our opinion the broad proposition advanced by counsel involves some misconception of the relations between the public and a railroad corporation. It is unsound in that it practically excludes from consideration the fair value of the property used, omits altogether any consideration of the right of the public to be exempt from unreasonable exactions, and makes the interests of the

[22] 143 U. S. 345.
[23] 134 U. S. 458.
[24] 134 U. S. 459.
[25] 154 U. S. 412.
[26] Supra, p. 71.

corporation maintaining a public highway the sole test in determining whether the rates established by or for it are such as may be rightfully prescribed as between it and the public." [27]

Upon this point the utterances of the Court have been clear, vigorous and numerous. Stated briefly, rates must be just both to the public and to the railroad:—these are the words in which the theory has been repeatedly phrased in the dicta of the Court.[28] Unfortunately, however, these dicta have always been obiter. The nearest approach to an exception to this statement may be found in the Gill case, which was a suit between a railroad and a private citizen, in which no public officers were involved. The company's contentions were admitted in the demurrer of its opponents; but, deciding that these contentions were not sufficient to prove the schedule unreasonable, the Court sustained it, adding, moreover, an expression of its reluctance to declare rates void when "the company's case depended on allegations admitted in the demurrer of a party who in no adequate sense represents the public."[29]

Aside from this, the numerous declarations of the Court, that the rights of the public are not to be ignored, that rates must be just to the public as well as to the railroad, and that therefore earnings must not be higher than what is fair, regarding the question from the point of view of the public as well as the corporate interest, have all been uttered as obiter dicta.

IV. Closely related to the principle just mentioned are certain other circumstances and conditions recognized by the court as important in determining the reasonableness of a railroad's income. Indeed, they may be regarded as more definite applications of the general and somewhat

[27] 169 U. S. 543.

[28] 164 U. S. 596, 598; 169 U. S. 547; 173 U. S. 687; and 174 U. S. 754-6.

[29] 156 U. S. 666.

abstract principle that the rights of the public must be considered. These are the considerations which pertain to the industrial condition of the country through which the road is built.

In a recent case the broad and very general rule has been laid down that when the condition of the country is such that rates high enough to pay operating expenses would be exorbitant, the legislature may impose lower one.[30] At first blush this declaration seems a little startling, but when it is remembered that the force of the rule depends upon the meaning given to the word "exorbitant," apprehension is speedily abated. No definition of the term was given in that case, nor has one been given since. The exact or even approximate meaning of the dictum is therefore still undetermined.

In other cases, however, the Supreme Court has been more specific. In the Reagan cases it held that a road which was unwisely built, in localities where there is not sufficient business to sustain a road, may not be entitled to earnings sufficient to remunerate those who have put money into it.[31] And in the Covington case it was held that when competition of new lines has so reduced business that earnings sufficient to yield a profit on the business would necessitate rates unjust to shippers and the public, the company must be content with smaller earnings.[32]

Such are the circumstances and conditions which, according to the dicta of the Supreme Court, are to be considered in determining what a reasonable income is, in the case of any particular railroad; such are the considerations which must decide the question as to whether the general rule shall prevail—that a railroad is entitled to revenue sufficient for all expenses and for dividends as

[30] Minneapolis and St. Louis Rd. Co. v. Minnesota, 186 U. S. 268.
[31] 154 U. S. 412.
[32] 164 U. S. 596.

well—and which furthermore determine the amount of dividends which may be regarded as reasonable, if any are allowed. This matter decided, a court's task is practically done. It has but to compare the earnings thus decided to be reasonable with the earnings possible under the rates in question. If the former are less than the latter the rates are valid; if greater, the rates will clearly general rule shall prevail—that a railroad is entitled to deprive the company of a part of its reasonable income, and to that extent will deprive it of property. In the absence of just compensation, therefore, the rates will be held unconstitutional and void.

In looking over this summary of "circumstances and conditions" one cannot but be impressed with the inadequacy of the principles which have so far been announced by the Court as controlling the question of reasonableness in earnings. Their inadequacy arises from two principal causes: first, their small number, and second, the vagueness and generality of some of them. At this point the doctrine of judicial review is in need of considerable elaboration, and of much more definite and detailed statement. It is to be hoped that litigation will soon make necessary the further development of this phase of the doctrine and will lead to its more thorough, more precise, and more concrete exposition. At the present time one of the crucial tests in determining the validity of rates—reasonableness of earnings—is but poorly understood; and public control of railroad rates must therefore find its progress retarded until the subject is fully illumined. For this weakness in the doctrine of judicial review, however, the Supreme Court is not to blame. For up to the present time but few points in connection with that subject have been presented to the Court for its decision, and therefore what principles we find in the reported cases are for the most part voluntarily tendered by the Court to promote a better understanding of a difficult subject.

What, now, is the doctrine of judicial review? We have seen the crude form which it took in the Minnesota case, and we have considered its evolution as it may be traced in later cases. It remains now simply to state what, as the result of the whole discussion, we may regard as the doctrine of judicial review. The following is offered as a formal statement of the doctrine:

I. Although railroad companies are *quasi*-public in character they are entitled to the protection of the Fourteenth Amendment. Therefore:

1. They cannot be deprived of property without due process of law. But to deprive a railroad of the reasonable income from its property without just compensation is to deprive it of property without due process of law within the meaning of the Amendment. Rates, then, which are calculated to reduce a railroad's earnings below the point of reasonableness are repugnant to the Constitution, unless compensation is made by the state for the property so taken.

2. They cannot be denied the equal protection of the laws. But if they are deprived of property without just compensation while other persons receive such compensation for property appropriated by the State, they are denied the equal protection of the laws.

II. There may, then, be a question raised as to the constitutionality of rates established by the state. This question it is, of course, competent for any court, and especially for the courts of the United States,[33] to decide. Its determination necessarily involves a consideration of three minor questions:

1. Whether the rates in question do deprive, or if they have not been put in force, whether they are calculated to deprive the railroad of those reasonable returns from its business to which it is entitled;

[33] 156 U. S. 657.

2. Whether the state has made any provision for reimbursing the railroad for such loss of property as may be involved, and

3. Whether such compensation is just and adequate. Should the first question be answered in the affirmative and the other two in the negative, or should the first two be answered in the affirmative and the third in the negative, the rates must be held to be repugnant to the Constitution, and must be restrained. Otherwise they must be sustained. In deciding the first question the courts determine the effect of the rates on earnings, and also the reasonableness of the company's earnings according to the principles and methods set forth in this and the last chapter.

It may be well to conclude this inquiry into the evolution of the doctrine of judicial review by setting forth a few miscellaneous considerations which may be found in the opinions of the Court. That the presumption is always in favor of the rates has, of course, been recognized, and in recent decisions there has been a well-marked tendency to specifically state that fact. On the authority of the Wellman case it may be said that rates should not be overthrown in a friendly suit, or upon agreed and general statements of fact, or upon the testimony of two witnesses. In the Tompkins case it was decided that the proper procedure is for a court to appoint a master whose duty it is to fully find all facts needed by the court in the determination of the case.[34]

In *Smyth v. Ames* the Court definitely commented on the idea so often implied in popular discussion that it is a strong argument against rates in one state to show that rates are, in general, lower in neighboring states. That little if any weight should be attached to such a contention is clearly inferable from the foregoing exposition of

[34] 176 U. S. 167.

the methods of the Court, for we have seen that the effect of rates is to be determined as to each railroad, with respect to its earnings and expenses on purely local business. In the case just referred to, however, the Court made inference unnecessary by quoting with approval the explicit statement of Mr. Justice Brewer in the court below:

"To enforce the same rates in both states might result in great injustice in one while in the other it would only be reasonable and fair. . . . A mere difference of rates in two states is of comparatively little significance." [35]

The question has occasionally arisen as to whether a court, in setting aside rates as unconstitutional, may substitute in their place others which in its opinion are conformable to the Constitutional requirements. This power the courts have never asserted. In fact they have definitely disclaimed it. "The courts are not authorized," said Mr. Justice Brewer in his opinion in the Reagan cases, "to revise or change the body of rates imposed by a legislature or a commission; they do not engage in any mere administrative work." And twice in the same opinion he reiterated the substance of this remark.[36] The true distinction which determines the answer to this question is most clearly drawn in the *Interstate Commerce Commission v. Cincinnati, etc. R. Co.*: "It is one thing to inquire whether the rates which have been charged and collected are reasonable—that is a judicial act; but an entirely different thing to prescribe rates which shall be charged in the future—that is a legislative act." [37] It is, then, beyond the scope of judicial authority to substitute valid rates for those which have been declared invalid.

Still another question has arisen in cases involving a state law which provides that the rates shall not be con-

[35] 169 U. S. 539.
[36] 167 U. S. 479, 499.
[37] 154 U. S. 397, 399, 400.

clusively reasonable, but that the railroad may test their reasonableness in the state courts. In the presence of such a law, may a suit be brought at once in a federal court? Such were the provisions of laws involved in both the Reagan and Smyth cases. There could be but one answer to the question, however, and it was given clearly by Mr. Justice Brewer in the Reagan case:

"No legislation of a state, as to the mode of proceeding in its own courts, can abridge or modify the powers existing in the Federal Courts, sitting as courts of equity. So that if in any case, there should be any mistaken action on the part of a State, or its Commission, injurious to the rights of a railroad corporation, any citizen of another state, interested directly therein, can find in the Federal court, all the relief which a court of equity is justified in giving." [38]

We have now concluded our study of the growth of the doctrine of judicial review and are ready to consider the effect which that doctrine has had on the efficiency of state railroad control.

[38] 154 U. S. 395.

CHAPTER V.

THE RESULTS OF THE DOCTRINE.—I.

We are now to undertake an investigation of the influence which the doctrine of judicial review has exerted on our American system of railroad control, in order to discover whether it has strengthened or weakened the efficiency of that control. In this inquiry we shall consider, first, its effect on the state's power to reduce rates; second, its effect on the state's power to enforce the rates it has established; and third, its effect, as a resultant of the other two, upon the spirit and ideas of railroad commissions.

Before coming to these precise questions, however, we shall do well to reflect for a moment upon the spirit of the law which has shaped the doctrine of judicial review, and which directs its application; for it will serve to illumine our entire discussion of this subject to recall at the outset the general attitude of the law and of the courts in all cases which involve both public and private interests. The attitude of the courts is determined by the fact that they are charged with the duty of interpreting and applying a law in which the individualistic spirit of the age has been firmly crystalized. In our modern regime the *individual* is the central figure. His importance, his dignity, his sanctity, his rights, and his liberties are everywhere recognized. His use of a free ballot is supposed to guard civil rights and to shape aright the course of government; his pursuit of his individual self-interest is supposed to secure industrial justice and welfare; his freedom of conscience, of thought, of will, and of action is not to be lightly infringed. "All men are created free and equal,"

says our Declaration of Independence, " and are endowed by their Creator with certain inalienable rights. . . . *To secure these rights, governments are established among men.*" The only limitation upon them is that they shall not, in their exercise, encroach upon the equal rights of other individuals.

It is true that this is a theory which has been gradually losing its hold both upon the minds and upon the hearts of men. So pernicious have been some of its results, especially in the world of industry, that the inquiry now is whether it has not passed the zenith of its usefulness, and whether it is not now necessary to modify it by an assertion of the social duties and responsibilities of individuals, and accordingly, by the enactment of laws restricting the individual for the general good. In this inquiry different minds have pursued different courses, have gone different lengths, and have, of course, reached different conclusions. Socialists would have us abandon the theory of individualism entirely and substitute therefor a theory of social duty, to be applied by the state. Long since, more conservative minds suggested factory legislation. Some thirty years ago, the consensus of public opinion demanded regulation of railroads for the public good. To-day there is agitation for municipal ownership, trust regulation, and other limitations upon private enterprise. This view is not intended to be complete. Its purpose is merely to recall the fundamental theory upon which our society is based, and some of the modifications of it which have been urged by many from time to time.

But while observing the gradual departure from the theory of individualism in industrial economics we must always remember that the law under which we live grew up with the growth of the individualistic theory and has received its stamp. The history of the English law is a

record of the successful struggle of the individual, first for recognition, and then for supremacy. Indeed our law is permeated, saturated, with the theory of individual rights. Two centuries ago English law had been shaped to that theory, while in our country it no less lies at the basis of our law; and its dignity has been recognized in the bills of rights of our state constitutions, and in most of the Amendments to the Federal Constitution. Such limitations as the state may impose on private rights are regarded as exceptions to the general rule, repugnant to the spirit and genius of the law, and therefore to be confined within strict bounds. Moreover—and this is a point of deep significance—for almost all purposes the law considers those artificial persons, corporations, as individuals entitled to the legal rights and privileges of natural persons.

This is the law which our courts are established to interpret and apply. "The primary duty of the courts," said Mr. Justice Brewer, in deciding Railway Co. v. Dey, "is the protection of the rights of persons and property." [1] And again, speaking for the Supreme Court in the Wellman case, he said, "the protection of vested rights of property is a supreme duty of the courts." [2] This duty, it must be admitted, has not been neglected. In railroad rate cases its demands have been faithfully obeyed.

Such being the character of the law in which our judges are trained, and such being the acknowledged duty of the courts in its application, it is but natural that the professional sympathies of judges should all be with the railroads. Not that the judges, as *men,* are callous to the abuses which for a third of a century have irritated the general public, sometimes beyond the point of endurance;

[1] 35 Fed. Rep. 872.
[2] 143 U. S. 346.

but nevertheless, as *judges,* they must apply a law which is in thorough sympathy with private persons, their property and rights, and which knows almost nothing of the "public welfare" except as it is to be secured through the assertion and maintenance of individual rights. If it be true, as is sometimes stated, that judges are disposed to subordinate the public weal to individual advantage, it is because they have entered fully into the spirit of a system of law which allows no other course.

In the light of these general observations, let us proceed to inquire the effect of the doctrine of judicial review, as developed and applied under our legal system, and first to notice the manner in which it has affected the power of the states to reduce rates.

Low rates are not, of course, the only ideal of railroad regulation. Doubtless the most important thing is *proportion,* that is, a proper adjustment of rates as among the various commodities and the various localities. But given this adjustment, the lower rates are, the better. There can be no doubt that the public interest demands that, so long as the due proportion is not disturbed, rates shall be as low as possible. A commission, therefore, being charged with the duty of advancing the public welfare, must require reductions in railroad schedules which are too high to be in accord with the public interest. And the efficiency of a commission must depend in no small measure on its ability to accomplish the reductions which are demanded by considerations of public utility. Now how great is its ability in this regard?

Clearly, if its action in the matter of rates were final and binding upon the companies, its power of lowering rates would be absolute. There would be no obstacle to prevent it from meeting in the most complete manner the requirements of the industrial situation. We have seen, however, that its rates are subject to review by the courts,

and the consequence of judicial review has been to seriously impair a commissioner's power to reduce rates. While it is impossible to measure with exactness the extent to which this power is impaired, it is possible to see that the limitation placed upon the commissions' activity in this particular is very great. And in order that this may clearly appear, let us consider at length three reasons why the doctrine of judicial review, as practically applied by the courts, stands in the way of public reduction of rates. These reasons may be stated as follows:

I. The doctrine fixes an improper limit beyond which reduction of rates cannot be carried.

II. The methods employed by the Supreme Court in determining the effect of rates on earnings are such as to make that effect seem more disastrous than is the fact.

III. The principles recognized by the Court in determining reasonableness of income are unduly favorable to the railroads, and afford no adequate protection to the interests of the public.

These propositions we shall take up in order.

I. The first limitation upon the state's power to reduce rates is found in that part of the doctrine of judicial review which requires that rates shall be high enough to permit the railroad company to secure reasonable earnings. A state cannot lower rates so as to reduce earnings below that point without making adequate compensation to the company for all earnings, below the point of reasonableness, which are so taken. For to take any part of a railroad's "fair returns" is to deprive of property,—an act which, under the Fourteenth Amendment, must be accompanied with proper reimbursement.

This phase of the doctrine of judicial review is certainly subject to criticism, and the criticism touches a point so vital as to call in question the entire doctrine. The vulnerable point is the distinction made between

earnings above the point of reasonableness, and earnings below that point. In effect the Court declares that above that point earnings are not property; but below it they are property; for the state may freely appropriate earnings above that point without violating the constitutional provision protecting property, though to take any below that point is declared to be a violation of it. This distinction is ingenious, and in making it the Court has perhaps saved from annihilation the state's right of rate control, but whatever merit may be claimed for it on that account, it may be admitted that it is a distinction which is artificial and which cannot be supported by reason. For, if income from property is itself property at all, surely all income must be property. To divide income into two parts—"property" and "not-property"—giving one part the protection of the constitution, and leaving the other defenseless, is an extraordinary proceeding. No one has ever thought of making a similar division in the case of any other kind of property. If the state were condemning a person's lot, it would not divide the lot into two parts and say: "one of these parts is property, and for it you may have compensation; but the other is not property, and for it, therefore, no payment will be made." Such a proceeding is unheard of, even in the case of property belonging to a quasi-public corporation. It cannot be imagined that the state, in taking any such property, would divide it into two parts and say: "one of these parts is property, and for it compensation will be made, but no payment will be made for the other because it is not property, since you are a quasi-public corporation and, your property being devoted to a public use, a part of it has ceased to be property"! But the absurdity is more clearly seen when such a distinction is applied, not to real estate or equipment but to the income of railroads. Suppose the state were to seek in the treasury of a rail-

road company the earnings it had received from the operation of its road, and were to attempt to appropriate those earnings. There is not the least doubt that if the appropriation were permitted at all, the courts would require the state to reimburse the company for every cent of the earnings taken. The wildest stretch of the imagination cannot picture the courts saying to the state: "a part of these earnings are reasonable, and hence are property, and if you take them you must recompense the company; but the rest of the earnings are not property, because not reasonable, and you can have them for nothing." Yet this is just what the Supreme Court has said in regard to depriving a railroad of its income through the agency of low rates. The distinction is clearly without warrant and must be given a place among the pure fictions of the law.

It is evident from the absurdity of this distinction, which the Court has found it necessary to maintain in order to prevent judicial review from practically denying the established legislative power of rate control, that somewhere in the reasoning of the Court there is an error which is fundamental and which vitiates the whole process. That error, it is believed, consists in the actual, though not professed, transfer of rate regulation from the basis of the police power, where it has always been held to rest, to the basis of the eminent domain. While continuing to insist *in words* that rate control is an exercise of the police power, the Court has *in fact* treated it as if it were a phase of the power of eminent domain. The Court has apparently looked upon it as a means whereby the state may take property (in the form of income) for public use, and has consequently subjected it to the ordinary rules of eminent domain, requiring just compensation for property appropriated. It is because of this change of base that the Court has been

driven to the dilemma of holding either that all income is property, which practically denies the ancient legislative right of control, or else that none of it is property, and hence that all of it is beyond constitutional protection, which the judicial mind is unwilling to concede. From this dilemma our jurists have extricated themselves by advancing the extraordinary idea that a part of income is property and a part is not. But they would have saved themselves from getting into the dilemma, and so would have spared themselves the necessity of resorting to this untenable fiction, had they actually continued to regard rate control in the light of their own repeated assertions, as a phase of the police power. For viewed as a part of the police power, rate regulation is, of course, not subject to the rules applying to the condemnation of property. It is the exercise of an entirely different sovereign power, subject to entirely different rules and restraints. If the court should really so regard it, there would be no question of appropriation or compensation to consider, no inquiry as to the effect of rates on earnings would have to be made, and hence no classification of income.

But, it may be objected, though rate regulation is a part of the police power, is it not true that in its exercise the income of the railroad may be decreased, which would amount to a deprivation of property, income being regarded as property? True;—from the control of rates many consequences may flow, and among other results, the income of a company may be reduced. But that is a consequence which also flows from other police regulations which the state may adopt. Railroad rate control is not peculiar in that regard. Yet no one thinks of subjecting other police regulations to the rules of eminent domain. Thus the legislature may pass laws requiring railroads to put in cattle guards at highway crossings, or to equip each passenger car with an ax, saw, and ham-

mer, or with drinking water, or to substitute, within a given time, automatic couplers of a certain type for the couplers in use. Any of these requirements would necessitate an expenditure of money and consequently would reduce the net income of the company by increasing expenses while the improvements were being installed. In effect, if one wishes to think of it in this way, it amounts to an appropriation of property for a public purpose. A portion of the income, instead of being devoted to paying operating expenses, or interest on bonds, or dividends on stock, must be expended in a manner required for the benefit of the public. Thus income is affected just as truly,—though in a somewhat different way—through these measures as through rate control. A railroad company may be deprived of income just as truly through police regulations requiring an expenditure of money for the public welfare, as though those requiring a reduction in rates.

Nevertheless a railroad company is not permitted to object to ordinary police regulations on the ground that its "reasonable income" is threatened. A case can be imagined where a railroad could show that its existing income was no more than reasonable, and where the courts would so hold. In such a case to enforce a law requiring the installation of new couplers or other equipment would so increase the expenses of the company that the income would no longer be reasonable. Its existing income being just barely a reasonable one, to require expenditures from it for the public good would be in effect to deprive the company of a part of its reasonable income. But could the company demand compensation for the sum so taken? Of course not. In passing upon police regulations a court does not consider their incidental effect on earnings. It makes no difference whether the road can earn a reasonable income under them or not.

A company in the last stages of insolvency is just as subject to them as the most prosperous of roads.[3]

In short the state is permitted through police regulation, to appropriate earnings for the public benefit without any obligation, under the Constitution, to provide compensation. But the police power differs from eminent domain in that the appropriation of property is not direct, but is incidental and resultant. The direct and immediate effect of a police regulation is always the establishment of some condition or method or other regulation which the public safety or welfare or comfort demands. And its indirect or consequent effect on income is not regarded as a deprivation of property such as is contemplated in the law of eminent domain. There is no valid reason why an exception to this rule should be made in the case of that form of police regulation called rate control. It is a perfectly legitimate exercise of the police power and should certainly be treated in the same way as other police regulations,—at least it should not be subjected to more stringent restraints.

Two objections to this view of the case might conceivably be raised, neither of which, however, it is believed, is well taken. In the first place it may be said that there is a difference between rate control and other forms of

[3] It should be noted that the validity of a police regulation is not a matter which is personal to certain individuals within the class affected, but rather is a quality of the regulation itself. A factory act applying to factories of a certain class is never valid as to some and void as to others. Its validity is determined on its own merits, irrespective of its financial effect on certain factories, and if it is held to be a valid exercise of the police power, it is binding on all the persons coming within its terms. Yet a general schedule of railroad rates may, under the present judicial doctrine, be held void as to one road but binding upon another, perhaps a competing line. This unfortunate consequence is, of course, a result of bringing into rate cases the rules of eminent domain, instead of judging rates on their merits, as a police measure designed to promote the public welfare.

police regulation, in that the latter are of real benefit to the company. The railroad is in possession of equipment which proves of decided advantage to it. For example, its automatic couplers and cattle guards decrease accidents, with their losses of property and subsequent damage suits, while passenger car equipment encourages patronage by the greater security and comfort offered to travelers. But two replies may be made to this objection. One is that public regulation of rates also is of advantage to the company. It does away with law suits to recover damages for overcharge, for a company is never guilty of extortion so long as it keeps within the maximum fixed by the state. Moreover, it tends to increase the popular favor in which the roads are held and to encourage traffic. The development of industry resulting from efficient public regulation is in itself of great advantage to the roads. But while this answer to the objection can be made, a better one, and one fully sufficient, is this: that the benefit which a police regulation confers on the road is *not* the reason why the courts do not subject the regulation to the law of eminent domain. The reason is simply that it is not an exercise of that power. The second possible objection is that a regulation of rates necessarily affects income; but that in the case of other police laws the company may recoup whatever expense is involved, by raising its rates and so increasing its earnings. The reply to this objection is that a company is not able thus to manipulate its earnings. It is at many points subject to competition, and so is not, commercially speaking, free to raise its rates. And an increase of rates at any point might simply have the effect of decreasing traffic, so that earnings would be but slightly increased, if at all. Moreover, it may be that the state has prescribed rates and they are in force, so that the company is without legal power to raise its rates,

and thus without the means wherewith even to try to recoup the expense forced upon it. Even here the attitude of the courts is just the same. A railroad cannot claim exemption from police regulations because it is unable to make up the expense through the manipulation of its rates.

We conclude, therefore, that since rate control is an exercise of the police power and not of the eminent domain, it should not be subjected to the law of eminent domain; that, accordingly the test of its validity should not be, as is now held by the courts, its effect on the income of the company.

Does this mean that the legislative power of rate control is absolute and without limit? No. It simply means that the legislature is subject to the same limitations that it is in exercising other forms of the police power. In other words, the validity of rate control is to be determined just as the validity of other police regulations is determined. The same test that is applied to them should be applied to it. The question upon which the validity of a cattle-guard, or automatic coupler, or drinking water law hangs,—or, for that matter, a factory act, or sanitary legislation, or an inspection law—is whether a sufficient public interest demands the law. Upon that same question should the validity of rate regulation depend. It should be a question of public welfare. And therefore just as a court sometimes sets aside a police law because its enactment is not justified by the public advantage to be secured through its operation, so rates made by public authority might be set aside on the same grounds. But this is vastly different from saying that their effect on earnings should be the conclusive test in determining their validity.[4]

[4] Of course it is perfectly conceivable that the effect of rates on earnings might be *one* of the points considered by a court. It might be made a question whether the public interest demanded certain

If the view of the matter here suggested were to command acceptance, judicial review would be transformed. Instead of being what it now is, it would become a judicial investigation designed to apply to rate control the same test which is judicially applied to other police regulations. And beyond a doubt this would result in giving to legislatures and commissions much greater freedom of action in rate matters than they enjoy under the present doctrine. The full measure of their proper authority, of which they have been largely deprived by the courts, would be restored to them. And that it is their proper authority is made more evident by the following consideration. A state may, of course, and frequently does employ the police power to control private persons in matters of private concern. In such cases, as has been said, the regulation stands or falls according to whether the public interest, welfare, safety, health, morals, comfort, or, sometimes, even convenience, demand it. If that is the only limitation placed upon the legislature in its control of private persons in their management of private matters, surely no more stringent limitation should be placed on it in its regulation of the management of public business by quasi-public corporation. Indeed there is evidently much ground on which to contend that legislative authority should be even more extensive over public than over private business. It would certainly seem that the government should have more control over property devoted to public use than over property retained for purely private use. It is not an immoderate suggestion, therefore, that the authority

rates, if they reduced income so much that bare operating expenses could not be paid, for in that case the road might have to suspend operation. But even if the effect of rates were so considered, the limitation on legislative action would be decidedly different from what it is at the present time.

in the first case should be barely equal with that in the second.

That a broader governmental power over rates would render more precarious the earnings from railroad properties is evident, but that, of course, is simply one of the hazards which one must contemplate in going beyond the boundaries of private enterprise, into the uncertain field of public activities. A forcible judicial expression of this idea may be found in the words of Mr. Justice Brewer, uttered *obiter,* in Cotting v. Kansas City Stock Yards Company.[5] In entering a public business, said he, a person " expresses his willingness to do the work of the state, aware that the state in the discharge of its public duties is not guided solely by a question of profit. It may rightfully determine that the particular service is of such importance to the public that it may be conducted at a pecuniary loss, having in view a larger general interest. At any rate, it does not perform its services with the single idea of profit. Its thought is the general public welfare. . . . Is there not force in the suggestion that as the state may do the work without profit, if he voluntarily undertakes to act for the state he must submit to a like determination as to the paramount interests of the public? "

In this connection it is instructive to notice that in other ways persons embarking in a public business must assume the risk of losing much or even all of their investments. Such dangers exist,—have been permitted by the courts to exist even since the adoption of the Fourteenth Amendment. Thus, it has been held that a state may grant a franchise to one railroad to parallel an already existing road. The value of the older property may be impaired by competition with the new road, yet

[5] 183 U. S. 93.

it is held that the owners have no vested rights which can prevent its construction and operation. So also the value of a turnpike may be practically annihilated by the state through a franchise permitting a parallel railroad. Yet it has been held that the Fourteenth Amendment does not command just compensation in any sense which would require the state to compensate the turnpike company for the property so taken.[6] When the public welfare demands more efficient means of transportation, the owners of existing roads must expect to suffer; and the courts, aside from declining to relieve them, have not even claimed that any one but the legislature should be the final judge of the public necessity of the new improvement. A power such as this is one which properly belongs to the state to enable it to deal with property devoted to a public use in a manner conducive to the welfare of the community, and one of which the state has been deprived, so far as rate regulation is concerned by the doctrine of judicial review.

We thus conclude the discussion of our first reason why the doctrine of judicial review has seriously impaired the legislative power to reduce rates. It has fixed a limit beyond which reduction cannot be carried, and that limit is an improper one. By basing rate regulation on eminent domain rather than on the police power, it has prevented the legislatures and commissions from exercising the authority that is their right, and has thus subjected them to a serious restraint.

II. But this is not the only reason why the judicial doctrine has impaired the power of the state to reduce rates. The present judicial limit on legislative action is, as we have seen, the point of "reasonable income." But while the

[6] For further illustrations see Cooley's Principles of Constitutional Law, 3rd ed., p. 370.

Court has repeatedly declared that this is the proper limit, it has, nevertheless, adopted principles and methods in the trial of rate cases which do not permit a state to fix rates so as to reduce income even to the point of reasonableness. In other words, the Court employs principles and methods which unduly favor the railroad and unduly restrict the state; and thus the legislature cannot exercise even the limited authority which the Court has in general terms allowed it. Rates may be made which will not actually reduce the income below the point of reasonableness, yet the Court may hold that they will—so erroneous is the way in which it determines that point. In the further elucidation of this contention, let us consider the methods by which the Court determines the effect of rates on earnings. We shall see that those methods inevitably make that effect appear more favorable to the railroads than is really the case.

As we have already seen,[7] the Court begins with the rule that the effect of rates upon earnings shall be determined on the basis of *past* business. That is, the judicial estimate of earning capacity of the road under the new rates is arrived at on the assumption that the rates will neither increase nor decrease the traffic, but that the traffic will remain the same that it was for a period of time prior to the establishment of the rates.

Extraordinary as this assumption is, it is one which, as we have seen from our review of the cases, the courts have repeatedly recognized as legitimate. It need hardly be said that in this matter the courts have failed to take into consideration one of the most fundamental characteristics of the railroad business. For it is a matter of general knowledge that, usually, a reduction in rates results in an increase of business. At this stage of the railroad controversy no argument is needed to prove this

[7] Supra, p. 58.

contention, nothing beyond a mere appeal to those general facts of which all are cognizant. Curiously enough, it was even admitted, with innocent frankness, by Mr. Carter, of counsel for the railroads in Smyth v. Ames. In arguing that there are sufficient protections against the danger of extortion, he said, "Moderate charges yield more profit by the greatly increased business they draw. A sound policy perfectly well known to railroad managers, advises them that it is better to tempt and draw out a large traffic by low prices than to try to make a large profit on a small business."[8]

In spite of this universally accepted fact, however, the courts have definitely settled that the effect of lower rates may properly, for judicial purposes, be determined on the assumption that increase of business will not result from the decrease in rates. It must, of course, be admitted that compensating circumstances may occasionally prevent an increase in traffic, but such an occurrence is out of the ordinary. The rule remains that a reduction in rates, other conditions remaining the same, always tends to augment the volume of business. For the courts, then, to proceed upon the assumption which it does, is to unduly favor the railroads. It enables them to make a stronger case than they could were the correct assumption to be made. Upon this principle the judicial view must always be that rates will more seriously affect the earnings of the companies than would be true in nineteen cases out of twenty. As a matter of fact, to put the rates in operation might not reduce either gross or net earnings at all, or might reduce them but slightly. Yet, in contemplation of the courts, earnings would be diminished exactly in proportion to the reduction in the rates.

Of course it may be urged that this is the only definite test which the courts can apply; that to attempt to esti-

[8] 169 U. S. 506.

mate the probable increase in traffic resulting from a decrease in rates would involve the courts in speculations in which they could never have the guidance of reliable principles.[9] Let this be granted as true; let it be conceded that the courts can find no other test. Nevertheless that fact does not make the test a good one, nor one adequate to the needs of rate cases, nor does it affect the fact that the test gives to the railroads an undue advantage as against the public.

No more favorable is the view which must be taken of the next step in the procedure of the Court. After declaring that the effect of rates upon earnings must be decided on the basis of past business, the Court goes on to hold that that effect must further be determined by applying to past earnings the percentage of reduction in the rates.[10]

If the effect of the new rates upon earnings were to be determined at all on the basis of past business, it would seem that the correct method of arriving at the result would be to apply freight rates to past tonnage, and passenger rates to past passenger traffic. This would give the maximum earnings which could be secured by the railroad under the new rates, on the condition, assumed by the courts, that traffic would continue unchanged. Instead of this method, however, the courts determine the percentage of reduction made by the new rates in the rates in force, and then assume that future earnings will equal past earnings reduced in the same proportion. For

[9] "It is said that it cannot be determined in advance what the effect of the reduction of rates will be. Often times it increases business, and who can say that it will not in the present case so increase the volume of business as to make it remunerative, even more than at present? But speculations as to the future are not **guides for judicial actions; courts** determine rights upon existing facts."—Mr. Justice Brewer in Chicago, etc. Ry. Co. v. Dey, 35 Fed. Rep. 881.

[10] Supra, p. 58.

example: Suppose that past earnings were $1,000,000, and that the new rates are 80 per cent. of the old rates. It is assumed by the courts that earning capacity under the new rates will be $800,000.

Now, here, again, is an assumption which gives the railroads a distinct advantage in suits involving rates. For the basis of the whole process is the reduction made by the new rates in the old schedules. Yet the old schedules, of course, contain only the *nominal* rates established by the railroad. As a matter of fact, in very many cases, the *actual* rates charged are lower than those named in the schedules. Discriminations, rebates, drawbacks, preferential advantages, all awarded, usually, under the veil of secrecy, are not yet, unfortunately, things of the past. The past earnings of the company, therefore, have been derived, not by charging the rates fixed in the schedules, but by charging rates which average considerably less than those scheduled. When the courts, then, compare the new rates with the old *nominal* ones, they discover a percentage of reduction greater than the percentage of reduction made by the new rates in the old *actual* ones. The assumption, therefore, that the earning capacity of the road will be reduced in proportion to the greater percentage, is clearly wrong. It makes the company's criminal practices a source of advantage to it, and of disadvantage to the public, in the trial of rate cases.

For example, let us make the same assumption, made above, that past earnings were $1,000,000, and that the new rates are 80 per cent. of the old nominal rates. In such a case the courts hold that the maximum earning capacity of the road under the new rates will be $800,000.

Suppose that the nominal rate per mile was $.01; the new rate is, then, $.008. Now, it is evident, from the merest knowledge of railroad practices, that the earnings of $1,000,000 were not secured by charging an average

of $.01 for each of 1,000,000 ton miles. As a matter of fact, the actual average rate charged was less than $.01. It might have been $.009, or $.008, or $.007, or even less. But in order to deal generously with the railroad, let us assume for the moment that it was as high as $.009. Then, the earnings of $1,000,000 were secured by charging $.009 for each of 111,111,111 ton miles. The actual traffic, therefore, being 111,111,111 ton miles, to put in force a rate of $.008 would give an earning capacity of $888,888.88. This indeed, is less than the former earnings, but, on the other hand, it is over $88,000 greater than the earning capacity which the Court assumes the railroad would possess under an $.008 rate.

Now let us alter our last assumption, and suppose that the actual average rate which earned the receipts of $1,000,000, was low, say $.007. Then the $1,000,000 were earned by charging $.007 for each of 142,857,142 ton miles. But to apply to that tonnage a rate of $.008 would give an earning capacity of $1,142,857. This is greater by $142,857 than the old earnings, and is $342,857 greater than the earning capacity reached by the processes of the Court.

Thus it appears that the earning capacity determined by the courts is always less than that which the railroad will actually possess under the new rates. Furthermore, it appears that the earning capacity of the road under the new rates, if it will abstain from discrimination, may even exceed the actual amount of earnings received under the old rates.

This practice of the courts, then, is always unfair to the new rates, since it makes out their effect upon earning capacity be to more disastrous than it will be, except in the purely hypothetical case of a road which has not deviated from its nominal rates. As an item in a test of reasonableness, it is, therefore, clearly inadequate, and

unduly favorable to the railroads. Under this practice, the more flagrant a company's violations are of the laws against discriminations, the more complete is its immunity from public regulation of its rates. In any event, a railroad is able to make out before the Court a stronger case than it has in fact.

True, in the Reagan cases, it was laid down that a railroad's right to profitable compensation is limited, *inter alia*, when it has indulged in "unjust discriminations resulting in general loss."[11] Accordingly the way is opened for the state to attempt to prove the unjust discriminations of which the road has been guilty. But satisfactory evidence upon such matters is, of course, almost impossible to get; and even were it secured, it is not certain to what extent and in what way the courts would make use of it. So far as the question of the effect of rates upon earning capacity is concerned, no fair or correct result can be secured by the method now employed by the courts. As said above, if past business is to be the basis of the calculation at all, the correct method would seem to be the application of the new rates to past tonnage, or past passenger traffic. Without discussing this point farther, however, it is sufficient for our present purposes to note that the method now employed by the Court may often result in the suspension of rates which, while looking toward the public welfare, are not really calculated to impair the earning capacity of the railroads, to say nothing of reducing it to the point of "reasonable returns."

III. Beyond this, however, it may be urged that the judicial conception of "reasonable income" is not adequate. At least it may fairly be said that the principles which the Court has laid down as the controlling considerations in determining reasonableness of income, have

[11] Supra, p. 74.

so far proven unduly favorable to the railroads, and have not, as yet, given proper expression to the interests of the public. Let us recall what these principles are. Briefly stated, the Court has held [12] that a railroad's earnings must be sufficient, in general, to pay all expenses, including interest on bonds, and yield a reasonable dividend upon stock, but that the reasonableness of the dividend, and, indeed, a railroad's right to any dividend at all, is dependent upon a large number of considerations. These considerations, we have also seen, may be grouped into four classes—one pertaining to the base upon which the rate of profit shall be reckoned, the second to the management of the road, another to the rights of the public, and the fourth to the industrial condition of the community.[13] The enunciation of these limitations upon a railroad's right to compensation is a most interesting feature of rate cases. At first blush it might seem that they are admirably calculated to aid in restoring the proper balance between the public and private interests. Yet it cannot escape observation that almost all of them are simply obiter dicta, and investigation shows that the Court has often forgotten them, either in determining procedure or in deciding special cases.

A few instances of this kind will serve both to explain and to enforce the point. In the Reagan cases is laid down the doctrine that the failure of rates to yield profitable compensation is not conclusive of reasonableness when, *inter alia,* the railroad has indulged in unjust discriminations resulting in general loss. And yet, as has just been seen, the Court has employed a method of determining the effect of new rates, which enables a railroad to take refuge under the very shelter of its own discriminations, and from that safe retreat, protected by

[12] Supra, p. 70.
[13] Supra, p. 72.

the strong bulwark of the law, to defy legislatures and commissions. Again, the Reagan cases also recognized a limitation when a road was unwisely built, in districts where there is not sufficient business to sustain a road. Yet such was the case with almost all, if not all, of the roads involved *in those very cases.* The International and Great Northern had never been able to pay the interest on its bonds, and had been in a receiver's hands for three years. Of two other roads the Court speaks as follows:

"The St. Louis Southwestern Railway Company is called by counsel for defendants, in their brief, 'a reorganized bankrupt concern.' It would seem to be a railroad *which was unwisely built, and one whose operating expenses have always exceeded its earnings.* Counsel say that 'it is familiarly known as a "teazer," and, if it ever passes beyond this interesting but unprofitable stage, even its friends will be surprised.' We are not advised and we can hardly be expected to take judicial notice of what is meant by the term "teazer," but *it is clearly disclosed by the record* that this was an unprofitable road. . . . The Tyler Southwestern Railway Company has a short road of ninety miles, and also appears to be a 'reorganized bankrupt concern,' and one whose road has been operated with constant loss." [14]

Here are cases which clearly, by the admission of the Court, come under the general limitation expressed in the body of the opinion. Yet the limitation was entirely ignored. After making the statement quoted above, the Court continued, "it will not do to hold that, because the roads have been operating in the past at a loss to the owners, it is just and reasonable to so reduce the rates as to increase the amount of that loss." Here, then, one who has read, a few pages back in the opinion, the general rule laid down by the Court, finds the hopes aroused by it most rudely dashed.

Further evidence may be found of the Court's tendency

[14] 154 U. S. 403.

to ignore the limitations upon a railroad's right to profitable rates. It is worth while mentioning that the Court in the Reagan cases specifically denied two claims which were allowed in general terms in later cases. The Covington case limits the railroad's right when competition of parallel lines so diminishes business as to make profitable rates exorbitant, and the last Minnesota case further limits that right when the industrial condition of the country is such that profitable rates would be exorbitant. Yet in the Reagan cases the Attorney-General showed that there were four lines in competition with the International and Great Northern, reducing its share of the traffic; alleged that there had recently been a commercial depression; and offered evidence to show that the price of products was so low that rates would have to be lower than those charged by the railroads in order to permit the farmers to market their produce with any profit. All this was not gladly received by the Court, as tending to support the rates which are " presumed to be reasonable." On the other hand it was summarily dismissed, and given no weight whatever in the case. We are accordingly left in grave doubt as to whether the court meant much if anything by its later dicta in the Covington and the last Minnesota cases. At any rate, it is evident that the play of the Court's sympathy for individual as opposed to public rights, operates to seriously limit the limitations, as it were, which it has recognized upon the rights of the railroads. The view of the railroad industry which has been taken by the Court since the Granger cases requires the limitations to be stated; but the predilections of the judges create a tendency to disregard them. As statesmen, or publicists, the judges might recognize the full force and importance of those limitations; but as *lawyers or judges,* they almost inevitably forget them.

It is true that as yet the Court has not been put to a

severe test, and consequently it is not clear to just what extent it will go. For, up to the present time, counsel for the states have shown comparatively slight disposition to urge upon the Court the limitations it has recognized, or to introduce evidence in such matters. The Court by its repeated declaration and affirmation of its dicta, has offered an opportunity the significance of which has apparently not been fully appreciated by the representatives of the public. But the treatment which those dicta have received in the cases where they have been urged, as we have just seen, forbids any very sanguine hope that they hold much promise of better things for public control.

But it is not only because the Court tends to ignore in special cases the rules it has laid down in general terms, that they are not available for the cause of the public welfare. A further reason is that many of the limitations upon the rights of the railroads are so vague in character, and involve considerations so difficult to establish, that the public can derive little advantage from them. One illustration of this fact is to be found in the limitation which is recognized to exist when the management of the road has not been prudent and honest. But how difficult must it always be for state officers to secure satisfactory evidence upon such a point! The secrecy which enshrouds many railroad operations, and the possibility of manipulating accounts makes difficult even the discovery of imprudence and dishonesty, to say nothing of securing evidence which will be satisfactory at law.

Again, the courts have, in general terms, given recognition to the rights of the public. In the Gill case the Court was hesitant to declare rates unreasonable when, among other things, the claims of the railroad were admitted in the demurrer of a party who in no adequate sense represented the public. In the Reagan

cases it was said that the right of the road to compensation is limited, among other things, by "matters affecting the rights of the community in which the road is built."[15] And in the Covington and Smyth cases, it was stated that the rights of the public are not to be ignored, that rates must not be more than the services are worth to the public, that, in short, rates must be just to the public as well as to the railroad.[16] But what are the "rights of the community," or the " rights of the public," and how are they to be established? How is it to be determined what a railroad's services are worth to the public? How, indeed, is it to be discovered what rate is just to the public as well as to the railroad? And, when the interests of the public and of the railroad clash, which is to prevail? It need hardly be stated, in view of the preceding discussion, what the coloring is which must necessarily prevail in the Court's answers to these questions. The rights of the public are indeed difficult to establish. Generally speaking, the public has rights, which must not be invaded by the railroads. But specifically, what rights? To be exempt from the high rates necessary to compensate a railroad for losses due to its discriminations, or necessary to make profitable a road unwisely built, or necessary to sustain as many competing roads as may chance to divide the traffic? We have seen what answers the Court has given to these questions. The vague " rights " of the public have vanished with the appearance of a practical test.

But there is still another " limitation " upon the right of the railroad to compensation, namely, the industrial condition of the community, which is too vague and general to mean much in practice. Here again, it may be asked, how is the industrial condition of the community

[15] 154 U. S. 402.

[16] 164 U. S. 596-8; 169 U. S. 544-7. And see also, 173 U. S. 754-6.

to be established at law, and just what "industrial condition" will justify a reduction of a road's earning capacity? Is it not inevitable that counsel for the state should find it difficult to secure satisfactory evidence in such a matter? The limitation is in general terms. In specific cases how much would it amount to? Probably not much. The only points ever argued by the states, have, as we have already seen,[17] been summarily rejected by the Court.

The fact unfortunately seems to be that the euphonious generalities in which the Court has bound up the industrial welfare of the American commonwealths are more beautiful for contemplation than they are efficacious in use. To discover the practical meaning which is embodied in them, and to obtain recognition of it by the courts, is one of the difficult problems which now confronts the commissions, and one in the performance of which the attitude of the judiciary up to the present time gives little encouragement.

In these three ways, then—by placing an improper limitation on the legislative power to reduce earnings through regulation of rates, by employing erroneous methods in determining the effect of rates on earnings, and by setting up inadequate standards of reasonableness in earnings—has the Court practically destroyed the state's power of rate reduction. The doctrine of judicial review is therefore of great importance in the development of the railroad problem. But, more than that, it is of significance as a notable triumph achieved by the principle of individual interest over that of the public welfare. Under whatever constitutional pressure the courts may have been in announcing the doctrine, it is felt that it is a movement against the current of the times, and that it must result, in part, in deepening the conviction already

[17] Supra, p. 106.

growing in the minds of men, that the proper balance between the public and the private interests in industrial action has been much disturbed, and should be speedily restored.

CHAPTER VI.

The Results of the Doctrine.—II.

The course of our investigation as outlined at the beginning of the last chapter now leads us to consider the effect of the doctrine of judicial review upon the ability of a commission to enforce its rates. The conclusion that will be reached is, indeed, suggested by the discussion in the last chapter, but nevertheless deserves separate statement and elucidation. It may be said, therefore, that as a consequence of the application of the doctrine of judicial review no little restraint is placed upon the enforcement of rates by public agencies. A ready mode of escape has been provided for the railroads, and one of which they have not been slow to avail themselves. The power of the state to make its rates effective has been very seriously impaired.

The reasons for this fact are two in number: first, that rates made by public authority may be immediately suspended by injunction; and second, that the suspension of rates for a few roads may and usually does permit the escape of all the other roads in the state. These statements both demand explanation, but as the second can be disposed of somewhat briefly, it will be considered first.

The effect of injunction suits brought by a few roads in a state extends far beyond the interests of those roads, for such suits are usually sufficient to settle the matter for all the other roads in the state. If a few companies secure injunctions, the others may safely ignore the rates. There are many reasons why this is so. After losing a number of cases under its rates, the commission will

hardly dare to attempt an enforcement against the remaining roads; knowing that, even should it do so, the chances are that the rates will also be held unconstitutional as to them. Moreover its inclination to bring suit for enforcement is weakened, not only by the prospect of defeat, but by the fact that the final result may be so long postponed that even should it be favorable, the commission will perhaps no longer care to enforce the rates, because of changed conditions in industry. The most powerful consideration, however, is, that public policy would no doubt forbid that a comprehensive schedule of rates designed for all or many of the roads in the state should be enforced against only a part of them. And a further fact of no little practical importance is that the commission may lack the financial means to prosecute so many suits through so many Courts.[1] For all these reasons it is evident that judicial review may permit many roads to escape the operation of a commission's rates without even submitting their cases to the courts. The tremendous significance of this fact itself furnishes the emphasis to which the fact is entitled.

But while this is clearly true, exception may perhaps be taken to the first statement,—that a commission's power of enforcing rates is impaired by judicial review because rates may be immediately suspended by injunction. To this it may be objected with apparent justice that the courts will not suspend any and every rate submitted to them, but that only such rates as, after judicial

[1] "The trial of the St. Paul case so completely occupied the time of the commission and their attorneys, and exhausted the meagre appropriation for the expense of litigation it has been impossible to proceed with the cases of other railroad companies. . . . The funds appropriated for litigation expenses, together with about $1,561.27 which had been provided from private sources, had been expended in the trial of the St. Paul case." Report of Railroad Commissioners of South Dakota for 1898, pp. 18, 19.

inquiry, are found to be unreasonable will be subjected to equitable restraint. And it may be added with still greater show of justice, the unreasonable rates *ought* to be suspended.

This is a contention which on its face seems plausible enough, but which is nevertheless not sound. The discussion of the last chapter in part discloses its weakness. Manifestly the force of the contention must depend upon the meaning given to the word "unreasonable." If it is true that the judicial standards and tests of reasonableness are proper and adequate then it follows that the suspension of rates is wholly justifiable. But if, on the other hand, those standards and tests are erroneous, then it follows that the suspension of rates may sometimes be wrong, and may be an unjust restraint upon the power of the state.

Now *are* the judicial standards and tests of reasonableness wholly commendable? We have tried to show in the preceding chapter that they are not. The Supreme Court has read into the Fourteenth Amendment a meaning which has resulted in an improper limitation being placed on the reduction of rates by a state,—in the requirement that rates must always yield a reasonable income. But even if it be conceded that the limitation is entirely fair and just, the fact still remains that rates which keep within the limit are not always enforced, but that, on the contrary, many of them may be declared invalid and may be suspended by the courts. This fact, of course, results from the methods and principles laid down by the Supreme Court for use in rate cases. We have seen that the methods of the Court are such that it must always determine that the effect of rates on earnings will be much more disastrous than will in fact be the case. Thus many rates may be suspended which are really calculated to yield all the revenue required by the

Court. Such rates a commission cannot enforce. But, moreover, we have also seen that the principles upon which reasonableness of income is determined are such as unduly to favor the railroad and give no adequate expression to the public interest. Thus, under the doctrine of judicial review, many other rates may be suspended which, while not yielding all of the earnings demanded by the Court, are nevertheless calculated to afford what should *properly* be regarded as a reasonable income to the railroad companies. Such rates, also, a commission cannot enforce.

But this is not all. We may go farther and say that not only may inherently " reasonable " rates be suspended because of the inadequate methods of the courts, but that many rates which conform perfectly to judicial standards may also be suspended. This somewhat startling statement is explained by the familiar fact that the courts regularly issue temporary injunctions in rate cases on a merely prima facia showing—that is, without being convinced or, indeed, without having evidence to convince them, that the rates ought to be declared invalid.

It is not proposed to suggest a sweeping condemnation of the temporary injunction. Its use, in general, is undoubtedly desirable. It serves to preserve intact the rights of the parties to a suit until a complete investigation can be made. All that is contended here is that there are sufficient reasons why the use of the temporary injunction in rate cases cannot be approved. At least three such reasons suggest themselves.

1. The temporary injunction is inappropriate in rate cases because rates made by public authority are acts of legislation. They are statutes, whether made by the legislature or by a commission under a delegated legislative power. But it is a fundamental rule of Constitutional Law that all statutes are presumed to be constitu-

tional, and will be so held until the contrary is shown beyond all reasonable doubt. "To be in doubt is to be resolved, and the resolution must support the law." [2] That this rule applies to railroad rates there can be no doubt, for the fact has been repeatedly declared by the Court. Yet one cannot fail to observe the inconsistency between this rule and the use of the temporary injunction. In one breath the Court declares that the unconstitutionality of rates should not be determined in a *prima facie* case; yet in the next breath it decrees a writ of injunction, involving the determination of their constitutionality upon a merely *prima facie* showing. The judge has not a "clear and strong conviction" of their invalidity. On the contrary he does not know whether the rates are constitutional or not, for a merely *prima facie* showing has been made. He is *always* "in doubt"; otherwise he would decree a perpetual rather than a temporary injunction. But being in doubt, he ought to be resolved that the rates are valid; and therefore he ought to refuse to issue a restraining order until the case has been fully tried and his doubt is removed. The use of the temporary injunction, then, is in direct conflict with the fundamental rule of law which is designed to guard the deliberate judgment of the legislature from ill-considered interference by the judiciary.

2. A second reason for believing that the temporary injunction cannot properly be granted in rate cases is to be found is the nature of the interests involved. A rate case in a controversy between the public and a corporation chartered for a public purpose. It is true that in such a case the railroad may be threatened with injury for which there is no adequate remedy at law—a situation which ordinarily furnishes ground for equitable interference. But with this fact should also be weighed

[2] Cooley: Const. Law, 3rd Ed., p. 172.

the important consideration that the railroad is a *quasi* public concern, and that because of that fact it owes to the public certain duties which the public is entitled to exact of it. The case is different from most of the instances in which injunctions are sought, the significant characteristic being the public nature of the obligation owed by the railroad. Is not this a characteristic which should control a court in the exercise of its equity jurisdiction? Even admitting that the granting of a perpetual injunction after full hearing is a proper method of procedure, it is hard to agree that public control of a *quasi* public corporation should be thwarted by a writ issued upon only probable cause. Is the public interest in railroads so slight that it should be defeated by a merely *prima facie* showing? Or, to put the converse, is the private interest of the railroad company so great that a merely probable case is sufficient to exempt it from public control?

3. A third reason for condemning the use of temporary injunctions in rate cases is the fact that when the courts have once recognized that the company is entitled to relief from the rates until a final hearing has been had, the "temporary" suspension of rates becomes for all practical purposes permanent. For after the suit has been disposed of in the trial court, at least one court of appeal remains, and in that the temporary injunction may be continued. An apt illustration of the abiding nature of the temporary may be found in the case of Chicago, Milwaukee, and St. Paul Ry. Co. v. Tompkins,[3] the history of which is as follows:

On August 26, 1897, the South Dakota Railroad Commission promulgated a schedule of rates to take effect on September 15, 1897. The day after the announcement of the rates several companies brought suit in the United

[3] 176 U. S. 167.

States Circuit Court, and secured an order, returnable on September 6, to show cause why a temporary injunction should not be granted. The Commission appeared and resisted the application, but the injunction was nevertheless granted. On July 7, 1898, the court decided the case in favor of the Commission and refused to issue a perpetual injunction. But the St. Paul road promptly perfected an appeal to the Supreme Court, *which immediately ordered the temporary injunction continued pending the final decision of the case.* In other words, the original presumption that the rates were valid, supported, as it was, by the decision of the circuit court affirming their validity, was not enough to save them from " temporary" suspension by the Supreme Court. About two years later the latter court remanded the case with instructions —the rates being still " temporarily " suspended,—and at last in August, 1901, the trial court rendered the final decree.[4] Thus had the rates been " temporarily " suspended for almost four years.

The lesson of this case need hardly be suggested. The theory that a *prima facie* showing is sufficient to warrant a temporary injunction, coupled with the theory that a railroad company may make such showing even against the decision of a trial court as well as the inherent presumption that rates are valid, practically annihilates all possibility of rate enforcement. For a rate to be suspended for four years—it matters not that the suspension is "temporary"—is to destroy practically all possibility of its usefulness. In these days of changing industrial conditions it is seldom true that rates made to suit the needs of the times four years ago are applicable to conditions of to-day.

But this is not all that may be said as to the power of a

[4] C. M. and St. P. Ry. Co. v. Smith, 110 Fed. Rep. 473. The final decision was in favor of the railroad. See Supra, p. 112, footnote.

commission to enforce its rates. Not only *may* the railroads secure the suspension, "temporary," if not permanent, of practically every rate at all inimical to their interests:[5]—under the practice of judicial review they are much encouraged and strongly tempted to contest such rates in court. The reason for this incentive to seek judicial shelter are numerous, but only a few can be mentioned.

In the first place it is obvious that they are impelled to litigation through a realization of the fact that their chances of success are excellent. As we have seen, it is easy for a railroad to establish its case; it is difficult for a state to establish its case. For the former has the significant advantages of a tribunal which is professionally sympathetic to it, of the protection of a Constitutional provision which has been interpreted as fixing a close limit to state action, and of principles and methods used in the interpretation and enforcement of that provision which are exceedingly favorable to the corporate interests. And no one knows so well as the railroad counsel, how favorable those methods and principles are to them. Added to the probability of ultimate success, however, is the fact that "temporary" relief can be secured in the case of practically any rates which the companies would care to contest, and that this temporary relief may be extended over a considerable period of time. All that a company has to do (practically speaking) is to keep a case in the courts, in order to be legally exempt from the rates.

Another motive impelling a railroad to bring suit is to be found in the fact that the suit may operate to force a compromise. Fearing the outcome of the action, and

[5] An exception to this statement may, under the Minneapolis and St. Louis Case, be found in the instance of special rates made for isolated commodities. As to general schedules it holds true.

the ultimate failure of all its work, a commission may be induced by a suit or even the threat of a suit to propose or accept an increase in its rates. But compromised rates are never thoroughly satisfactory to any one but the railroad: they are satisfactory to the road, for otherwise it would reject the compromise and carry the case through; but they cannot be wholly satisfactory to the rest of the community, for, being compromised they cannot be specially adapted to the public needs. This evil is all too common, and seriously impairs a commission's power to enforce its rates.

Still another motive which may inspire a road to sue for an injunction, is that one result of a suit must be to tie the commission's hands so long as the case is in the courts. Let a commission promulgate a schedule of rates,—the road, by simply taking a case through the courts, practically prevents the board from taking any other action as to rates during the three or four or five years in which the case is dragging from one tribunal to another. It means just so many years of immunity from public regulation.

A final reason which impels a road to resort to judicial adjudication of the rates, is a desire to reap the advantages which come with a triumph over the commission. The very facts that the courts stand ready to test the reasonableness of a commission's rates, opens to the railroads a means of discouraging the commission and perhaps of bringing it into disrepute. Of course, no commission establishes rates without allowing the railroads a full opportunity to be heard and to introduce evidence. Often the rates are fixed as the result of a complaint brought by some shipper or locality and in such cases the roads are summoned to appear in answer to the complaint. The roads realize, however, that if the commission's ruling goes against them, they have recourse to the courts; they

know, moreover, that the courts are favorably disposed to them—much more so than the commission. Accordingly it is to their interests to have the case tried by the courts rather than the commission. They therefore have a strong motive for making only a perfunctory showing before the commission, concealing the real strength of their case. When the commission rules against them, however, and they appeal to a court, they open their case with full force, and make their best showing. The public's case is an old story to them, for it has come out very fully in the proceedings before the commission, and they have had time to work up a defense to it. Their own case, however, is new to the public officers. For this as well as other reasons the suit goes in their favor, the injunction is granted, and the commission is defeated,—perhaps discouraged, and discredited. It may be that, had the commission been in possession of all the evidence introduced in court, it would never have made the rates which it did. But, in any case, so much has it been hindered and crippled by the right of judicial review.

But it may be said in reply that the temptation to bring suit must always be weakened by the consideration that indiscriminate litigation must result in occasional defeats for the railroads, which will tend to arouse popular feeling and create a prejudice in the courts against the railroads. Unfortunately there seems to be little strength in this contention. From what has already been said it is evident that defeats for the roads must be very occasional. But even should they be fairly frequent it is hardly probable that the roads would be damaged by such prejudice as would be aroused. So far as the public is concerned probably the only feeling would be one of gratification at the defeat of the railroads. And so far as the judiciary is concerned, it cannot be imagined that our federal judges could be turned by feeling or prejudice from the path of legal justice.

Judicial review has, then, practically destroyed a commission's power to enforce its rates, both because of the incentive given to the railroads to contest the rates and because of the treatment accorded them in the courts. Do serious consequences flow from this loss of power? Inevitably so. Some of them deserve special mention.

1. One consequence is that a commission cannot adapt its rates to changing industrial conditions. This, of course, in itself would be well-nigh fatal to its efficiency. Our modern industrial community is far from static; conditions change from time to time, sometimes gradually, sometimes suddenly. And since transportation is a factor lying at the very basis of all other industry, it follows that transportation rates should be adjusted to meet the needs of business. It was chiefly for this reason that the policy of legislative rates was early abandoned. It was found that a schedule of rates made by a legislature would, at many points, get out of accord with industrial conditions before its next session, after a lapse, in most states, of two years. Accordingly the making of rates was delegated to a commission which, being in continual session, could make such prompt adjustments in rates as might appear to be necessary. But the doctrine of judicial review has rendered the expedient futile. A commission may make rates, it is true, but the *immediate* enforcement of them, which is a prime desideratum in public control, is an impossibility. At least temporary suspension is practically inevitable, whether the rates are fair or not, and we have learned what "temporary" means. Thus does judicial review prevent a commission from fulfilling a supremely important object of its existence.

2. Another consequence of a commission's inability to enforce its rates is that the evil of instability in rates is enhanced. We have already had occasion to mention this

evil.[6] and to say that the public welfare demands that railroad rates should be stable, except when they are *bona fide* altered to meet changing industrial conditions. It might seem that public control of railroads, and especially control through a regulative commission, would offer exemption from unstable rates. And indeed there can be no doubt that commissions, if able to enforce their rates, could in a reasonably satisfactory manner accomplish this object. But if conditions were bad when roads could make and unmake rates at their pleasure, they are worse in a system of public control which struggles under the burden of judicial review, where, in the main, the railroads still fix the rates, but where the intervention of a commission occasionally works changes, and where, moreover, the commission's rates may be carried to the courts and made the subject of almost endless litigation, —leaving both carrier and shipper in doubt as to their legality. Nor should it be forgotten that during the long period of litigation, the railroads are practically free to manipulate rates at their pleasure. Thus is the situation complicated and the evil of instability rendered greater than it would be had no commissions ever been appointed, and such is the way in which judicial review has affected the power of a commission to discharge this important phase of its duty.

3. In the third place, as a consequence of the loss of power both to reduce and to enforce rates, the commissions have become unable to make rates on the principle of public utility. The railroad rate problem is more than a mere matter of the correction of specific abuses. Such work is valuable, of course, but it touches merely on the borders of the problem. The heart of the matter is the promotion of the public welfare by such a regulation of

[6] Supra, p. 9.

rates as will provide the conditions for a healthy and vigorous and well-proportioned industrial life. Rates should be adjusted among commodities and among localities with reference to sources of raw materials, centers of manufacturing, location of markets, and so forth, the aim being to produce the highest degree of industrial well-being. Railroad rate-making offers a powerful engine for the public good, and the rate problem will not be solved until that engine is used to its best advantage. But it is painfully evident that the commissions, limited and restrained as the now are, find themselves utterly unable even to approach this broader and more significant phase of the problem set before them. And herein do we find one of the most melancholy consequences of judicial review.

We have now considered the effect of the doctrine of judicial review upon a commission's power to reduce rates and its power to enforce its rates. It will serve to illumine and enforce the conclusions which have been reached, to quote from a letter received by the author from one of the youngest and most vigorous of the state commissions:

"In answer to your question, 'To what extent and in what way, has this power of judicial review been a source of embarrassment to you, as railroad commissioners, in the exercise of your power to fix rates?' beg to say that this power to review the rates made by a railroad commission, assumed by the Courts, has been the source of some embarrassment to this Commission, as it has to almost all State Commissions. In the the State Courts we have had to compromise two suits, rather than allow them to go to trial, fearing the final decision of the Court would be delayed to such an extent as to render the order fixing rates useless, or else fearful of a perpetual injunction's being granted, estopping this Commission from future action. . . . Unquestionably, the effect of such decisions makes a Railroad Commission extremely cautious as to

the rates which it establishes, and certainly is a barrier in the way of their making many rates which in their minds are reasonable, just, and necessary. I may say, however, that with the exceptions noted, this Commission has been remarkably free from litigation over its orders, and has not suffered to a great extent from Court decisions. The suggested trend of the decisions has, though, put the Commission on its guard, thus rendering its work less efficient than it might be, were these apparent difficulties of judicial interference removed."

But what now, to proceed to the last step in our inquiry, has been the consequence of this deprivation of power both to make and enforce rates, upon the attitude of the commissions toward the problems which have been given to them to solve? What has been the effect of judicial review upon the spirit and ideas of the commissions? While it cannot be said of all of the state commissions, as to a large majority of them it is a fact that the gradual growth of the doctrine of judicial review. and the gradual development of the methods employed by the courts, have gradually paralyzed the commissions by destroying their will as well as their power. Under the burden of judicial review the commissions have become discouraged from the task of rate regulation; most of them pay relatively slight attention to the matter of rates, confining themselves largely to the other and much less important duties imposed upon them. Some have practically desisted from rate making. Some esteem their duty done when they attempt to arbitrate the few cases, between carrier and shipper, which are brought to their attention, but which form only a microscopical part of the great question of rates. This relaxation of effect, this growing indifference to the most important of all their functions, has been conspicuous in recent years.[7] and

[7] Though somewhat less so within the last year or two, since President Roosevelt began to rekindle popular interest in the rate problem.

is a discouraging feature of the railroad problem of to-day.

But a far more disheartening fact is that some commissions have come to the point where, forgetting the real nature and the real necessities of public control, they consciously or unconsciously adopt the theories of the courts. Respect for the law as pronounced by the courts, aided by the presence of an excessive number of lawyers upon the Commissions has no doubt gone far to accelerate the growth of the conviction that, after all, the principles and methods of the courts must be just and wise and beneficent. How far that is true we may judge from the discussion in this and the preceding chapter. But the result of this conviction has been that insofar as such commissions attempt to fix rates at all, they for the most part adapt them for review by the courts. Some of them say they welcome review by the courts, believing that such review is salutary, and that they would not wish to enforce a rate which, according to judicial standards, is unjust. Thus they make their rates according to judicial methods, practically ignoring the real public interests involved, making no effort to remedy the serious difficulties of their situation, and all this they do with the impression, more or less sincere, that it is right.

Of no commissions does this seem to be so true as of the older ones. Said one of these in writing to the author:

"It is provided by law that the rates promulgated by this Board are only *prima facie* evidence in the courts of this state as to what reasonable rates should be. The Board has not felt that this provision of law has been a hardship upon the shippers of the state, but rather a safeguard preventing unreasonable exercise of the rate making power. The Commissioners have never had any hesitancy in fixing a rate which they believed reasonable, and since the great cases of 1888 and 1889 there have

been no contests in this state involving the reasonableness of the Commission's schedule or amendments made thereto from time to time. Of course, future events may change the opinions expressed in this matter, but from the experience of this Board up to the present time, the Commissioners could hardly suggest any change in the conditions in this state that would be more equitable and just to all interests involved."

A more astonishing statement, however, was received from a commission which a number of years ago was most vigorously contesting the doctrine of judicial review. One sentence of its letter reads:

"This Commission rather invites a review of their work by the Courts, and we do not feel that it in any way embarrasses us or causes us to hesitate in making an order fixing what we deem to be reasonable rates."

And the closing sentence of the letter is almost pathetic in its ingenuousness:

"The length of time required to get a final decision in matters of this kind is the only feature of the law that causes any embarrassment."

Thus has judicial review not only fettered the hands of the commission: it has tended to destroy their will as well. It has, moreover, in many quarters corrupted the very idea of public control, perverting the views and distorting the vision of those upon whose soundness of judgment and keenness of insight the public is relying for its protection and welfare.

It is desired, in concluding this branch of the subject, to make a practical application of the general ideas involved in judicial review to the attitude which railroad companies habitually assume toward proposals for rate control. All movements in Congress to endow the Interstate Commerce Commission with power to regulate rates have been vigorously resisted by the railroad lobby, which has never been more strenuous in its opposition than it is at the present time. So also the introduction

of a bill providing for rate control in any state legislature —as in Wiscinsin during the recent legislative session— has always been a signal for sturdy and stubborn resistance on the part of the companies. Now how is this conduct to be explained? In view of the guarantee which judicial review offers the railroads, that rates must always yield a reasonable income, and especially in view of the definition which the courts have given to the term reasonable, and of the judicial methods employed in rate cases— a definition and methods exceedingly favorable to the corporate interests—what possible interpretation can be placed on the railroads' conduct except this: that it is a confession that rates are now unreasonably high—unreasonably high even according to judicial standards of reasonableness—and that, moreover, the companies desire to maintain them where they are? What else can explain the determined opposition of the roads? If rates are now reasonable, and if the railroads intend to maintain them on a reasonable basis, surely they have nothing to fear from governmental regulation. If their schedules are fair, even according to the liberal theories of the courts, the government cannot touch them. Why, then, this resistance?

It may, indeed, be pointed out that the corporate opposition is always directed with special force against a provision often inserted in rate laws to the effect that the rates shall be in full force and effect pending a review by the courts. Under such a provision, it may be claimed the roads, even if they could ultimately prove the unreasonableness of the commission's rates, would have to suffer the loss due to operating the rates while the suit was in the courts. But the discussion offered above shows clearly enough that there is no force in this contention The railroads have nothing to fear from a statutory provision of this sort. For in rate cases they repose on their

constitutional rights, and to these rights statutes must always yield. Under the Constitution their property cannot be taken by the public without just compensation; consequently rates so low as to deprive of property are, in the absence of compensation, invalid. But now the courts have held that a railroad is entitled to immediate relief, by injunction, from rates which seem calculated to deprive of property, for,—such is the judicial argument—were it to be compelled to operate the rates pending judicial investigation, it would have no adequate remedy at law for the injury it had suffered, should the rates finally be found to be unreasonably low. Beyond a doubt the right of the road to equitable relief is fully established. For a legislature, therefore, to enact that rates shall be in force until found invalid by the courts, is an attempt to deprive the railroad of its constitutional right, and such an enactment must consequently be unconstitutional. If the only effective means of enforcing a constitutional right is through a suit for immediate suspension of rates. a statute forbidding immediate suspension must certainly be a denial of the right, and hence must be repugnant to the Constitution. Accordingly the federal courts have never hesitated to grant injunctions even when the state statutes provided that rates should be effective pending judicial review, and there is no reason to doubt that the same policy would be pursued in regard to federal legislation, should occasion arise. Under the law as it now stands, therefore, the railroads have no reason to fear a Congressional enactment of the kind under discussion.

From all of which we conclude that under the doctrine of judicial review a railroad cannot be compelled to operate, either temporarily or permanently, a rate which does not conform to judicial standards of fairness, standards which, we repeat, tend decidedly to the advantage of the railroads as against the public. What else, then, can

railroad opposition to the creation of rate-making commissions mean, other than an admission of a desire to charge unreasonably high rates, or a denial of the obligations which railroads owe to the public?

CHAPTER VII.

REMEDIES.

Our study so far has attempted to disclose the nature of judicial review, and its effect upon the efficiency of railroad rate control. It remains now to inquire what means may be suggested to overcome the difficulties which the doctrine has raised. Those difficulties, as has been shown, are chiefly two—the inability of a commission to reduce rates, and its lack of power to enforce them. Accordingly this chapter will consider three classes of expedients—those suggested to relieve both difficulties, those designed to permit greater freedom in reducing rates, and those proposed to make enforcement possible.

I. First, then, as to suggestions for correcting both of the difficulties. Perhaps the most obvious measure is a constitutional amendment. Conceivably a provision might be added to the Constitution which would affect the Fifth and Fourteenth Amendments insofar as their relation to railroad control is concerned, and this could doubtless be so framed as to restore to the legislative department of government the power which it possessed under the decision in *Munn v. Illinois*. The exact form which such an amendment should take, however, it would be fruitless to consider at the present time, for the project is without a shred of feasibility. A constitutional amendment is a modern miracle, and it would be folly to rely upon it. The suggestion may therefore be dismissed with mere mention.

It will be observed that the above plan is designed to remove from the railroad the protection of the Constitu-

tional amendments. A further plan, however, may be suggested which, while according to the roads the full benefit of the Constitution, would nevertheless obviate the difficulties interposed by judicial review. This expedient is suggested by the very nature of the Constitutional provisions. In effect, that instrument has been interpreted as providing that no railroad company can be deprived of its property without just compensation—in other words, no company can, by reduced rates, be deprived of any part of its reasonable income *unless* just compensation is made by the state. But if compensation is provided, then such deprivation may be freely made. This statement suggests the nature of a plan which, if executed, would meet with at least a fair degree of adequacy the demands of the situation. The trouble with government-made rates has not been that they have been so low as to deprive of property; the kernel of the difficulty has been, as we have already seen, that they have been imposed in the absence of any provision for compensation by the state in case they should prove destructive of property. In view of this fact the courts have brought the injunction to the relief of the railroads, holding that they should not be compelled to operate the rates and then recoup their loss through multifarious and unprofitable suits for damages against their patrons.

The difficulties, then, of judicial review would be remedied were the state (or federal) government to adopt some such plan as the following:

The Commission would, as now, be empowered to fix rates, and each railroad would be required to operate them as soon as directed by the Commission; but it would also be entitled to bring suit after an adequate period—perhaps one year—the object of the suit being to disclose whatever loss it had incurred by reason of the rates. For the purpose of trying these cases the state might well

create a special court, composed in part of lawyers, and in part of men whose experience in business or public affairs would specially qualify them for the work. If no such court were created, however, the suits should be instituted in one of the higher courts of the state, and in either instance the Commission should be made, on behalf of the state, the party defendant.

In such cases as these the object of the railroad would be the same that it is now in a suit for an injunction—to show that the rates are so low as to deprive them of a reasonable income on their business. The difference would be that, whereas the courts must now estimate the future effect of the rates on the basis of past business, under the plan suggested the actual effect of the rates for an adequate period of time would form the basis of their conclusion. Should the court decide that the railroad had not earned a reasonable income under the rates, its further duty would be two-fold:

1. To determine the exact amount of the loss which should be attributed to operating the rates in question. This sum being thus fixed, unless either party elected to appeal the case, (for, of course, the right of appeal at least to the United States Supreme Court would always exist) the railroad would be entitled to collect it from the state treasury on warrant of the proper officer of the court. Just compensation would thus be made by the state for the property which it had taken in the public interest.

2. The Court should also be required to indicate in its opinion the exact vice of the rates in question. Its judgment, of course, would not operate to suspend the rates, but its conclusions as to their defects would be of great service to the commission in determining whether any revision of the schedules would be advisable.

Before proceeding to indicate the advantages of such a plan as that just outlined, there are certain apparent objections which it would be well to consider.

(1) In the first place it may be objected that the railroads would be compelled to rely on the good faith of the state; and that, if the legislature should fail to make provision for the payment of the damages, the companies would be without means of recoupment. To this it is sufficient to reply that the good faith of a state is not contemptible security; that it is the only thing which any of a state's creditors have to rely upon; also that it would be hard to imagine a state treasury so depleted as to be unable to meet the warrants that would be presented. But a conclusive answer is that should any action be taken by the state which would preclude the payment of damages, the companies would of course be entitled to sue at once for an injunction to restrain the enforcement of the rates. There seems, therefore, to be little force in this objection.

(2). But it may be contended that the scheme here proposed would be expensive to the state. The best answer is that the state would receive a consideration in return for its money. The economic and social benefits which would result from the application to railroads of the principle of public utility would be worth buying, if they could be procured in no other way.

But, on the other hand, it is believed that the actual amount which the state would be compelled to pay in damages would be much smaller than one would at first suppose. Several considerations lend support to this conviction. In the first place, the commission, realizing that the exact effect of its rates might be disclosed to the public, and that a mistake due to too radical action would result in a drain on the state's finances, would be inclined to proceed with all due care and prudence. More important, however, is the fact that the plan we are discuss-

ing would deprive the railroads of many of those undue advantages which we have seen that they now enjoy as against the public. For example, the effect of the rates on earnings would not be determined by the court, as at present, on the basis of past business—a basis always unfair to the rates; but rather would their actual effect have been observed. Moreover the system would permit the practical application of the Court's theories concerning the rights of the public, the industrial condition of community, and so forth, theories which have for the most part found expression only in obiter dicta. The Court would not have to rely upon conjecture, but could observe the actual effect of the rates on the public welfare and in relation to industrial conditions. Thus a stronger case could be made out for the state than is possible under the present system. And, finally, since the railroads have to make their case on the basis of facts, it would be comparatively easy to detect the existence of doubt in their allegations, and doubt would have to be resolved in favor of the rates. There would be no suspension of rates by temporary injunctions, on the presentation of a merely probable case. Such are some of the more important reasons for the belief that the suggested plan would not prove expensive to the state in a very serious degree.

(3). But it might be urged that under the proposed system it would be possible for a road for which a low rate was prescribed to throw traffic temporarily to a higher rate line, thus showing smaller earnings and, apparently, substantial injury as a result of the rates, entitling it to compensation by the state. This objection, however, is not a serious one, and for many reasons. First of all, it is to be presumed that in many cases a Commission would make the same rate for all roads performing the same service, so that all would have an equally strong motive to get rid of traffic. But even should the commission's

rate not apply to all competing lines, or should different rates be fixed by the commission for different lines, such practices as are here suggested could be discouraged by being penalized, if that seemed necessary. Certainly they would be regarded by the Court as sufficient cause for the diminution of damages claimed by the road, and the loss of traffic by a low rate road with corresponding gain by a high rate road would properly be taken as evidence of the practice. But would the motive to throw over traffic be strong in any case? It is believed not. For if the process were accompanied by a secret agreement whereby the receiving road should pay a bonus on such traffic, the amount so paid would have to appear among the receipts on the other company's books some time or other, and it is not likely that the latter would be content to wait for it until the termination of its suit. Moreover, such a contract could be made void and unenforceable at law. But it is not probable that such a secret agreement would be omitted from the deal between the roads, for certainly no company would esteem that it had anything to gain by substituting for the immediate certainty of receipts from traffic the uncertainty of damages. which, if secured at all, could be gained only by a suit at law. All points considered, it is hard to see that the effectiveness of the proposed plan would be in any measure frustrated by any such attempted evasion. It is highly improbable that even a penal provision would prove necessary.

(4). Finally it might be claimed that it would be unjust to compel the companies to wait so long for their compensation. This, however, cannot be admitted. Certainly, if the state goes so far as to concede a right to compensation, the least which it can expect of the company is that it shall wait until that right can be established, and that then, like all other persons to whom a

right of action has accrued, shall be content to await the outcome of legal proceedings.

So far we have confined our discussion to objections which might conceivably be offered to the plan we have proposed. What now may be said of its advantages?

Obviously its chief merit is that it meets one of the important requirements of the situation. It is a plan which enables the state to prescribe rates made upon the principle of public utility. The commission is not embarrassed by the necessity of considering the effect of its rates upon railroad earnings. It can proceed with an eye single to the general welfare of the community, knowing that for any real financial injury suffered as a consequence of the rates the roads find satisfaction in the state treasury. Further it is a plan whereby rates may be made immediately effective. The adequate provision made for compensation for all loss removes the case from the equitable jurisdiction of the courts, and abolishes the injunction as a remedy for the roads, which can therefore have no legal excuse for not operating the rates at the time fixed by the commission. The delays in enforcing the rates, which go so far toward destroying the efficiency of the present system, would be unknown.

Another advantage of the proposed plan, and one of great practical importance. is that it is thoroughly in harmony with the Constitution as at present interpreted. in that it provides compensation for whatever property is taken by the state. In the minds of many this respect for private rights would, as a matter of theory also, form a commendable feature. Those who believe that owners of property devoted to a public use should receive compensation for loss through public regulation of that use could find no offence in railroad control under this system. The demands of the most radical advocate of private rights are fully met.

Other benefits of this plan have already been touched upon in considering possible objections to it. Suits brought by the roads would not, as now, throw upon the courts the necessity of estimating the future effects of the rates. Rather would the courts have as a basis for their decision the actual results of a year or so of application of the rates. No more artificial and inadequate methods and principles would be needed. And no longer would the numerous expressions of the courts as to limitations upon the rights of the companies remain simply *obiter dicta,* for often the facts could be found which would make their application possible.

Would not such a system require commissions of a very high grade of ability? Most assuredly. Of course it is too much to hope that in all states competent commissioners would at once be found. But it is believed that the serious responsibility resting upon the boards would by a process of selection speedily produce such an elevation in the competence of their membership as, in itself, would be a most auspicious event.

But while this plan has much in it that is worthy of commendation, it is, after all, but a make-shift. It recognizes that an erroneous doctrine of judicial review exists, and simply resolves to make the best of a bad matter. It would be far better, of course, to have that doctrine thoroughly revised and reformed, but until that is done, such a plan as the above is worthy of consideration.

Possibly one other suggestion should be made before leaving those measures designed to remedy both of the evils of judicial review. It is probable that the legalization of pooling and of the consolidation of parallel lines would relieve the situation to an appreciable extent. Doubtless one of the reasons why the roads now resist public control so strenuously is, that the intense competi-

tion which the law compels them to maintain forces them to discriminate, that is, to accept in many cases a rate lower than the public schedule. A law, however, giving to pooling contracts a legal status, and permitting parallel roads to consolidate, would tend to do away with competition and hence with discriminations, and would enable each company to charge in all cases the public rates. With this advantage—to the roads as well as to the public one of great value—the companies would in all probability receive in a better spirit the public efforts at control of rates, and it is not too much to believe that contests as to their validity would be somewhat less frequent.

II. We are next to consider such measures as may be proposed to restore to the commissions a power to reduce rates. Undoubtedly most of what can be done along this line must come as a result of renewed and energetic action on the part of the commissions. The existing situation behooves them to urge constantly upon the courts the injustice of the present judicial doctrine,—its fundamental error in subjecting rate control to the principles of eminent domain; but more especially the inadequacy of its methods, for example, its methods in finding the earning power of a company under the legislative rates. But beyond this a wide field for their activity is to be found in the numerous "circumstances and conditions" which the Supreme Court has recognized as important in determining reasonableness of income.[8] These

[8] Supra, p. 72.

dicta, pronounced by the Court during the last ten years, have opened the way for many new departures; and the duty now rests on the commissions to compel the Court to apply, or at least more accurately to define its theories. That the commissions have not thus far seemed to see this duty is unfortunately true. Perhaps the chief reason

is that for several years—we may say, generally speaking, until after the Smyth case—the commissions were fighting the theory of judicial review itself. They were trying to uphold their right to be exempt from judicial restraint. And when at last the courts positively asserted their right to pass upon rates, the battle seemed lost. Since then a chronic despondency on the one hand, or a too willing acceptance of their fate on the other, has kept the commissions from discovering and utilizing the germs of opportunity contained in the opinions of the courts.

To illustrate: the commissions might call up the dicta, restricting the right of the companies to profitable rates, which pertain to the management of the roads; in some cases they might show definitely wherein the management had not been prudent or honest, and wherein the companies had been guilty of unjust discrimination. They might show that there had been needless expenditure in the construction of the road, and so forth. So also they might take up the dicta regarding the rights of the public and try to make something tangible of them, putting their cases as fairly and as concretely as possible, especially endeavoring to show that competition of other lines had so reduced business that a profitable rate would be unjust to the public. Again they might strive to prove that certain roads were built unwisely, where they were not warranted by business conditions; or they might offer definite evidence to show that the industrial condition of the community demanded the rates in question.

It was noted, in discussing these dicta, that the courts were most hesitant to apply them, and that in the few cases where they have formed a part of the state's contention, the Supreme Court has refused to apply them. It must be admitted, however, that few of the dicta have ever been urged with great force, nor have the contentions

based upon them been often supported by perfectly adequate evidence. By itself, however, in the absence of evidence, a court can do nothing about them; unless facts are presented as a basis upon which to proceed, it cannot make a concrete application of them. Unless the commissions realize this fact, and act accordingly, all the dicta must forever remain simply dicta. But if the commissions care to undertake the confessedly difficult task of establishing a connection between these dicta and facts which will make good evidence, it is not unlikely that in time the doctrine of judicial review will be still further refined by a new body of rules and principles which will offer some firm foothold to the agencies of public regulation.

Beyond these mere obiter dicta, however, further opportunities present themselves to the commissions. Under a recent decision of the Supreme Court,[9] it is possible for a commission from time to time to re-adjust the rates on single commodities. Though such re-adjustment might involve a considerable reduction in those particular rates, it would be hard for a railroad to prove their invalidity, for the Court has held that a road is not entitled to the same rate of profit on all commodities, and, further, that it is not a sound complaint to say that if the same reduction were made in the rates on all articles, the company could not secure reasonable income. This decision enables a commission, therefore, to effect a gradual revision of schedules, by dealing with single articles, or a few articles only, at any one time.

A somewhat similar opportunity is presented by the decision in the Gill case, where it was held that rates would not be suspended when the company could show, as a consequence of them, a loss upon only a part of its road. Under this rule, a commission might make re-

[9] Minneapolis and St. Louis R. Co. v. Minnesota, 186 U. S. 257.

ductions affecting all commodities, but only on such a portion of the road that it would be impossible for the company to show a general loss on all its local operations

Now, it is, of course, admitted that the utility of these two expedients could not well be as great as would at first appear. They offer a means for but lame and halting progress in public control. A commission would not always wish to make all the re-adjustments possible under these two decisions, for such action might not be at all in accord with the principle of public utility. That is to say, considerations of the general welfare might, and in many cases would forbid that rates be lowered on certain commodities, or between certain points, while rates on other commodities and between other points remained unchanged. This is evident, and therefore it is apparent that the two measures just suggested would have to be employed with rare prudence and discrimination. They could never lead to a full expression of the principle of public utility, nor could they ever produce entirely satisfactory conditions in the railroad industry. But as occasional expedients, in special cases, they might surely prove of use to the commissions.

III. We come finally to a consideration of remedies for the present inability of a commission to enforce its rates. Perhaps the first thought which occurs in this connection is that immediate enforcement of rates might be made possible through an act of Congress regulating the procedure of the federal courts in rate cases in such a manner as to prevent the issue of injunctions. At the close of the last chapter, however, we indicated our conviction that such a statute would be held unconstitutional. For equitable relief is now granted because it is held to be the only adequate remedy which the roads would possess—the only effective means of maintaining their constitutional rights. Therefore an act which deprived

them of this means would, in all probability, be construed as denying the constitutional protection to the roads, and would consequently be declared void. It is practically certain, therefore, that this suggestion would not be fruitful of good. If an act were to be passed forbidding the temporary injunction only, as has recently been proposed by Senator Bailey in the United States Senate, there would perhaps be some possibility of its validity, but even that is very doubtful.

Another plan, not, indeed, to secure prompt enforcement of rates, but to remedy the evils resulting from non-enforcement has been repeatedly suggested and has been adopted in a few states. It gives to the company the privilege of refusing to operate the commission's rates, but requires that it file with some public officer a bond to secure the repayment to each shipper of the difference between the rates charged and the commission's rate, should the latter be finally held to be valid. The objection to this scheme is to be found in the long period of time required to get a final ruling—a period as long, frequently, as four or five years. This is time enough for the company's rates to do damage which an ultimate repayment of overcharge could never repair. A business ruined is not restored by the mere transfer of a sum of money.

State statutes have frequently provided for a speedy trial of such rate cases as may be brought in state courts. Rate cases are given precedence over others, except, usually, criminal cases, and the procedure is directed to be of an expeditious and summary character. Such provisions regarding the trial of cases in the federal courts would do something toward securing more speedy enforcement of rates. So also would the creation of a special commerce court, such as has recently been proposed in Congress, and elsewhere. Even under the most favorable

circumstances, however, it must be admitted that the trial of a case would drag behind the march of industrial events. Such proposals as these must be looked upon as remedies which are simply partial, and leave much else to be done.

One final suggestion is offered. The difficulties presented by the doctrine of judicial review might be in part avoided were the schedules imposed by the state to err more on the side of conservatism than of radicalism. Much has been lost in the past through too sweeping changes, too great reductions in rates. An effort has been made to reach the goal at one bound, the state not being content to patiently work out, through a period of years, what it considered a fair standard of charges. The Nebraska Maximum Rate Law, overthrown in *Smyth v. Ames,* furnishes an apt illustration. The Court determined that the statute lowered existing rates by twenty-nine and one-half per cent., and this, it must be admitted, was a large reduction to be made at one time. It will be recalled that seven roads were involved, each making a showing for three years. Now, from the figures given in the opinion of the Court it may easily be computed that had the statute reduced existing rates only thirteen and one-half per cent., a very different result might have been reached by the Court. For in that event according to the methods of the Court, in sixteen out of the twenty-one cases the rates would have made possible the payment of expenses. One road would, indeed, have showed a loss for each of the three years, and two others a loss for one year apiece; but in the sixteen cases the average excess of percentage of receipts over percentage of expenses would have been a fraction over eleven. Thus in regard to at least six of the roads that statute would have had more than a fighting chance, and might possibly have been upheld.

These facts illustrate the proposition that more can be gained by moderate reduction, which the railroads would hardly venture to contest or would be defeated in contesting, than by sweeping changes which are almost sure to meet with judicial condemnation. It is true that such conservative action postpones the day when, if ever, the ideal basis of rates can be established, but it accomplishes something instead of nothing. It means victory for the state, instead of defeat.

It is obvious from what has been said that the problem raised by the doctrine of judicial review demands for its solution patient, wise, and energetic conduct on the part of the commissions, and thoughtful consideration on the part of the public. Upon the commission rests the responsibility and duty of seizing the opportunities which, as suggested above, have been offered by the dicta and rulings of the Supreme Court. This duty should be discharged and would beyond a doubt be productive of much good, though, of course, it could never furnish a satisfactory solution of the problem. After all, some more sweeping reform is needed. Doubtless the thing most to be desired is a revision of the judicial doctrine by the courts, restoring to the legislative department of government its full and proper authority. In the absence of this highly improbable reform, however, some other expedient is necessary to meet the demands of the situation. The plan of compensation, suggested in this chapter, would perhaps meet them in a more thorough and generally satisfactory way than any other. While complying with the requirements of the Constitution as interpreted by the Supreme Court, and satisfying fully the most extravagant claims of private rights as against the public, it would nevertheless give to the commission the opportunity of adopting public utility as the controlling principle in rate making, and of giving efficient expres-

sion to that principle; and this is the ideal of railroad control. Industrial well-being can never be a reality so long as railroads are operated on the commercial principle of private advantage; nor is it attainable under our present conglomerate system where that principle still controls, though modified in some particulars. It can be achieved only when the realization that the railroad industry is a public business of fundamental importance to society, shall lead to the definite adoption of the principle of public utility as the guiding and controlling influence in railroad management. State ownership would make this possible, but state ownership has very many serious objections. With a system of private management it will be possible only when the problem of judicial review is solved. Under such circumstances, it is easy to perceive the significance of the plan which this work proposes, or of any other which can more readily accomplish the desired end.

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