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THE HOPE NATURAL GAS CASE AND ITS IMPACT ON STATE UTILITY REGULATION

In the recent case of Federal Power Commission et al. v. Hope Natural Gas Co.,¹ the Federal Power Commission, acting under the Natural Gas Act of 1938, after a full hearing upon complaint of several wholesale customers, ordered the Hope Natural Gas Company to cut its rates for natural gas sold in interstate commerce so as to reduce its operating revenues by $3,609,857, or about 20% (or more than 60% of its net income). In doing this, the Commission figured that the Company would still have a return of 6½% or better on a rate base of $33,712,526, the "'actual legitimate cost' of the Company's interstate property less depletion and depreciation and plus unoperated acreage, working capital and future net capital additions." The Company had submitted evidence from which it estimated reproduction cost at $97,000,000 and a so-called "original cost" which exceeded $105,000,000 (based on 1938 material and labor prices). Allowing for an accrued depreciation of about 35% of reproduction cost, the Company claimed a rate base of $66,000,000 and asked for an 8% rate of return. The Company's estimate of original cost (actual?) was about $69,735,000. The Commission estimate was based on this but excluded (before deducting depreciation) an item of $17,000,000, made up largely of expenditures which had been charged to operating expenses prior to 1938 ($12,000,000 for well digging prior to 1923 and various other expenditures which for one reason or another had been charged to operating expenses as they occurred).

In a petition for review of the above Commission's order, the Fourth Circuit Court of Appeals set the order aside for the reasons:²

1. "that the rate base should reflect the 'present fair value' of the property, that the Commission in determining the 'value' should have considered reproduction cost and trended original cost, and that 'actual legitimate cost' (prudent investment) was not the proper measure of 'fair

¹ 64 S. Ct. 281 (U. S., 1944). A companion case, decided in the same opinion, was City of Cleveland v. Hope Natural Gas Co.
utility regulation

value' where price levels had changed since the investment;"
2. "that the well-drilling costs and overhead items in
the amount of some $17,000,000 should have been included
in the rate-base;" and
3. "that accrued depletion and depreciation and the
annual allowance for that expense should be computed on
the basis of 'present fair value' of the property not on the
basis of 'actual legitimate cost.'"
The Supreme Court granted petitions of certiorari to
the decree of the Circuit Court of Appeals because of the
public importance of the questions presented, and, after
hearing, reversed the Circuit Court of Appeals. Justices
Reed, Frankfurter and Jackson wrote separate dissenting
opinions, and Justices Black and Murphy wrote brief con-
curring opinions taking special issue with Mr. Justice
Frankfurter's dissent. Mr. Justice Roberts took no part
in the decision of the case.
The majority opinion written by Mr. Justice Douglas,
after an extended delineation of the facts, is a rather brief
justification of the result. It could be boiled down to a
conclusion of administrative law, namely, that the Court
would not substitute its judgment for that of the Commis-
sion as to the reasonableness of rates, the determination
of which was left by Congress to the Commission under
no formula other than that of "just and reasonable". Un-
less the end result of the Commission's action was clearly
demonstrated to be "unjust and unreasonable" by the com-
plaining parties, they had failed to make a case for chang-
ing the Commission's conclusions. In a brief introductory
paragraph, the Court assumed that it had already been
established that there was no doubt as to the constitutional
validity of Commission set rates which might impair the
value of property regulated. The Court said in part:

"When we sustained the constitutionality of the
Natural Gas Act in the Natural Gas Pipeline Co. case,
we stated that the 'authority of Congress to regulate
the prices of commodities in interstate commerce is at
least as great under the Fifth Amendment as is that
of the states under the Fourteenth to regulate the
prices of commodities in intrastate commerce.' . . .
Rate-making is indeed but one species of price-fixing.
. . . The fixing of prices, like other applications of
the police power, may reduce the value of the property

319 U. S. 735 (1943).
which is being regulated. But the fact that the value is reduced does not mean that the regulation is invalid. . . . It does, however, indicate that 'fair value' is the end product of the process of rate-making not the starting point as the Circuit Court of Appeals held. The heart of the matter is that rates cannot be made to depend upon 'fair value' when the value of the going enterprise depends on earnings under whatever rates may be anticipated.

"We held in Federal Power Commission v. Natural Gas Pipeline Co., supra, that the Commission was not bound to the use of any single formula or combination of formulæ in determining rates. Its rate-making function, moreover, involves the making of 'pragmatic adjustments.' . . . And when the Commission's order is challenged in the courts, the question is whether that order 'viewed in its entirety' meets the requirements of the Act. . . . Under the statutory standard of 'just and reasonable' it is the result reached not the method employed which is controlling. . . . It is not theory but the impact of the rate order which counts. If the total effect of the rate order cannot be said to be unjust and unreasonable, judicial inquiry under the Act is at an end. The fact that the method employed to reach that result may contain infirmities is not then important. Moreover, the Commission's order does not become suspect by reason of the fact that it is challenged. It is the product of expert judgment which carries a presumption of validity. And he who would upset the rate order under the Act carries the heavy burden of making a convincing showing that it is invalid because it is unjust and unreasonable in its consequences."

The Court then proceeded to emphasize: (1) that the Hope Company was a wholly owned subsidiary of the Standard Oil Company (N. J.) with no securities outstanding except $28,000,000 of capital stock; (2) that over the four decades of its operations it had earned the total investment in the Company nearly seven times; (3) that the Company's regular dividends had been high and its accumulated depreciation reserves and earned surplus accounts were large. After thus surveying the facts, and reviewing some of the Federal Power Commission's conclusions from them, the Court concluded:
"In view of these various considerations we cannot say that an annual return of $2,191,314 is not 'just and reasonable' within the meaning of the Act. Rates which enable the company to operate successfully, to maintain its financial integrity, to attract capital, and to compensate its investors for the risks assumed certainly cannot be condemned as invalid, even though they might produce only a meager return on the so-called 'fair value' rate base. . . ."

After thus disposing of the valuation problem, the majority opinion briefly approved the Commission's approach to the calculation of annual depreciation on cost and expressly disapproved the United Railways decision to the contrary, accepting by footnote reference Mr. Justice Brandeis' dissenting opinion in the United Railways case for "an extended analysis of the problem."4

The opinion then devoted several pages to the rights of West Virginia as an intervener in the litigation and concluded that the Federal Power Commission was correct in not allowing the effect on the taxing problem of that State to control its result in this rate regulation of the interstate sale of gas produced in West Virginia. This section of the opinion, while of interest in relation to the problem of Federal and State cooperation as visualized by the various acts conferring authority on the Federal Power Commission,5 is not within the scope of this comment.

The major impact of the case, of course, has been in its popular interpretation as striking the death knell of Smyth v. Ames6 and the constitutional protection to prop-

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4 United Railways & Electric Co. v. West, 280 U. S. 234, 259-288 (1930). This problem of the appropriate base for the calculation of annual depreciation is important enough to call for extended comment on its merits. However, that is beyond the scope of the present note. State law on the subject would seem to fall under the general comments which follow with reference to the rate base.


6 169 U. S. 466 (1898). The fair value rule is too well known to call for independent discussion here. For its development see: Wilcox v. Consolidated Gas Co., 212 U. S. 19, 41 (1909); Minnesota Rate Cases (Simpson v. Shepard) 230 U. S. 352, 454 (1913); Denver v. Denver Union Water Co., 246 U. S. 178, 191 (1918); Newton v. Consolidated Gas Co., 258 U. S. 651 (1920); Galveston Electric Co. v. Galveston, 258 U. S. 388 (1922); Southwestern Bell Telephone Company v. P. S. C., 292 U. S. 276 (1934). The last case contains a concurring opinion of Mr. Justice Brandeis (concurred in by Mr. Justice Holmes) setting forth the "prudent investment" theory which became the basis for most of the modern attacks on the doctrine of Smyth v. Ames. A good history of the cases up to the time of its publication may be found in Bauer and Gold, Public Utility Valuation for Purposes of Rate Control (1934). Cor-
property as embodied in the "fair value" rule of that decision. Actually, as said earlier, the opinion assumes that there is no such constitutional protection as "rates must yield a fair return upon the present fair value of property." There is no mention of *Smyth v. Ames* or the long line of subsequent cases resting on the above statement of its rule. There is no express over-ruling of its doctrine. However, in so far as the opinion in its entirety is predicated on the assumption of need for compliance only with the statutory standard, and in so far as the facts of the case indicate that the Federal Power Commission made no attempt to allow a return based on value, and in so far as the result of the Supreme Court action and several brief statements of the opinion accept the fact that the Constitution offers no such protection, the doctrine of *Smyth v. Ames* as far as Federal constitutional interpretation is concerned would seem to be as dead as if expressly overruled.

This becomes the more true if it is observed that none of the concurring or dissenting opinions rests on the assumption of any continuing constitutional protection of "fair return upon present fair value of property" in rate making. The dissent of Mr. Justice Reed, which comes closest to this, rests upon the assumption that the statute under which the Commission acted authorized "just and reasonable rates" as currently interpreted in the cases at the time of passage of the statute, which called for a Commission's appraisal of fair value as the rate base. Mr. Justice Reed was satisfied that the Commission had stayed within its powers as to the property valued, but felt that the Commission had acted unreasonably in excluding the $17,000,000 of development expenditures.

The dissents of Mr. Justice Frankfurter and Mr. Justice Jackson likewise rested on statutory construction. They emphasized, however, that the statutory standard had to be specially interpreted with reference to the particular industry regulated and they felt that there had not been sufficient consideration of the particular problems attendant upon the development and exploitation of natural gas fields for the Commission's action to be allowed to stand. Mr. Justice Jackson was the more explicit as to the nature of the things he desired to have considered. Mr. Justice

Frankfurter adopted Mr. Justice Jackson's views, but emphasized that Congress under the statute involved, had left review of the Commission's determination to the Courts, and for this to be carried out properly the Commission was required to be more explicit as to the criteria that guided its ultimate determination along the lines of the reasonableness of the rates in the particular field regulated.

The brief concurring opinion of Mr. Justice Black and Mr. Justice Murphy went largely to criticize Mr. Justice Frankfurter's dictum assumption that the silence of Congress over the years had indicated "Congressional acquiescence to date in the doctrine of Chicago, etc., R. Co. v. Minnesota," and to indicate their disagreement with his assumption.

Thus, it might be said that all the judges participating were willing to acquiesce in the abandonment of the constitutional guarantee that rates to be reasonable must yield a fair return upon the present fair value of property regulated. The conclusion might be even more broadly put that the Court indicates that it will not exercise any more supervision over rate-regulation than over any other economic regulations of Congress, or of the States. To acute observers, this was the only practical end the Court could reach, once it had established the validity of price regulation outside the category of utility regulation. That is, when in Nebbia v. New York, and later even more broadly

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7 134 U. S. 418 (1890). The doctrine of this case to which Mr. Justice Frankfurter referred was that the Courts must exercise the final say as to the reasonableness of rates set by legislative action. Or, as put more broadly by Mr. Justice Black and Mr. Justice Murphy, "That was the case in which a majority of this Court was finally induced to expand the meaning of 'due process' so as to give courts power to block efforts of state and national governments to regulate economic affairs." Cf. Olsen v. Nebraska, infra, n. 9.

8 This is confirmed in the majority opinion of Bowles v. Willingham, 64 S. Ct. 641 (U. S., 1944) (Mr. Justice Roberts alone dissenting) where Mr. Justice Douglas speaking for the majority in upholding rent regulation under the Emergency Price Control Act, said: "Of course, price control, the same as other forms of regulation, may reduce the value of the property regulated. But, as we have pointed out in the Hope Natural Gas Co. case . . . that does not mean that the regulation is unconstitutional." However, the same opinion later continued: "We need not determine what constitutional limits there are to price-fixing legislation. Congress was dealing here with conditions created by activities resulting from a great war effort. . . . A nation which can demand the lives of its men and women in the waging of that war is under no constitutional necessity of providing a system of price control on the domestic front which will assure each landlord a 'fair return' on his property."

in Olson v. Nebraska, the Court indicated that price control was not limited to special businesses (i.e., as affected with a public interest" or "dedicated to a public use") but could be extended by the appropriate legislative authority wherever it would be "reasonable" and not "arbitrary or discriminatory," the situation was pregnant with the possibility of the Court's ultimately facing the application of the "fair value" rule to any and every industry whose prices were controlled. With the guarantee of independent judicial review of the fact of value established by the Ben Avon Borough decision, the task of the courts could easily have become insurmountable, and effective price control impossible. Accordingly, the approach of the Court in the Nebbia and Olson cases contained the philosophy that spelled the death of Smyth v. Ames (and with it the doctrine of the Ben Avon Borough case as applied to price control).

The Court in the Nebbia case said:

"If the laws passed are seen to have a reasonable relation to a proper legislative purpose, and are neither arbitrary nor discriminatory, the requirements of due process are satisfied, and judicial determination to that effect renders a court functus officio."

In Olsen v. Nebraska, the Court said:

"We are not concerned, however, with the wisdom, need, or appropriateness of the legislation. Differences of opinion on that score suggest a choice which 'should be left where . . . it was left by the Constitution—to the States and to Congress.' . . . There is no necessity for the state to demonstrate before us that evils persist despite the competition which attends the bargaining in this field. In final analysis, the only constitutional prohibitions or restraints which respondents have suggested for the invalidation of this legislation are those notions of public policy embedded in earlier decisions of this Court but which, as Mr. Justice Holmes long admonished, should not be read into the Constitution. . . . Since they do not find expression in the Constitution, we cannot give them continuing

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10 313 U. S. 236 (1941).
vitality as standards by which the constitutionality of
the economic and social programs of the states is to
be determined.”

Thus if Congress, or a State legislature, sets a rate the
Court would not lightly substitute its judgment as to the
validity of such rate. If the power to set the rate is dele-
gated to a Commission, the Court similarly would be slow
to alter the Commission action except for failure to con-
form to the legislative standard. Thus, unless a statute
embodied as a standard the rule of Smyth v. Ames (Mr.
Justice Reed seemed to feel that the Natural Gas Act did),
the Court would not accept that rule as the sole test of
reasonableness.

However, prediction of the Court’s result in the Hope
case did not need to rest on such broad deductions from
the Court’s general constitutional philosophy. In a series
of preceding rate, or valuation, opinions, the evidence was
clearly present that the “fair return upon present fair
value” formula of Smyth v. Ames (as understood at least
in the early twentieth century) was to be foundered by
the broader constitutional and administrative law doctrines
of the present Court. The Hope case made explicit what
was already implicit in prior decisions, namely that the
Supreme Court had relaxed the Constitutional guarantee
of the rule of Smyth v. Ames and that the Federal Power
Commission would not be forced to construe the Natural
Gas Act as embodying that rule.

It is a little surprising, therefore, that the Hope case
caused such a wide popular furor and so easily created
an impression that all utility regulation was immediately
changed thereby. This interpretation of the case com-
pletely overlooks the nature of utility regulation.

The State Commissions, like all other administrative
bodies, are dependent upon the authority given by the
Statutes under which they were created and continue to
act. They are bodies of delegated power, obliged to stay

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18 Los Angeles Gas & Elec. Corp. v. Railroad Commission, 289 U. S. 287, 304, 305 (1933); West Ohio Gas Co. v. P. U. C., 294 U. S. 63, 70 (1935); Clark’s Ferry Bridge Co. v. P. S. C., 291 U. S. 227 (1934); West v. C. & P. Tel. Co., 295 U. S. 662, 692, 693 (dissenting opinion); Fed-

19 Language of the Maryland Court of Appeals in P. S. C. v. Sun Cab
Co., 160 Md. 476, 479, 154 A. 100 (1931) is typical:

“... The powers of the commission are such as are conferred
by the Act of 1910, ch. 190, and amendments, known as the Public
Service Commission Law, and all its acts are legislative; but, unlike
the Legislature, it is limited strictly to the powers so delegated.
within their delegated functions. The *Hope* case indicates that the Natural Gas Act did not embody the rule of *Smyth v. Ames* as a restriction on the rate-making powers of the Federal Power Commission. But, in a majority of jurisdictions, the State Commissions are acting under statutes which expressly, or by interpretation, have embodied the *fair return upon fair value* rule of *Smyth v. Ames*. And, in such jurisdictions, there would seem to be no justification for accepting the *Hope* case as changing Commission powers to act.

That this is true has already been recognized in two states. In *People's Natural Gas Co. v. Pennsylvania Public Utility Commission*, the Pennsylvania Superior Court, in anticipation of the *Hope* decision, said:

> “And it is important to bear in mind that, even though the Supreme Court of the United States as presently constituted, may, in the near future, overrule some of its former decisions and uphold as constitutional something other than fair value as a rate base, such change of position would not effect a change in the law of this commonwealth. Since the legislature put fair value into our law, together with what in 1937, when the law was passed, was universally understood to have been the elements of fair value, that body alone can take it out and substitute something else in its place. If and when the change comes—the concurring justices in Federal Power Commission v. Natural Gas Pipeline Co. . . . suggest that it has already taken place—it will simply mean that a constitutional limit on the power of the legislature to experiment or innovate will have been removed.”

In *Northern States Power Company v. Public Service Commission*, decided since the *Hope* case, the highest court of North Dakota expressed a similar view:

> “In the former appeal in this case (Northern States Power Co. v. Board of Railroad Com'rs, 71 N. D. 1, 298 N. W. 423) we held that the fair value formula as set

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Gregg v. Public Service Comm., 121 Md. 1, 87 A. 1111. As stated by Judge Offutt in Public Service Comm. v. Phila., B. & W. R. Co., 155 Md. 104, 114, 141 A. 509, 514: 'It exercises a naked statutory authority, and has no power save such as were expressly granted to it by the Legislature and such implied powers as are necessary to enable it to exert its express powers.' . . ."

15 13 N. W. (2d) 779, 785 (N. D., 1944).
forth in Smyth v. Ames, 169 U. S. 466, 18 S. Ct. 418, 42 L. Ed. 819, and as modified by subsequent decisions of the Supreme Court of the United States had been adopted by the Legislature of this State in 1919 as the formula for determining rate bases for public utilities. There can be no doubt today, but that, insofar as the federal courts are concerned, the 'ghost of Smyth v. Ames had been laid.' . . . That circumstance, however, has no bearing upon the question before us now. We are concerned with the law of this State as enacted in 1919. In the decision in the former appeal in this case we gave extended consideration to the construction of this statute and we see no reason now to modify that construction."

It is reasonably to be expected that most courts and commissions would feel legally bound to the approach indicated in these opinions. Only states such as California and Massachusetts, whose commissions for years have been interpreting their empowering statutes as supporting returns based on "prudent investment" cost, derive immediate "go" signals from the Hope case. Other State Commissions will continue to operate within the limits of empowering statutes embodying the "fair value" rule and some may even find constitutional restrictions. The Maryland Court of Appeals has indicated that such a restriction exists in Maryland.16 Obviously the meaning of state statutes and state constitutions is entirely within the control of the state courts.17

However, without need for considering constitutional limitations, the Public Service Commission Law of Mary-

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17 Green v. Neal, 6 Pet. 291 (1832); Leffingwell v. Warren, 67 U. S. 599 (1862); Merchant and Manufacturers National Bank v. Pennsylvania, 167 U. S. 461 (1897); Erie R. Co. v. Tompkins, 304 U. S. 64, 78, 79 (1938); Moore v. Ill. Central, 312 U. S. 630, 634 (1941); 1 Willoughby, CONSTITUTIONAL LAW (1929) 37. In Erie R. Co. v. Tompkins, Mr. Justice Brandeis, speaking for the Court, said in part:

"Except in matters governed by the Federal Constitution or by Acts of Congress, the law to be applied in any case is the law of the State. And whether the law of the State shall be declared by its Legislature in a statute or by its highest court in a decision is not a matter of federal concern. . . ."

". . . Supervision over either the legislative or the judicial action of the States is in no case permissible except as to matters by the Constitution specially authorized or delegated to the United States. Any interference with either, except as thus permitted, is an invasion of the authority of the State and, to that extent, a denial of its independence."
land in its valuation section seems to have incorporated the fair value rule of *Smyth v. Ames* and the Commission would seem to be bound to follow that rule. The statute reads:

"396. The commission shall, whenever it may deem it desirable to do so, investigate and ascertain the fair value of property of any corporation subject to the provisions of this sub-title and used by it for the convenience of the public. For the purpose of such investigation the commission is authorized to employ such engineers, experts and other assistants as may be necessary. Such investigations shall be prosecuted with diligence and thoroughness, and the results thereof reported to the legislature at each regular session. Such valuation shall show the value of the property of every such corporation as a whole, and the value of its property in each of the several counties and municipalities within the State of Maryland. . . ."

While this language might leave some room for speculation as to the meaning of value, the history of the act, the interpretations of the Public Service Commission in prior rate proceedings, and the rulings of the Court of Appeals in the rate cases that have been before it, leave no doubt but what the fair value rule for rate making is statutory law of Maryland.

The Public Service Commission Law was enacted in 1910 just after the Supreme Court of the United States had decided the case of *Wilcox v. Consolidated Gas Company of New York*,\(^\text{19}\) relating to gas rates in New York City. The case, following earlier decisions, specifically held that if utility property had increased in value (from the time of its original purchase) the company was entitled to earn a return on such increased value. Mr. Justice Peckham, speaking for a unanimous Court, said:


\(^{18}\) Md. Code (1939) Art. 23, Sec. 396.

\(^{19}\) 212 U. S. 19, 41, 52 (1909).
And we concur with the court below in holding that the value of the property is to be determined as of the time when the inquiry is made regarding the rates. If the property which legally enters into the consideration of the question of rates has increased in value since it was acquired, the company is entitled to the benefit of such increase. . . ."

There can be little doubt that the Legislature was aware of such pronouncements as to the meaning of "value" when it adopted a Public Service Commission Law worded in terms of "value." But, be that as it may, the Court of Appeals has left no doubt as to its opinion in the matter. In Miles v. Public Service Commission, the Court specifically took cognizance of the fact that the valuation provision of the Maryland law was enacted in order to embody into State law the principles previously enunciated by the United States Supreme Court. The Court of Appeals said:

"... as was said by the Supreme Court in San Diego Land & Town Co. v. National City, 174 U. S. 739: 'What the company is entitled to demand in order that it may have just compensation is a fair return upon the reasonable value of the property at the time it is being used for the public.' It is such a valuation which section 385 of article 23 of the Code of 1924 authorizes the Public Service Commission to make; the language being: 'The commission shall, whenever it may deem it desirable to do so, investigate and ascertain the fair value of property of any corporation subject to the provisions of this sub-title and used by it for the convenience of the public. . . . Such valuation shall show the value of the property of every such corporation as a whole and the value of its property in each of the several counties and municipalities within the State of Maryland.'

"The very purpose of authorizing the commission to ascertain the value of the property of the various

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20 The Maryland Act was largely in terms of the New York Law and New York litigation had just been completed in the United States Supreme Court. Also, the bill as proposed to the legislature contained a reference to "Wilcox v. Gas Co., 212 U. S. 19" in explanation of the valuation section. See a draft of the proposed bill as submitted by Attorney General Isaac Lobe Straus under title "A Public Utilities Bill . . . for the consideration of Governor Crothers and Cabinet" (1909) 59.

public service corporations is to enable it to fix the
rates which the corporation is permitted to charge the
public for the service rendered. . . .” (Emphasis
added.)

Actually, the Court of Appeals had earlier indicated
that reasonable rates meant rates calculated to yield a fair
return upon the present value of the property of the regu-
lated utility, in the first case presented to it calling for con-
sideration of the valuation problem under the Public Serv-
ice Commission Law. In Havre de Grace Bridge Co. v.
Public Service Commission,22 the litigation involved an
order of the Public Service Commission issued to the Havre
de Grace Bridge Company to reduce its rates of toll on a
bridge over the Susquehanna River between Havre de
Grace and Perryville. The bridge had been officially built
as a railroad bridge some 40 years earlier at a cost of over
$2,000,000. The bridge had become inadequate as a rail-
road bridge and the railroad had built a new bridge with
the assent of the Legislature, subject to a requirement that
the old bridge be removed. The railroad converted the old
bridge into a highway bridge at a cost of some $89,000
(probably to avoid a greater expense of destruction) and
turned the bridge over to the Havre de Grace Company,
formed for the purpose of operating the bridge with a
capitalization of $50,000. The Bridge Company spent
$1,700 in erecting tool houses, etc., and began operating
the bridge, which yielded only a meagre income as had
been expected. However, with the development of the
automobile, the annual revenues suddenly increased to
where they were in excess of the original capitalization of
the Company. The litigation grew out of protests by resi-
dents of adjoining counties that tolls were too high and the
consequent Public Service Commission, order to reduce
them (by 40% according to the P. S. C., 72% according to
the Company). This order the Bridge Company unsuc-
cessfully attacked in Circuit Court No. 2 for Baltimore
City. On appeal, the Court of Appeals reviewed the facts,
the procedure of the Commission, and of the lower Court in
considering the propriety of the Commission's action in
determining value. It then set forth the Court's ideas of
what the Public Service Commission Law allowed the
Commission to do, and reversed and remanded the case

22 132 Md. 16, 103 A. 319 (1918).
to the end that the order be set aside and the case be remanded to the Commission. The Court said in part:

"Both in the argument and in the brief filed on behalf of the Public Service Commission there was used, probably by inadvertence, an expression calculated to mislead, namely, the value of the property of the bridge company for rate making purposes. The provision for the valuation of the property of a corporation, subject to the Public Service Law, is found in the Code in Article 23, section 442 (now Sec. 396, supra), where the Commission is empowered to 'ascertain the fair value of the property of any corporation subject to the provisions of this sub-title.' That, and that only, is the valuation which the Public Service Commission is authorized to ascertain, and it would tend not only to work an injustice, but to render absurd a proposition that the property of a public service corporation might have one value in fact, another for purposes of rate making, and a third for purposes of taxation, in the absence of statutory provision such as obtains in some states, that for taxation purposes property is to be assessed at only a given percentage of its real value. What the Commission in this case was authorized to ascertain under the section referred to was the fair value of the property.

"...

"... the company owes a duty to the public as well as to its stockholders, and must charge no more than a reasonable rate for the services rendered.

"In reaching this, there are many factors to be considered. A partial enumeration of these would include the value of the property employed, the value of the service rendered to the user, whether or not the corporation enjoyed a monopoly, the rate of return which should be made to the stockholders after the payment of operating expenses, upkeep and fixed charges, a reasonable allowance for depreciation, whether or not the utility is in operation or in fieri, the risk incurred by those who began the undertaking, and others which may arise out of the utility which is being operated.

"...

\[23\] See this language explained in Miles v. P. S. C., 151 Md. 337, 344, 345, 135 A. 579, 49 A. L. R. 1470 (1926)
"In undertaking the work of the valuation of this bridge the Commission proceeded about as follows: it had its own regular engineer estimate the cost of the reproduction of the bridge, and in the course of the testimony before the Court another engineer, Mr. Shirley, was called upon the same point. The Commission had determined naturally and properly to reject the valuation of the bridge simply upon the basis of what it had cost the incorporators. This would have been as far afield as it would have been to have taken the cost of the bridge to the P., W. & B. R. R. at the time of the original construction. The real point to be ascertained was not what it had cost either the railroad company to build the bridge, or the incorporators of the Bridge Company to acquire it, but what was its fair value at the time of the investigation by the Commission. In a number of cases recourse has been had to this line of inquiry for a similar purpose, but the value testified to of such a structure is only one of the factors to which consideration must needs be given in such a proceeding, and the reproduction value is liable to be increased from other considerations, and diminished by various allowances." (Emphasis added.)

In this first interpretation of the Maryland Public Service Commission Act, the Court predicated its result entirely on its construction of the Statute. No sentence, word, or phrase referred to any constitutional compulsion for its result. No decision of the United States Supreme Court was mentioned or referred to in the opinion as influencing the Court's approach. It is improbable that the meaning of a statute, so construed, would be affected by the Hope case's departure from earlier federal doctrine.

The approach of the Havre de Grace case was confirmed by the Court of Appeals in Miles v. P. S. C., supra, and in P. S. C. v. United Ruys. Co. In the latter case, the decision went largely to the reasonableness of the rate of return allowed. However, in a brief reference to valuation, the Court said:

"The central dominating question presented by the appeal is whether the schedule of rates promulgated by the commission is sufficient to yield such an income

\[155\text{ Md. 572, 579, 142 A. 870 (1928).}\]
as will give to the company a fair return on the value of its property. . . . So that the question actually is whether a schedule of fares which, after deducting all reasonable and proper expenses for the management and operation of the company, permits it to earn a net return of 6.26 per cent. on the value of its property, is confiscatory within the meaning of the state and federal constitutions, or unlawful and unreasonable within the meaning of the statute creating the commission. To that question there are various approaches, all differing in some degree in the effect they have upon the meaning and weight of the facts of the case.

". . .

"In valuing the property for rate making purposes, the commission based its conclusion upon its present value and not upon its original cost, and in fact the case of Havre de Grace Bridge Co. v. Pub. Serv. Comm., supra, left it no alternative. . . ." (Emphasis added.)

A survey of the Public Service Commission reports confirms that the Commission, from the first opinion rendered to it by its first general counsel, through its latest rate proceedings, has followed the legislative mandate of reasonable return based upon present fair value.

The failure of the Legislature to change the statute during more than thirty years of such consistent interpretation of its meaning is to give practically conclusive effect to such interpretation. This doctrine of ratification by acquiescence is supplemented in Maryland by the fact that, in 1941 in passing a statute giving the Public Service Commission authority to establish temporary rates, the Legislature worded the law in terms of "reasonable return

26 See 4 Md. P. S. C. Reports 39 (1913); 8 Md. P. S. C. Reports 198 (1917); 14 Md. P. S. C. Reports 100, 104 (1923); 16 Md. P. S. C. Reports 74 (1923); 24 Md. P. S. C. Reports 288 (1933); 31 Md. P. S. C. 87, 95 (1940); which is the last formal opinion of the Md. Commission in a rate case, and which clearly states, "The Company is entitled to a reasonable return on the fair value of its property" and gives full weight to reproduction cost.
27 Mayor and City Council of Baltimore v. Machen, 132 Md. 618, 623, 104 A. 175 (1918); Burroughs Adding Machine Co. v. State, 146 Md. 192, 198, 126 A. 127 (1924); Arnreich v. State, 150 Md. 91, 103, 132 A. 430 (1928); Nashville, C. & St. L. Ry. v. Browning, 310 U. S. 362, 369 (1940); Note (1942) 7 Md. L. Rev. 87.
upon the value" of the property.\textsuperscript{28} Such use of language with well accepted construction by the Courts and by the Commission would normally be treated as adoption of the current usage of the terms.\textsuperscript{29}

With this consistent interpretation of the meaning of the Maryland Public Service Commission Law by the Court of Appeals and by the Commission, as calling for a return based on value, and practically a ratification of this by the Legislature in 1941, it would seem that the decision of the Hope Natural Gas case would have little immediate effect in Maryland. Like the courts of Pennsylvania and North Dakota, the courts of Maryland would be obliged to apply their own statute in ruling upon Public Service Commission authority to establish rates for Maryland utilities. If the Public Service Commission adheres to the established construction of the statute from which it derives its authority, the Courts will not even be called upon to face the issue.

Accordingly, other than to make the public rate conscious, and thus to stimulate Commission inquiry into the fairness of existing rates under traditional standards, the Hope case should not have any great immediate effect in Maryland, or in states with similar utility laws. Investigations, hastily stimulated, may or may not result in major rate changes in favor of the public. For, in a period of inflated values and increased costs of operation, such as now exists, any investigation made along the lines of fair return upon present fair value may as readily point toward a rate increase as to a rate decrease.

Aside from all else, the abnormal conditions accompanying a war economy are not appropriate for rate investigations.\textsuperscript{30} Many State Commissions have suggested an aversion to wartime investigations in connection with the instant war, or after investigation have refrained from action.\textsuperscript{31} This feeling was perhaps most cogently put by

\textsuperscript{28} Md. Code Supp. (1943) Art. 23, Sec. 272.


\textsuperscript{30} This has been deemed to be true of any period of abnormal price change, West v. C. & P. Tel. Co., 295 U. S. 662, 673 (1935). And see cases infra, n. 31.

\textsuperscript{31} Re: Jersey Central Power & Light Co., 34 P. U. R. (N. S.) 1 (N. J., 1940); Re: Northwestern Bell Telephone Co., 36 P. U. R. (N. S.) 1 (Minn., 1940); Re: Customers of Plymouth County Electric Co., 39 P. U. R. (N. S.) 20 (Mass., 1941); Re: Montana-Dakota Utilities Co., 40 P. U. R. (N. S.) 327 (Mont., 1941); Re: Kentucky Utilities Company, 41 P. U. R. (N. S.) 129 (Ky., 1942); Mayor of Lynn v. New England Tel. & Tel. Co., 42 P. U. R. (N. S.) 1 (Mass., 1942). See also the introduction to the annual
the Massachusetts Commission when it expressed itself with reference to an investigation of the rates and charges of the New England Telephone and Telegraph Company, after a public hearing at the petition of the town of Lynn with reference to exorbitant rates alleged to be charged its citizens. The Commission said:\textsuperscript{32}

"Apart from what we believe to be a fact that a statewide rate investigation would result in no tangible benefits in these times, we are conscientiously alert to the dangers which could result from such an untimely investigation.

"Prior to the declarations of war, and since, the company has expended huge sums of moneys in a co-operative effort to make intelligently effective the plans of the United States government directed toward a successful and efficient conclusion of the war. The defense program and now the war effort require many additional facilities. The energies and resources of the company are being used. Many of the company's officials and employees whose services would be needed immediately by the company, if a rate investigation were to begin, are engaged now in the solution of problems arising out of war activities and at present they are devoting practically all of their time and effort in that direction.

"On December 29, 1941, His Excellency, Governor Leverett Saltonstall, issued a proclamation which set forth and proclaimed 'that a state of emergency exists by reason of war whereby the peace and security of the commonwealth are endangered by the imminent

reports of the New York Commission 1940 and 1942; and also, statement of policy "In re: Earnings During War Emergency" issued June 9, 1943 by the Pennsylvania Commission quoted infra, n. 33. Cf. Annual Report of the Tennessee Valley Authority (1943) p. 46, saying:

"However, the war has intervened and forestalled any general trend toward rate reductions which a number of systems are financially able to make. There are several reasons for holding such reductions in abeyance. Rate reductions would tend to encourage increased use and would therefore conflict with programs for the conservation of fuel, transportation, manpower, and critical materials. From the standpoint of furthering the wider use of electricity, it is felt that rate reductions should be delayed until they can be accompanied by sustained and effective promotional activity in the appliance field. Delay also will permit a more complete appraisal of the probable post-war earnings of the distributors."

threat of belligerent acts of the enemies of the United States' and it was thereupon urged by the governor that:

"In addition, I urge all the people of the commonwealth to cooperate with and assist the duly constituted authorities in all measures taken for defense, and to avail themselves at every opportunity of the privilege of serving in some capacity in the common endeavor which will bring us victory over all our enemies."

"In our nation's present crisis, the company is commendably and capably serving in a 'capacity in the common endeavor.' Moreover, the resources of the company are needed by the nation. It would not be in the public interest for us to intervene at this time."

On June 7, 1943, the Pennsylvania Commission in a statement of policy issued to all public utilities subject to its jurisdiction clearly indicated that it deemed it inadvisable to conduct any general rate investigation during the war and that it would do so only if utilities refused to cooperate in the conservation of wartime earnings. The Commission formally declared its policy to be:

"(a) That it is imperative that public utilities maintain a strong financial position throughout the war emergency, to the end that they may render prompt and uninterrupted service during said emergency and that they may enter the post-war period prepared to promptly take up the matter of deferred maintenance and the rehabilitation of their properties.

"(b) That the Commission deems it inadvisable to institute formal investigations into the reasonableness of existing rates which appear to be producing increased earnings as the result of an artificial economic situation created by war conditions.

"(c) That the Commission invites the cooperation of all public utilities in refraining from the payment of dividends or owners' salaries materially higher than similar payments in peace-time to the end that cash may be conserved to adequately meet post-war conditions; but that without such cooperation the only alternative left to the Commission is to institute an in-
vestigation into the rates, depreciation and maintenance practices and other related affairs of any public utility showing abnormal earnings.\textsuperscript{38}

Thus, because of the time at which it was decided, plus its inherent nature, the Hope case is not likely to have the widespread immediate effect on utility regulation as was generally indicated by popular commentaries. As in Maryland, because of the wording of the Public Service Commission Law and its interpretation by the State Courts, many of the state utility commissions are given no authority to make wholesale revaluations of property because of the Hope decision. Investigations are called for

\textsuperscript{38} The Commission, after observing the increased earnings and before making its declaration of policy, said:

"Whether or not this increase in earnings has resulted in an unreasonable return to any particular utility is determinable only after full consideration of that utility's affairs. The Commission takes cognizance of the fact that the increased demands of the war and the limitations and restrictions imposed by the Government to expedite the war program, has produced an artificial economic situation, which renders difficult an adjudication of rates which would be fair and reasonable both in the present war emergency and the ensuing post-war period, giving due consideration to the interests of consumers, the investors, the tax authorities and the utilities.

The Commission takes cognizance of the increased speed and continuous use of equipment now required to meet demands for service; the departure from maintenance routine occasioned by such continuous use, as well as by the scarcity of maintenance personnel and materials; and, in some instances, the installation of equipment of a character or capacity which is suitable for wartime needs, but which may not be used or useful in the public service when peacetime operation is resumed.

The Commission expects the public utilities under its jurisdiction to offset these wartime costs against the wartime revenues they are producing, to the end that depreciation now being suffered, and maintenance now being deferred, shall not be offered as arguments in support of post-war rate increases, or to prevent, when otherwise warranted, post-war rate reductions. The Commission now advises the public utilities subject to its jurisdiction that it will scrutinize every such argument in the light of the equipment operating records, the charges to depreciation and maintenance, and the operating income, for the period through which we are now passing.

The Commission is also aware of the fact that many wartime inventions have peacetime applications, and thereby speed the obsolescence of pre-war devices; and that to provide the newest equipment and the most modern service, the public utility industry may require huge quantities of cash when the war is ended.

All of these factors point to a provident and cautious course in disposing of abnormal earnings. They indicate that the payment of abnormally large dividends, or of excessive salaries of partners and individual owners, may be ultimately injurious, not only to the recipients, but to the public service as well."

The quotations are taken from a mimeographed copy of the "Statement of Policy—In re: Earnings During War Emergency."
only to the extent to which existing requirements of state law have not been met.

The most that can fairly be said is that the Hope case indicates that, if a state commission in appropriate compliance with state law, reduces utility rates after a fair hearing and is sustained by the state courts, there is little reason to anticipate any further judicial protection from the United States Supreme Court on the ground of confiscation. It is doubtful, however, whether state courts and legislatures, which have shown no tendency to move away from the fair value rule during the last twenty years, will change overnight with the decision of the Hope case any more so than they have changed with other alterations or reversals of doctrine by the Supreme Court.

VESTED AND CONTINGENT REMAINDERS

Sale Deposit & Trust Co. of Baltimore v. Bouse

The testatrix died in 1922 and bequeathed one-fourth of the residue of her estate in trust for her son, Alfred, for life, and after his death to his child or children living at the time of his death, but if he should die without leaving any surviving children, or if his children should all die before the age of twenty-one years, then to the other children of the testatrix, naming them. A similar bequest was made to her daughter, Mary Helen. Both bequests were made upon condition that the life tenants make similar provision for the devolution of certain other property; these conditions were complied with by the life tenants, both of whom executed deeds of trust containing similar limitations, shortly after the death of the testatrix. Alfred died in 1940 without any surviving children; Mary Helen died in 1941 leaving three children surviving. After the death of the testatrix and after the execution of the trusts by the life tenants, but prior to the death of the life tenants, legislation was passed imposing certain inheritance taxes which, if applicable, would subject the remainders to taxation.

Held:

The remainders passing upon the death...