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**A PROPOSED SOLUTION
OF
THE RAILROAD PROBLEM**

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PROBLEM*

NEW YORK, October 24, 1917.

HON. FRANCIS G. NEWLANDS, *Chairman, Joint Committee on
Interstate Commerce, Washington, D. C.*

DEAR SIR:

For ten years I have advocated government control of the railroads without government ownership. Coupled with such government control would be government guaranty to finance the railroads. In presenting that idea I contributed articles to the North American Review in June, 1908; McClure's Magazine, January, 1912; Harpers' Weekly, April 4, 1914; Yale Law Journal, March, 1915; Michigan Law Review, November, 1915; a series of letters in the New York Sun in the year 1916; an article in the Yale Law Journal in January, 1917, and I also discussed the subject in the Prefaces to the Sixth Edition (1908) and the Seventh Edition (1913) of my work on Corporations. I drew a proposed Act of Congress to carry out my plan, and it was introduced in the United States Senate by Senator Thomas, December 7, 1915 (Senate Bill No. 18). As counsel of The Mackay Companies, controlling many telegraph and submarine cable systems, through ownership of their stocks, I know the feasibility, simplicity and efficiency of this plan. American lawyers have much to do with railroad administration, but no American lawyer heretofore has proposed any fundamental solution of the railroad problem. When the natural leaders cease to lead, dangerous remedies may be adopted.

The same fundamental idea has now been adopted as a war measure in Great Britain and Canada and soon will be in the United States, namely, government control without government ownership, but with government financing.

Great Britain: That country is handling its railroads to-

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day under this plan. The English railroads are being managed by a committee of railroad general managers, and the government guarantees to stockholders the same dividends that they received prior to the war. The results have been eminently satisfactory, and, in fact, the profits to the government have been so great that the government declines to state what they are.¹

United States: The Presidents or chief executive officers of the great American railroad systems, aggregating over 90 per cent of the railroad mileage, have formed an Association for co-operation between the railroads. Now that war has broken out this Association is taking steps which amount practically to a consolidation of all the railroads of the country under one management for operating purposes. They adopted a resolution April 11, 1917,

"that during the present war they will co-ordinate their operations in a continental railway system, merging during such period all their

¹ Mr. Henry W. Thornton, formerly of the Pennsylvania Railroad Company and later General Manager of one of the chief English railroads, said, in an article published in the *Railway Age Gazette* in June, 1917, on the subject of control of the English Railways by the British Government during the present war:

"In eliminating the financial necessity for seeking traffic, it also enabled the railways to revise their time-tables and cut out duplicate services, excursion trains, unremunerative mileage, and what may be termed profit-seeking facilities generally. Various stations, and even whole sections of line, have also been closed. Furthermore, restrictions were placed upon pleasure party and race meeting arrangements, affecting the public to such an extent as only to be possible when enforced upon patriotic grounds by an executive acting with all the authority of the Government behind it. I might mention here that one of the most drastic measures brought into operation, with the object of reducing railway travel, has been the universal raising of all ordinary fares by 50 per cent. * * * Generally speaking, the volume of traffic is at least 50 per cent in excess of what it was during the busiest year the railways had experienced previous to the war; but apart from occasional congestion and delay it has been worked satisfactorily, notwithstanding the fact that about 142,000 railway men (23 per cent of the pre-war staff) have joined the colors, either for general or railway service abroad, and that it is being conducted with fewer engines and wagons."

merely individual and competitive activities in the effort to produce a maximum of national transportation efficiency."²

That Association, together with the war Acts of Congress, gives the government practical control of American railroads without government ownership, and practically operates the railroads as one system, pools their equipment, routes their traffic, regulates their train service, and eliminates duplications of service. The war is repealing the Sherman Anti-Trust Act of Congress of July 2, 1890. That Act did good work in breaking up railroad combinations, which threatened to control the public, but the public is now learning by the march of events how to control without that Act. It may safely be predicted that the American railroads will never go back to competition, and that the past public policy of railroad competition is gone forever. It is a momentous step in the right direction. It is the application of the plan I have advocated for years, except that it lacks the financial backing of the government. That backing will have to come, and with it the government will insist on public control, instead of private control. It will mean what the railroad men themselves are now bringing about, namely, one vast unified railroad system, covering the whole United States. In fact, with almost unbelievable rapidity all of our great industries are being subjected to government control. The natural evolution of years is being accomplished

² President Willard, of the Baltimore & Ohio Railroad, and Chairman of the Advisory Railroad Commission on National Defense in an address June 29, 1917, said:

"One of the first problems requiring serious consideration after the declaration of war was the matter of transportation, and I feel that it is a great credit to the railroads of this country that in just five days after the Congress had declared war, men representing the 175 principal independent railroad companies in the United States assembled in Washington, and, after listening to a presentation of the situation, they voted unanimously then and there, and signed papers confirming their action before they left the city, giving to a small committee of five men, selected by these railroad representatives, full power to control the operation of all the railroads in the United States during the period of the war in order that the railroads might thereby be in a position to respond immediately and as a unit to any demand made upon them by the President in the interest of the general situation."

in a few months. And never again will we swing back to the old system in its entirety. Especially so with the railroads, without money, without friends, without hope under the present régime.

Canada: That country has adopted this idea permanently, and not merely as a war measure. A Royal Commission, consisting of Mr. Acworth, the eminent railway economist of London, Sir Henry L. Drayton, Chairman of the Canadian Railway Commission, and Mr. Smith, President of the New York Central Railroad, rendered a report May 2, 1917, in which Mr. Acworth and Sir Henry L. Drayton recommended that a Dominion Railway Company be organized, consisting of five Trustees to operate all the railroads in Canada, excepting the Canadian Pacific, the Canadian Government to assume financial responsibility. The Trustees were to acquire the stock of those railroads without disturbing outstanding bonds and debentures, and without the government guaranteeing those bonds and debentures.³

This plan in part has now become a law, not by the liberal or labor party, but by the conservative party, headed by Sir Robert Borden, the Premier. On August 1, 1917, in the Canadian Parliament, the Minister of Finance, Sir Thomas

³ President Rea, of the Pennsylvania Railroad, was reported on August 9, 1917, as favoring the Canadian Government's proposal to nationalize the Canadian Northern Railway. He is reported to have said: "Only one large system is pre-eminently profitable," and adds that the crux of the problem is Who is to provide for the deficiency in earning and interest charges and operating expenses and furnish the capital essential to finish and properly equip the new lines in the next ten years or more? "Obviously," concludes Mr. Rea, "the only available source in sight that can shoulder that great responsibility is the Canadian Government. It is also obvious that the Canadian people will not shoulder these obligations and at a future date permit private companies or stockholders to be the beneficiaries. The majority Commissioners suggested operation by a board of trained railroad and business men, with practically a life tenure of office. This is an experiment which may fail, but some such co-operative plan must be adopted to meet with the approval of the Canadian people. The burden is too great to be left solely to private capital and initiative, because there is no present or immediately prospective earning capacity to warrant private capital in assuming that load, and all capital sources are being drained by the war."

White, placed before the House of Commons a proposal that the government should acquire \$60,000,000 of the capital stock of the Canadian Northern Railway Company (the remaining \$40,000,000 being already owned by the government), and said:

"This opens up a great vista to the imagination of the members of this House and the people of this country, because it means that the people of Canada will own, not only a highway from Halifax to Vancouver, but a great transcontinental railway system in its grades, curvatures and connection second to none."⁴

The Canadian Parliament has passed the bill. This is government control and government financial responsibility

⁴Further details as drawn from the statement made to Parliament by Sir Thomas White on that occasion are as follows:

"With the \$40,000,000 par value of stock which we now have, we shall be the absolute owners of the Canadian Northern Railway system. Whatever money we expend in payment of fixed charges, for betterments or for rolling stock, will enure to the direct and sole benefit of the people of Canada. We think it desirable, in the interests of efficiency of management, and for the purpose of financing, that the system should continue to be administered as a corporate entity. Therefore, we propose, as I have stated, to acquire all the outstanding stock."

As to the mode of determining the value of the \$60,000,000 of stock, Sir Thomas White said that it would be by arbitration, and if all of the arbitrators did not agree the Supreme Court of Canada should decide the matter. Sir Thomas further said:

"We are preserving the corporate entity of the Canadian Northern Railway Company. When we get the stock, we are absolute masters of the Board of the Canadian Northern Railway Company and of its entire administration, and the Board, as we constitute it, will be the Board of the Canadian Northern Railway Company carried on for its shareholders, who will then be the people of Canada. In other words, the private ownership of the shares is entirely eliminated.

* * * * *

"In the appointment of the board of directors and the general administration of the Canadian Northern Railway system we shall, of course, have to consider what is in the interests of the public. Speaking offhand, I should say this: There are on the staff of the Canadian Northern some exceedingly capable officials—men like Mr. McLeod, Mr. Hanna and Mr. Mitchell, the operating heads of the several departments. My own view is that the government would be wise to retain as far as possible the services of these men in connection with the administration of the system.

* * * * *

"It is true that the Governor in Council, through the ownership

without government ownership.⁵ The Canadian Northern Railway system comprises about one-third of the railway mileage in Canada. The only difference between my plan and the proposed plan of the Canadian government is that under my plan the stock in the railroads would continue to be owned by the public in the form of government guaranteed stock of the five Federal Railroad Companies, while under the Canadian plan the government will own all of the stock.

The Canadian plan is good and we have a similar one in our recent device of Federal Boards controlling Federal Corporations. The next logical step is a Federal Railroad Board

of the stock, will have the power to elect the board, but we propose that the operation of the Canadian Northern Railway system shall be through its boards of directors. The administration of this system will therefore be under the boards, and not immediately under the minister, as the Intercolonial is under the Minister of Railways. In other words, we shall not have the actual physical property in this system, but we shall have control of the stock in its entirety, and we shall name the boards, and the boards will in turn, through their executive officers, administer the system.

* * * * *

"It could hardly be self-constituted, because it would have to be constituted in the first place by some authority, but after it was constituted the vacancies arising would be filled by the remaining members; in other words, it would be a complete sovereignty in itself—self-perpetuating."

⁵ The *Railway Age Gazette*, the leading railway paper of this country, first approved the majority report of the Canadian Commission and then disapproved it. Thereupon Mr. Acworth wrote that journal a letter reading as follows:

"I value highly your opinion, and regret that you do not approve of the solution of the Canadian railway problem recommended in the majority report. I do not think it would be proper for me to argue with you. But without arguing I should like to deal with two points in your article.

"You think that our proposed board of trustees 'would be a clumsy device for management'; you say that 'any commercial concern, to be successfully managed, must have its executive work conducted under the direct supervision not of five men but of one man.' I agree, and that is what is proposed. We have recommended that there should be three trustees, the best railway men that can be obtained. Let us call the chairman the president, and the two other whole-time trustees vice-presidents. We have recommended this board should be completed by the addition of two other members not

controlling Federal Railroad Corporations, organized for the purpose of controlling by stock ownership or otherwise all the railroads of the United States. The proposed Act of Congress attached to this paper carries out that idea. Briefly, the plan set forth in that proposed Act is as follows:

1. Congress should incorporate five Federal Railroad Companies for five divisions of the whole country. This corresponds to the plan of the twelve Federal Reserve Banks.

2. These five Federal Railroad Companies would acquire gradually the stocks and bonds of the present railroad companies, each in its own district, just as the Canadian Government is about to acquire the stock of the Canadian Northern Railway Company. These stocks and bonds would be acquired at their actual value by purchase, exchange or condemnation. The Federal Railroad Companies could obtain the money by the issue of their own stock with 3 per cent dividends guaranteed by the government, with a possible extra 3 per cent if earned, all over 6 per cent to go to the gov-

required to give their whole time; and we have assumed that they will leave the normal management of the railway to the president and his two vice-presidents. The only difference between our proposed board of trustees and the ordinary railway board of directors is that we have limited the number of non-experts to two. The reason for this is obvious, and I will refrain from stating it.

"Further, you express yourself in favor of a scheme 'under which the ownership and management of the present private railways would be left in private hands' and 'the enterprise and efficiency of private management' retained. I agree, but unfortunately am compelled to add the words 'if possible.'"

"I invite you to re-peruse pages 49 and 50 of our report. If we have come to a wrong conclusion in saying that a private company certainly could not be formed in Canada, probably could not be formed outside Canada, while in any case formation outside Canada would be open to the gravest objection, I invite you to put us right. If you will work out in such detail as to permit of fruitful criticism a private company scheme that in your judgment will meet the situation, you will confer an important service on the people of Canada. For my part, six months' study of the question has taught me that to desiderate or even to adumbrate a scheme is one thing, to work it out in practical detail of dollars and cents is quite another. The former is easy and valueless, the latter, I have been reluctantly constrained to believe, is, under the circumstances, impossible."

ernment. Such guaranteed stock would also be issued to provide fresh money for railroad extensions and additional facilities; also to acquire from time to time at their actual value the present outstanding railroad obligations. The guaranteed dividends could be at a higher rate than 3 per cent, if necessary, and would vary from time to time according to general conditions, but when once fixed as to any particular issue would not be subsequently changed for that issue.

3. The Federal Railroad Companies would then control the present railroad companies and could take over their tangible property if the state charters ceased to be desirable, or could condemn the railroads if necessary.

4. A Federal Railroad Board (similar to the present Federal Reserve Board) nominated by the President and confirmed by the Senate, would name the directors of the five Federal Railroad Companies and would control the finances of those companies and regulate all railroad rates and service.

Mr. Acworth has discussed the merits and demerits of this plan in an article reproduced at the end of this paper. The plan embodies the idea of government control and government financial responsibility (reduced to a minimum⁶) without government ownership. These two fundamental interwoven features, namely, a government guaranty and government control, may well be considered separately.

Government guaranty: The public insists that the railroads shall increase their terminals, tracks and facilities. The railroads are willing, but haven't the money and can't get it.

⁶ Sir Thomas White, Minister of Finance, in the debate on the bill authorizing the Canadian Government to purchase \$60,000,000 par value of stock of the Canadian Northern Railway, said: "The chief advantage of preserving the corporate identity of all the companies embraced in the system is that it maintains the financing which is already being done and it facilitates future financing; that is to say, by acquiring—and that is the third alternative of which my honorable friend spoke—the entire \$100,000,000 of the capital stock of the Canadian Northern Railway Company, which in turn controls the stock of all the underlying companies, the Government is enabled to assist the corporate financing of that system. In other words, the system of finance which has been adopted and which is now being employed will continue to be employed, the Government giving such assistance as may, from time to time, be necessary."

Investors are afraid. \$1,000,000,000⁷ a year is needed for at least the next five years and yet the railroads cannot obtain a tenth part of that sum. Last year only \$64,101,000 was raised by the railroads, exclusive of refunding; since January, 1915, only \$91,535,000. High grade first mortgage bonds in 1905 sold at an average price of 103, but to-day those same bonds are selling at an average price of 84. The New York Central not long ago issued \$100,000,000 debentures bearing 6 per cent interest. Last winter, when its stock was above par, it offered to its stockholders \$25,000,000 new stock at par, but the stock declined and the offer collapsed. To-day its stock sells at 71. The railroads have got to have money to keep up with the growth of the nation in population and commerce, but money they cannot get. The investor is afraid of regulation. This is the crux of the trouble. Mr. Prouty, the veteran Interstate Commerce Commissioner, says:

“This is the point at which regulation will break down if at all. Can private capital be induced, under the treatment which is accorded that capital by the regulating body, to invest? If government ownership ever comes in the United States it will probably be because private capital cannot be obtained in sufficient amounts to afford an adequate service.”

Railroad men point out that no double track railroad is found west of the Mississippi excepting one; that since January 1, 1915, only \$12,910,520 has been raised by the railroads by the issue of stock; that the year 1915 saw less new railroad

⁷ Mr. Thom, representing as counsel practically all of the railroads, says \$1,500,000,000 a year, including refunding. See p. 73 of your Record. Mr. Kruttschnitt, in his testimony, said (p. 921):

“Bearing the expenditures in mind which have been already made and realizing that a large additional amount will be necessary to provide for the desired adequacy of transportation facilities and for the refunding of maturing debt, it is necessary for the responsible railroad managers and for the statesmen of the country to form some estimate of the capital requirements during, say, the next ten years. It is, of course, impossible to be accurate in making this estimate. Mr. James J. Hill a number of years ago estimated that \$1,000,000,000 per annum would be necessary. Some have estimated that a very much larger amount would be required. Without undertaking to accurately state any amount, it is obvious that the necessary capital requirements to keep the railroads abreast of the times and to provide for the refunding of maturing obligations will be enormous, almost staggering to the imagination. And the question is: Where is this money to come from?”

construction than any year since the Civil War; that while the industrial development of the country is phenomenal, the railroads are standing still, and that the American people will insist on new railroad facilities even if government ownership is necessary to obtain them. Meantime, trade is blocked for lack of cars, locomotives and tracks. Last winter coal lay at the mouth of the mines and grain at way stations while prices soared. To-day the situation is still worse by reason of the war. The railroads cannot handle the traffic. They have not the money and cannot get it. And if the investing public have no confidence now in the credit of the railroads in these days of unprecedented railroad traffic, the prospect of interesting investors in the future is gloomy indeed. It is becoming more and more evident to railroad men, as well as the public, that the money cannot be had in sufficient quantity except in one way, and that way is government aid. I have read carefully your proceedings to this date and fail to find any solution that will really produce the necessary money. On the contrary, Mr. Thom, as counsel for practically all of the railroads, shows that the monetary situation of the railroads is desperate.⁸ All through the hearings of your Committee there is a note of despair on the part of the railroads. Help us or we perish. The volume of traffic is increasing daily, but the railroad facilities to handle that traffic are increasing not at all. Investors are afraid and will not put up any more money. Even if railroad rates were increased, investors would doubt their continuance after the war. As Chatham said: "Confidence is a plant of slow growth in an aged bosom." The railroads say that government aid is imperative. They do not ask a government guaranty, because they say they did not suppose the government would give it.⁹ What happens when the owner of a gas works cannot raise money to increase his plant to keep up with the growth of a city? He is forced by public interest to step aside and make way for someone who can, or else the city takes over the works.

⁸ Pp. 58, 59 of your Record.

⁹ Pp. 246, 247 of your Record.

Now this is a dangerous situation and there seems no way out except by a government guaranty or government ownership. We may not like it, but that is what we are coming to. Furthermore, government aid in some form is right, because the government has already taken almost complete power over the railroads through the Interstate Commerce Commission. The government should guarantee at least 3 per cent dividends on the stock of newly created Federal Railroad Corporations, the stockholders to receive an extra 3 per cent if earned and declared, and all over the 6 per cent should go to the government itself. That would produce the money.¹⁰

Government control: Before considering government control it is well to inquire as to the character of the present private control, bearing in mind that the railroads are great national highways, rivers of commerce, natural monopolies, the control of which naturally belongs to the public. Whom do the present railroad directors in the United States represent?

The stockholders they certainly do not represent. The stockholders no longer attend the meetings. They merely send in their proxies. There are tens of thousands of them living hundreds of miles away from the annual meeting. Personal attendance has become impossible, and, in fact, personal attendance would require a convention hall. The Union Pacific, with its \$321,835,100 of capital stock, holds its annual meeting in Utah; the Southern Pacific, with its \$272,677,905, in Kentucky. Stockholders' meetings have become a legal fiction and a farce. The elections merely perpetuate present control. No one claims in these days that the stockholders really elect the directors.

The *public* is certainly not represented by present railroad directors. The public has nothing to say about them. Not even the different parts of the country are represented by these directors. For instance, the Mississippi Valley has eight great railroad systems with 116 directors. Only 26 of these are

¹⁰ The only place in the United States where railroad extensions are keeping up with the demands of the public is in New York City, where the city furnishes the money by issuing its 4 to 4½% bonds at about par, and the money is used to extend the underground railroad system.

identified with that valley; 88 are in the east. Of these 88 eastern directors, New York has 59, Pennsylvania 16 and Massachusetts 6. And yet these eight railroad systems are the bones of the west—in fact, they are the life blood. Is it right that these boards of directors should be non-residents? Thirty-two years ago President Hadley wrote:

“Where one set of men own a railroad and another set of men use it, the two only coming in contact through the medium of the railroad management, we have a state of things corresponding to the ‘absenteeism’ of Irish landlords, and involving conflicts or dangers of the same kind.”¹¹

Does anyone think that this can continue? John Finley was right when he said, “Democracy, beginning in the Mississippi Valley, is seeking now a perfect impersonal transportation machine.” “An impersonal machine!” That means a great deal. It means that the public shall control. The present control is an intensely personal control. Controlling men vary with the times and requirements. This has been so with the railroad kings. Their necessary characteristics in the beginning were not the same as now. Huntington, Vanderbilt and other pioneer railroad men were big, pugnacious, brainy builders. It was a dominating and even domineering type, not easy to deal with, not always fair. In spots it still exists. Competition was cannibal competition. The management was predatory instead of public, wolfish instead of fair, ruthlessly prehensile. The country looked upon the railroads as pirates. Such presidents as Charles Francis Adams were brushed aside. The Hepburn Investigating Committee in New York uncovered some six thousand discriminations by one railroad alone. Fairness was not the order of the day. Big shippers got cut rates by cunning and graft. Those were the fine free days when “all sorts of rates could be had and all sorts of tariffs could be found.”¹² They found, however, that it does not pay to be unfair. The New York Central Railroad has been trying for years to get a monopoly of railroad freight terminals in New York City. Last spring the legislature stopped it.

¹¹ Hadley on Railroad Transportation, p. 21.

¹² 21 I. C. C. Rep. 347.

But the American people do not harbor resentment, and the present unpopularity of the railroads is due not to that, but to a far deeper cause, namely, that a democracy will not permanently allow a public business to be operated for private profit. This did away with private carrying of the mails, transformed plank roads into public highways, built the canals, created public irrigation ditches, and will take the control of the railroads out of private hands and place them in the hands of the government. The great question is, How shall this be done? I favor control through a Federal Railroad Board described below. About a year ago the National City Bank, the largest bank in the country, in its monthly publication, decried the idea of government aid to the railroads. It now reverses itself and sends up the Macedonian cry of "Come over and help us!" The imperative demand for more money for more railroad facilities is becoming insistent. We are moving swiftly onward. Wall Street says the government should advance \$2,000,000,000 to the railroads. Naturally one asks, on what security? The only available security is the giving up of "control." Is Wall Street willing to pay the price?

The fact is that of present railroad directors, some have inherited their positions; others have come in by a self-perpetuating process; others have taken office by default, the company being in trouble; others have broken in by a coup, and still others represent the bankers. I am speaking of the directors and not of the operating staff. The operating staff has been slowly built up on merit, and on merit alone. The best man to the front, and a wonderful staff it is, but they are operating men, not public men.¹³

Again these directors, as a rule, own very little stock in

¹³ The *Railway Age Gazette* in its issue of October 5, 1917, said:

"The managers of the railways know, first, that there are not many roads in this country that could now, or are likely ever to be able in future to cut melons. They also know that it is most inexpedient for the railways as a whole that those which can do should do so. Unfortunately, the hands of the responsible managers are often forced by men in Wall Street whose avarice is only surpassed by their ignorance of the state of public opinion west of the Allegheny Mountains."

their company. You can easily ascertain the facts as to that by asking the railroads, and they would be illuminating facts.

These directors largely represent the bankers, as they have for twenty years past. The bankers have to raise the money for refunding railroad notes and bonds, and hence it is easy for the bankers to control the railroads. Now, bankers are unfitted to control railroads. They have neither the training nor experience. They occupy a dual and inconsistent position in running the railroads. The greatest financial journal in the world, the London Statist, has pointed this out.¹⁴ New Haven sold at 255 in 1902. It was run by the bankers. It now sells at 26 and is headed for a receivership. They did not loot it. They simply mismanaged it: tried to have it buy all the railroads, steamboats, trolleys and electric lights in New

¹⁴ "Recent events have disclosed latent dangers and drawbacks from so close an association of bankers with railway and industrial enterprises, that errors of management or of judgment are attributed by the public not to the managing staff, or to the entire body of directors upon whom responsibility rests, but to individual banking houses whose representatives are directors of undertakings suffering from misfortune of one kind or another.

"Experience has, in fact, demonstrated that no banking house can perform the double task of carefully and impartially weighing the claims of borrowers of the savings of the investing public and of directing the affairs of every large borrower it assists to obtain capital from the public. It is now realized that for issuing houses to be both bankers and directors means the limitation to a restricted circle of the number of persons who can obtain the capital they need, and that the undertakings lucky enough to secure as directors representatives of the great issuing houses obtain an undue share of the new capital available.

* * * * *

"It is of vital importance to the public welfare that bankers should not be tied up to a limited number of undertakings, but should be able to consider on its merits any and every application for new capital from whomsoever it may be received, in order that all sound enterprises may be encouraged, and that the savings of investors may be safely placed in corporations which offer the greatest security and the most profitable return. It is the duty of bankers to act impartially as between borrowers and investors, and to scrutinize with the greatest care the securities offered and the prices demanded before recommending those securities to the investing public. If, however, bankers are directors of enterprises which need to borrow largely, they unintentionally throw their weight on to the side of the borrower against the investing public."

England. No wonder the present bankers' control is discredited. The public does not trust them to charge higher railroad rates, and will not grant them federal charters, and will not buy their railroad stocks and bonds. The public distrusts them intuitively and instinctively, although not always consciously. That distrust caused the public to insist that the railroads must compete, and the courts held that two competing railroad systems in the northwest could not unite,¹⁵ not even through a holding company,¹⁶ and that a railroad cannot legally control its competitor by stock ownership,¹⁷ and that railroad pools are illegal.¹⁸ Only now, under stress of war and a changing public opinion, is competition between railroads being abandoned, and properly so.

But this will not be allowed permanently unless public control be substituted, to say nothing about the financial necessities of the railroads, which cannot be met except by government aid. How can the change to public control be brought about without full government ownership? The present railroad charters cannot be amended so as to take the voting power away from the stockholders, because that would be unconstitutional.¹⁹

However, Congress may grant federal charters to the railroads. When those charters are drawn the government can retain the right to name the directors. That was what the old federal charter of the Union Pacific Railroad did in part, namely, reserved to the government the right to name five directors.²⁰ The legal possibilities in the drafting of these federal charters I discussed a few months ago in an article in the *Yale Law Journal*, a copy of which I sent you. The proposed Act of Congress, attached to this paper, gives to the government, acting through a Federal Railroad Board, the

¹⁵ *Pearsall v. Great Northern Ry.*, 161 U. S. 646 (1895).

¹⁶ *Northern Securities Co. v. United States*, 193 U. S. 197 (1904).

¹⁷ *United States v. Union Pacific R. R.*, 226 U. S. 61 (1912).

¹⁸ *United States v. Freight Assoc.*, 166 U. S. 290 (1897); *United States v. Joint Traffic Assoc.*, 171 U. S. 505 (2898).

¹⁹ *Lord v. Equitable Life, etc., Soc.*, 194 N. Y. 212 (1909).

²⁰ 13 U. S. Stat. 361 (1864).

power to name the directors in these new proposed Federal Railroad Companies. That Federal Railroad Board, thus dominating the railroad situation, would be nominated by the President and approved by the Senate, very much the same as the present Federal Reserve Board of our banking system. The plan is certainly simple enough and has that precedent, besides the Federal Farm Loan Board,²¹ and the Federal Shipping Board,²² and the Federal Board of War Insurance,²³ and the Federal Board of Food Control,²⁴ with the Government owning a part or all of the stock of such corporations. America is utilizing the corporation to separate the swelling mob of office hunters and grafters from the ever-increasing public administration of *quasi* public and even private enterprises.

The proposed Act of Congress, attached hereto, incorporating federal railroad companies, contemplates acquiring present railroad stocks and bonds by purchase or exchange or condemnation and even acquiring the present railroads themselves by condemnation, if necessary. All this is to be done gradually, to avoid shocks, waste, unfair prices and hasty inexperience. The railroads themselves, however, propose to you that Congress shall pass a law that the present railroads shall take out federal charters at once or else cease doing interstate business on a certain date. This is to be done under the power of Congress to "regulate" commerce. Power to "regulate" \$17,000,000,000 of property is alleged to give power to destroy \$17,000,000,000 of property, by forbidding its use unless it turns itself inside out by accepting a federal charter. That is

²¹ Act of July 17, 1916.

²² Act of September 7, 1916.

²³ Act of September 2, 1914; 38 U. S. Stat. 711.

²⁴ Act of Congress of August 10, 1917. While that Act did not expressly authorize the government to organize and subscribe for the stock of a corporation, yet a corporation was organized in Delaware August 16, 1917, to carry out the purposes of the Act for control and conservation of certain crops. Its entire capital stock of \$50,000,000 is owned by the government. This was done under Sections 13 and 14 of the Act, although it is a little difficult to see how the words of those sections authorize the formation of a corporation and the subscription by the United States Government to its capital stock.

hardly "due process of law." To the ordinary mind it would seem that the penalty of death does not fit the fictitious crime of holding on to a state charter which everybody admits is legal. I realize the desperate situation of the railroads, but I doubt the legality, feasibility or value of this plan of forcing the railroads to take out federal charters.²⁵ I think twenty years would not suffice for the litigation over any such scheme. A charter is a three-phase contract between the state, the corporation and the stockholders. To disregard all three phases of that contract would be revolutionary. Congress can no more violate a contract than the state.²⁶ The decisions referred to by railroad counsel, that the Acts of Congress relative to *uniform* rates may displace pre-existing contracts to the contrary, have little bearing on this proposition of arbitrarily and summarily transferring the title to \$17,000,000,000 of property. And the old corporations are to continue.²⁷ Certainly Congress cannot dissolve them, and hence the new federal corporations will have two charters, one from the state and one from Congress, with inextricable conflict, litigation and Pandora box confusion. The railroads themselves cannot afford to have compound charters. We would still have conflict of state regulation with national regulation; state commissions with the Interstate Commerce Commission; state persecution with national intervention. Many of the railroads already have

²⁵ I doubt the power of Congress to prohibit interstate commerce, except as the equivalent of a police regulation. In the Lottery Case, 188 U. S. 321, the court sustained the stopping of interstate transportation of lottery tickets, but the court was careful to say (p. 362) that this power of Congress "cannot be deemed arbitrary," and cannot infringe rights secured or protected by the Constitution. Even so, four judges dissented. Congress also has power to prohibit White Slave traffic. *Hoke v. United States*, 227 U. S. 308; *Caminetti v. United States*, 242 U. S. 470. Congress may also prohibit transportation of intoxicating liquors. *Clark Distilling Co. v. Western, etc., Ry.*, 242 U. S. 311. But it will be noticed that in all these cases there is an element of police regulation, and, in fact, the Supreme Court said (227 U. S. 323) that Congress in exercising its power over interstate commerce "may adopt not only means necessary but convenient to its exercise, and the means may have the quality of police regulations."

²⁶ *Sinking Fund Cases*, 99 U. S. 700.

²⁷ P. 98 of your Record.

two or more charters in different states. The result is paralysis in some instances. The New Haven cannot mortgage its property because Massachusetts refuses, although Connecticut and Rhode Island are willing. This certainly is a hydra-headed proposition. If state charters continue the states will still claim the right to regulate their own creations. No man can serve two masters. Judge Knowlton suggests that the state railroad charters may be amended by Act of Congress so as to allow a transfer of the corporate property to a federal corporation on vote of the stockholders.²⁸ This is unprecedented and I think unconstitutional. Even if legal, what good would it do if the stockholders refused to vote in favor of the change? A mistake might render due at once all of the bonds of the present railroad corporations; billions in amount. If so, every railroad would pass into a receiver's hands, unless the government assumed the debt.²⁹

Compare this with the simple, safe and gradual process of a federal corporation first acquiring present railroad stocks and bonds by purchase or condemnation and later taking over the railroad properties. The railroads themselves know that merely getting federal charters will not produce the necessary cash. Mr. Thom so stated in his plea.³⁰ Why, then, these makeshifts of the railroads—this bewildered and bewildering

²⁸ P. 1055 of your Record.

²⁹ A somewhat similar problem faced the Canadian Parliament recently when it decided to purchase the stock of the Canadian Northern Railway Company rather than the railroad system itself. The Minister of Finance said: "If the Dominion Government acquired by expropriation the physical assets of the Canadian Northern and the other railways in the system, it would be obliged to find the money to take care of the short date and other indebtedness I have mentioned, or if it failed to find the money to take care of that indebtedness, it would follow that the creditors of the company in respect of the short term and floating indebtedness, would be in a position to appoint a receiver, with the result that the funded indebtedness would at once become due, as to the principal owing under several trust mortgages securing it. The result would be chaos so far as the financial condition of the system is concerned."

³⁰ P. 103 of your Record.

talk?³¹ Apparently it is to escape the clutch of state commissions, and no one can blame them for that. Then, too, federal railroad stocks could not be sold except with a government guaranty, and the railroads are not prepared to give up their present control for such a guaranty. The situation is full of possibilities and, I would add, imperative necessities. Meantime, Canada has adopted the stock-purchasing plan in regard to the Canadian Northern Railway Company.

Is this the same as government ownership? The New York Evening Post, in commenting on the Canadian plan, said that this is "almost the last step short of government ownership and operation of Canadian railways." A professional writer in Collier's, a few months ago, in advocating federal charters for the railroads, referred to my plan as follows:

"Another suggests a Federal holding company for all the railroads of the United States, and makes his suggestion read so cleverly and so ingeniously that you all but forget that he is drawing only a thin veil over government ownership."

This is an easy way of characterizing my proposal. So far from the proposal being a government ownership plan, its sole purpose is to avert government ownership; otherwise I would drop it instantly. And it is not the same as government ownership. Government ownership would mean an additional

³¹ Among other nostrums proposed to your Committee is the issue of shares without par value in the proposed new federal charters to railroads. I have watched that mode of issuing shares for several years, but have failed to discover any public good in it. Apparently it merely renders safe the issue of watered stock. The public mind associates market value with par value. The public neither knows nor cares whether the shares are without par value, but it looks for par value and holds someone morally responsible if the shares are worthless, whether with par value or without. For the reputable promoter shares without par value are unnecessary; for the dishonest promoter they merely enable him to defraud the public safely. Excessive issues of shares would seem to be facilitated by this scheme because there is no limit or restriction on the amount which may be issued for property. Under the old law if a promotor went too far in valuing the property he was liable. Under this new scheme he is not liable at all. The public generally has little idea of the property for which shares are issued, and hence if there is no limit to the number the danger of fraud is greatly increased. Shares without par value add to the mystery while decreasing legal and moral responsibility.

national debt of about \$20,000,000,000. My plan would not. Government ownership would prevent the states from taxing railroad property and would deprive the states of about \$150,000,000 annual income from taxes. This plan would not. Government ownership would give all the powers and direct authority of an owner. This plan gives the government merely the control. Government ownership would be direct administration by the President and his Cabinet. This plan means advisory control, exercised through a gradation of separate bodies, each checking and balancing the other, namely, a Federal Railroad Board, Railroad Directors, General Managers. The English Government is handling its railroads to-day under practically the same plan, and yet no one calls that government ownership. One of the government managers, Mr. Thornton, an American, says that England will not go back to the old system after the war. Again, government ownership would have no stockholders, while my plan contemplates hundreds of thousands of stockholders eager to get 6 per cent instead of 3 per cent, and quick to oppose any invasion of politicians. This plan also contemplates paying each member of the Federal Railroad Board \$12,000 a year, with the possibility of \$62,000 a year if the Board holds down expenses, and keeps out the politicians, and succeeds in paying the guaranteed 3 per cent, the proposal being to pay each of them \$10,000 *extra* for each one of the five federal railroad corporations which pays the 3 per cent. The activity of politicians is best offset by the hope of reward of the managers. As a matter of fact, this plan is a compromise between private ownership and government ownership. As to its being a veil for government ownership, this railroad writer might as well say that the United States own Cuba because it controls Cuba, or that it did own the old Union Pacific Railway because it named part of the directors. President Ripley, of the Atchison, Topeka & Santa Fe Railroad, has recently been quoted as saying:

"I have never ceased to believe that government ownership of the railroads is not merely a possibility but a high probability. The way matters are going the government must step in and take charge

unless meantime some other means of saving the railroads is found."³²

The brilliant work of Yves Guyot, published three years ago, on "Where and Why Public Ownership Has Failed," culminates in a declaration that governments should not own, but should "*control*."³³ That is exactly my contention. The

³² Mr. Markham, President of the Illinois Central Railroad, takes issue as to this statement of Mr. Ripley, and says:

(1) That the interest on government bonds would be only one-half of 1% less than what "strong" railroads must pay, taxes considered. [How many "strong" railroads are there? The statement as to difference in interest is incorrect. The difference would be nearly 3%. The 6% debentures of the New York Central sell to-day at less than par, even though spiced with an option of convertibility into stock.]

(2) That the present consolidated management of the railroads shows what can be done without government ownership. [This statement is correct, but the public will not allow consolidated management to continue after the war, although traffic will go down and expenses stay up.]

(3) That the present war use of the railroads also shows that government ownership is not necessary in that respect. [True, but that ceases with the war.]

(4) That the war debt will be very great without adding \$20,000,000,000 for the railroads. [True, too, but so far as my plan is concerned it does not create an additional national debt.]

Mr. Markham is silent on the crushing fact that the railroads are not raising, and cannot raise, the \$1,000,000,000 fresh money a year necessary to furnish additional railroad facilities to keep up with the growth of the country. Railroad earnings now are great but expenses are fully abreast. Anyone can see what will happen when the war is over and business declines.

³³ P. 438. "First: Neither States nor municipalities should attempt tasks especially adapted to individual effort.

"Second: In the case of those utilities in which the public interest is general, as railways, water, gas, electricity, tramways, etc., there must be a physically and morally responsible body, accountable to the public on the one hand and the service on the other, and protected by contracts against vacillations of public opinion, and the extortionate demands of interested groups, whether employees, consumers or politicians.

"Third: For individuals the watchword should be action; for local and State governments, control."

Mr. Acworth, when he appeared before you in Washington on May 7, 1917, said: "Some day, perhaps, having learned by experience, a parliament and a people may recognize that management for the people

plain fact is that we will have to adopt something like the plan outlined in the bill attached hereto, or go to government ownership. The great, the fundamental, the all-absorbing problem is how to establish non-partisan, non-political public control of the railroads. Canada faces that problem to-day and will soon announce its proposed solution. America will watch the experiment with intense interest. Can a democracy devise a non-partisan, non-political public control of railroads, as it devised the Supreme Court of the United States? Canada inclines towards a self-perpetuating body. I favored that idea in an article written ten years ago, but I fear that such a body would fail to respond to the deep currents of the industrial life of America. Those currents are responded to by the President and the Senate, and may be safely trusted as to a Federal Railroad Board, as they have been trusted in the selection of other boards mentioned above.

Let us now examine some of the perplexing problems of the railroad question and see whether government control is not better than present private control or proposed government ownership.

Wasteful Competition. Competition is a very good thing in trade and manufacturing. But competition between railroads is discredited, first because it refuses to exist, and second, because it is wasteful. In England competition between railroads has been abandoned. George Stephenson, the originator of the railroad locomotive, foresaw this inevitable trend in the railroad business seventy-five years ago. "Where combination is possible," he said, "competition is impossible." For more than thirty years after that Parliament legislated against

is not necessarily management by the people; that there are other branches of government besides the judicial branch, unsuited for popular interference, and may establish a permanent State railway organization, with its own board of directors, with its own separate budget and entirely independent of parliamentary control.

"It would be controlled, like any private company, by a judicially minded commission, and required, also like a private company, to earn dividends for its stockholders, the people. And then a main objection to government railways in a democratic State will have lost its force."

the consolidation of railroads. This legislation proved to be utterly futile. In 1872 a parliamentary committee made an elaborate and exhaustive investigation of the subject. In its report it said that consolidation "had not brought with it the evils that were anticipated, but that, in any event, long and varied experience had fully demonstrated the fact that, while Parliament might hinder and thwart it, it could not prevent it." In America the same irresistible tendency has prevailed. In New England there is no railroad competition left. Elsewhere no more competitive railroads are possible and the trunk lines work together. Even now ninety per cent of the railroads appear as a unit before your Committee. They are surely getting together. They know that railroad competition is waste, besides leading to rebates and discriminations. Even present competition involves an enormous waste.³⁴ Duplicate trains, unnecessary trains, duplicate stations, expensive branch ticket offices, advertisements, and a whole cohort of runners play havoc with railroad balance sheets. Not long ago President Ripley, of the Atchison, said that every night five competing trains start from Chicago for Kansas City, six for Omaha and five for St. Paul, and that probably one for each would suffice.³⁵

³⁴ Wyman on Railroad Valuation and Rates (1916) says (pp. 337, 338):

"Nothing is clearer to-day than that competition in railroad rates between railroads is practically impossible, and not in the interest of the public. A long-continued and expensive experience has proven to the business interests of the country that such competition is not desirable from their standpoint. The only practicable competition is in service, and the plan herein suggested could be made to give much better service than existing conditions admit, because equipment as well as the other facilities could be pooled."

³⁵ Wyman says (pp. 336, 337):

"If the six lines operated between Chicago and St. Paul were all owned by one company, the method of operation would be different, and more economical, than under the present six managements. The Chicago, Burlington & Quincy and the Chicago, Milwaukee & St. Paul have short lines, and for much the greater part of the way they have water grades. The Chicago & North Western has the shorter line but heavier, though not excessive, grades.

"Evidently, through freight traffic can be carried at less unit cost

A combination of all the railroads, such as I propose, would put an end to this. All railroad men agree that the saving would be vast. It may truthfully be said that competition is the bane of the railroads. Thirty-nine years ago Charles Francis Adams wrote:

"We find that railroad competition has been tried all over the world, and that everywhere, consciously or unconsciously, but with one consent, it is slowly but surely being abandoned. In its place the principle of responsible and regulated monopoly is asserting itself."²⁶

Commissions, state and interstate. These have served their purpose well. They have been a sedative for twenty-five years. But they have outgrown their usefulness. The state commissions have become an unqualified, unmitigated nuisance, so far as the railroads are concerned. They have become centers of tyranny, narrow, selfish and destructive. They have few defenders and fewer friends. Practically everybody agrees that they have got to go, and the sooner they go the better, so far as the railroads are concerned. The Interstate Commerce Commission still has some use, but it is breaking down. It is attempting the impossible. Federal charters and a federal board in control could and would dispense with that Commis-

on the Chicago, Burlington & Quincy and the Chicago, Milwaukee & St. Paul than by the other four roads. If the through freight traffic were concentrated on these two lines, practically all of their through freight trains would be filled up to the capacity of the engines, and the whole through freight traffic would be hauled in fewer trains, with fewer train crews, and hence at less expense.

"The same is true as to the passenger traffic. Two or three of the lines would be found able to carry the through passenger traffic at less cost than the others, and such traffic would be diverted to them. There would then be two or three through lines moving through passenger trains, carrying something near their capacity, instead of five lines [the sixth line does not operate through passenger trains], moving more trains, many of which are carrying cars only partly filled, which is the present condition.

"There is a further advantage in such an arrangement, in that during periods of maximum traffic movements the lines not ordinarily employed for the through traffic would be utilized to move the surplus. This would avoid the necessity of constructing additional tracks and other facilities which would be required if one of the lines secured more than its share of the traffic."

²⁶ Railroads, Their Origin and Problems, pp. 204, 205.

sion, or, rather, absorb it as an investigating and consulting body. Commission rule is worn out and is going. The railroad men are urging you to extend it by adding subordinate commissions, but the railroad men do not really want them. The railroad men are trying to get away from the state commissions, which are clutching at their throats and cannot be shaken off except by federal railroad charters. Two cent laws, full crew laws and various other choice assortments of laws, are a part of the state regime, and the Interstate Commerce Commission and Acts of Congress are but little better. Writing twenty-six years ago, Mr. Acworth said that the adoption of

“direct State regulation, of constant and minute interference by a government department * by a series of haphazard and piecemeal decisions * will * land the country quite unexpectedly in a logical *impasse*, from which there can be no outlet, except by State purchase of the entire railway system.”³⁷

We have reached that *impasse*. Mr. Acworth, in an article in the Economic Journal, published in London, September, 1915, said, in regard to the Interstate Commerce Commission:

“In July, 1914, after an inquiry extending over more than twelve months, the majority of that Commission solemnly reaffirmed their refusal of three years earlier to permit the trunk lines to raise their rates. Under the compulsion of gross and palpable fact they reversed that decision some six months later. But it is safe to say that for every dollar Jim Fiske stole from the Erie—and he stole a good many—the inhabitants of the United States lost a million in the months succeeding July, owing to financial depression and trade dislocation consequent primarily on the unintelligent appreciation of the situation by the Interstate Commerce Commission.”

Physical valuation and watered stock. At present, on account of alleged watered stock, the life is being ground out of the railroads by commissions, legislatures and Congress. But is there any water? Up to the present the physical valuation scheme points to no water. Indeed, the increase in terminal values has been so great that the Commission is apparently alarmed, and has decided not to make any complete valua-

³⁷ Preface to “The Railways and the Traders.”

tion of the railroads after all.³⁸ And even if the valuation should fall short, there is no occasion for confiscation. We are infinitely better off than Europe in this respect. In England, when the railroads were built, the Lords who owned the land would not enact a railroad charter until they were paid an exorbitant price for the railroad right of way. American railroads are capitalized at \$62,657³⁹ per mile, bonds and stock included; Great Britain at \$274,562⁴⁰; all Europe at \$121,-

³⁸ At a hearing before the Commission at Washington, January 29, 1917, Mr. Prouty said (p. 45, President's Conference Reprint): "We have decided that the purpose of this Act is not the making of a final valuation, but the marshalling of certain facts out of which a final valuation may be made." The Railway Age Gazette in its issue of September 28, 1917, contains the following:

"Charles A. Prouty, director of the division of valuation, of the Interstate Commerce Commission, has filed a memorandum in the Texas Midland case, stating that while the solicitor's brief covers the legal points involved, the law of valuation is in such a plastic state that the decision of the commission will go far toward fixing the law in many instances, and he therefore confines himself to what he calls the practical considerations involved. Director Prouty says that while he fully concurs in the holding of the solicitor that the valuation act does not require the commission to find an ultimate value, it is still his conviction that an ultimate value for rate-making purposes should be stated, and that the full benefit of this valuation cannot be realized unless this be done. However, he says, this does not mean that any sort of the work now being done, or of the money now being expended, is thrown away because the commission is not required to establish at this time such ultimate value; for the facts are being prepared to be reported to Congress under the present act and a final value can be quickly stated when Congress has determined by whom and possibly by what rule such value shall be determined."

The obvious answer to this is that Congress is disqualified to fix rates, and the main business of the Commission is that very thing.

³⁹ Dunn on Government Ownership of Railroads, p. 32.

⁴⁰ The British railroads "commonly had to incur enormous expenses to get their charters through Parliament, and to pay for land several times its value. It has been estimated that it has cost the British railways \$25,000 a mile to get their franchises from Parliament. To these things is largely due their very heavy capitalization, amounting to \$274,562 per mile." Dunn, pp. 17, 18. Acworth in "The Railways and the Traders," pp. 234, 235, says "the same spirit which prompted, and the same legislation which permitted Lord Petre to levy blackmail on the old Eastern Counties [Railway Co.] to the tune of £100,000 has survived in England from that day to this."

214.⁴¹ In England there is no demand that the "water" be squeezed out. In America the demand comes from the west, which holds few stocks and bonds. But it is well to remember the precept of M. Thiers: "The state must act like an honest man." If physical valuation should show there is no "water" at all, it would be poetic justice. But in any case, the above figures show that to recognize the validity of present railroad stocks and bonds by absorbing them at their present actual value into new federal railroad charters is not a radical proposition. In the recent debate in the Canadian Parliament relative to buying the stock of the Canadian Railway Company, the storm center was not the plan, but the price. There, as here, it was asserted that the stock was all water. There, as here also, it was claimed that the stock had no value. Certainly the Commission had so reported. The government, however, thought it better to pay something for the stock than to adopt government ownership.

Labor. This is an unsolvable problem for present control. First, the railroad unions force higher wages; then Congress raises them still higher. The railroads are helpless. The reason is that the public has no sympathy for them. All that the public demands is that traffic shall not be stopped. There is but one way of regulating this railroad labor trouble. That way is to enlist public sentiment in favor of fair wages; no more; no less. That public sentiment can never be enlisted while present control continues. If, however, a Federal Railroad Board, representing the public, were in control, I venture to say that public sentiment would quickly insist on labor getting its just deserts. A great strike never succeeds as against public sentiment. I am aware that government-owned railroads are forced by labor votes to increase wages, but the plan herein set forth is designed to separate the voters so far from the control that the voters would have many bulwarks to surmount before they could increase wages, build unnecessary railroads, give unnecessary service or break down the

⁴¹ Dunn, p. 43.

discipline and economy of the railroad system. Nor does this mean unfairness towards railroad labor. High wages is an essential principle of American life. Unfortunately, foreign cheap labor produces cheap goods, which in times of peace undersell American goods, and that forces American labor, including transportation, down to a competitive basis. Then, too, labor is like the ocean, ceaselessly seeking an equilibrium. Labor adjusts itself. It rises here and falls there, higher now and lower then, beyond the power of man to control, but following always, sooner or later, the immutable law of supply and demand.

Present investments as affected by this plan. Do not imagine that I propose that present railroad stockholders shall turn in their stock for new 3 per cent guaranteed stock share for share. Some of the present stock is worth more, some less than the 3 per cent guaranteed stock. The exchange would be made in each instance on a basis fixed by the Federal Railroad Board. Nor would present stockholders be required to exchange at all. They could refuse, and then the Federal Railroad Corporation, if it desired the stock, would have to condemn and pay to the present holder the full value of the stock in cash. That prospect is certainly better than the present prospect. Things are getting worse instead of better. Railroad stockholders should realize that their present directors have made a failure of their management. A new deal is necessary if the investors are to save their investments. They have from \$17,000,000,000 to \$20,000,000,000 already in and \$1,000,000,000 a year sought for. They have on their hands a group of directors who are distrusted by the public. Until that distrust is removed the investment is unsafe. The investors' only hope is to substitute public control that will allow higher rates and check higher expenses, especially those due to regulation. This can never be brought about by the present control. Anyone can see that. In order to get fresh money and protect money already in, government aid is imperative, just as the European Allies now get American money, through the American Government, at 3½ and 4 per cent, formerly

obtained with difficulty at $5\frac{1}{2}$ and 6 per cent, and just as the Canadian railroads are turning to the government for aid.

Government ownership. I shall not discuss this at length. Government ownership would have its advantages. It would furnish the necessary fresh money, stop state regulation, abolish the Interstate Commerce Commission, end discriminations and rebates, save the waste of competition, and end the present conflict between the public and the railroads.

My plan would equally well accomplish all this.

But government ownership would have its disadvantages, and some of them are insuperable. It would be a political machine and our republican institutions could not stand that strain; it would give bad service, unnecessary service, make undesirable extensions and be subject to labor unions. It would create an additional \$20,000,000,000 debt, and in addition there would be an annual deficit in operation. It would deprive the states of about \$150,000,000 annual income from taxes.

I believe my plan would avoid all this. The railroads are opposed to the plan because they want to continue as they are. They ignore it and concentrate their efforts on attacking government ownership, as though that were the only alternative to the present private control. They refuse to believe what all thinking men now see is inevitable, namely, that public control in some form or other is bound to come within the next few years, inasmuch as the railroads cannot get the money which they must have. They no longer have the confidence of the public and cannot get it. Financial aid must come from the government and with it will come some form of public control. Meantime there is chaos in railroad financing, maintenance and management.

Yours respectfully,

WILLIAM W. COOK.

PROPOSED ACT OF CONGRESS

AN ACT TO PROVIDE FOR THE CREATION OF FEDERAL RAILROAD COMPANIES,
TO ESTABLISH A MORE EFFECTIVE SUPERVISION OF RAILROADS IN THE
UNITED STATES, AND FOR OTHER PURPOSES.

Section 1—Wherever the words "Federal railroad company" are used in this act the words shall be construed to refer to each of the five corporations to be organized under this act as herein provided.

The words "Federal Railroad Board" used in this act shall be construed to mean the board of six members herein provided for.

The words "Secretary of Railroads" used in this act shall be construed to be the head, at the seat of Government, of an executive department to be known as the Department of Railroads, said head to be appointed by the President, by and with the advice and consent of the Senate. Said appointee shall receive a salary of \$12,000 per annum and his term and tenure of office shall be uniform with other members of the Cabinet.

FEDERAL RAILROAD DISTRICTS

Sec. 2—Continental United States, excluding Alaska, is hereby divided into five districts, to be known as New England railroad district, Central railroad district, Southern railroad district, Northwestern railroad district and Central Pacific railroad district.

The New England railroad district shall include the New York, New Haven & Hartford Railroad system and all other railroads in Maine, New Hampshire, Vermont, Massachusetts, Rhode Island and Connecticut not controlled by any railroad system in another Federal railroad district.

The Central railroad district shall include the Pennsylvania Railroad system, New York Central Railroad system, Erie Railroad system, Baltimore & Ohio Railroad system, Chesapeake & Ohio Railroad system and all other railroads in the States of Illinois, Indiana, Ohio, Michigan, Pennsylvania, New Jersey and New York not controlled by any railroad system in another Federal railroad district.

The Southern railroad district shall include the Southern Railroad system and Illinois Central Railroad system and all other railroads in the States of Delaware, Maryland, Virginia, North Carolina, South Carolina, Georgia, Florida, Alabama, Tennessee, Kentucky, West Virginia and Mississippi and the District of Columbia not controlled by any railroad system in another Federal railroad district.

The Northwestern railroad district shall include the Chicago, Milwaukee & St. Paul Railroad system, the Chicago & Northwestern Railroad system, the Northern Pacific Railroad system, the Great Northern Railroad system and all other railroads in the States of Wisconsin, Minnesota, North Dakota, South Dakota, Montana, Wyoming, Idaho, Oregon and Washington not controlled by any railroad system in another Federal railroad district.

The Central Pacific railroad district shall include the Union Pacific Railroad system, the Atchison, Topeka & Santa Fe Railroad system, the Southern Pacific Railroad system and all other railroads in the States of Iowa, Nebraska, Kansas, Missouri, Arkansas, Louisiana, Texas, Oklahoma, Colorado, New Mexico, Arizona, Utah, Nevada and California not controlled by any railroad system in another Federal railroad district.

Any question which may arise as to whether a particular railroad is included within any particular Federal railroad district shall be decided by the Federal Railroad Board.

FEDERAL RAILROAD COMPANIES

Sec. 3—The Federal Railroad Board shall supervise the organization in each of the said districts of a Federal railroad company by nine individuals in each district selected by the Federal Railroad Board, and thereupon such individuals in each district shall under their seals make an organization certificate which shall specifically state the name of such Federal railroad company, the territory and extent of the district as defined by States in Section 2 of this act, the city and State in which its principal office is to be located in said district, the amount of capital stock (\$9,000), and the number of shares into which the same is divided (\$10 each), and the number of shares subscribed for by each incorporator (100). The said organization certificate shall be acknowledged before a judge of

some court of record or notary public; and shall be, together with the acknowledgment thereof authenticated by the seal of said court or notary, transmitted to the Secretary of Railroads, who shall file, record and preserve the same in his office. Upon the filing of such certificates with the Secretary of Railroads as aforesaid, each of the said Federal railroad companies shall become a body corporate, and as such and in the name designated in such organization certificate, shall have power:

First—To adopt and use a corporate seal; to have succession in perpetuity, unless it is sooner dissolved by an act of Congress or unless its franchise becomes forfeited by some violation of law; to make contracts; to sue and to be sued in any court of law or equity; to appoint by its board of directors such officers and employees as are not otherwise provided for in this act, to define their duties, require bonds of them and fix the penalty thereof, and to dismiss at pleasure such officers or employees; to prescribe by its board of directors by-laws not inconsistent with law, regulating the manner in which its general business may be conducted, and the privileges granted to it by law may be exercised and enjoyed; to exercise such incidental powers as shall be necessary to carry out the purposes of this act.

Second—To acquire, hold and exercise the power of ownership of any or all of the shares of the capital stock and bonds and other obligations of any or all railroad companies within its district as aforesaid; also to construct, acquire, maintain and operate railroads within its district; also to issue shares of its capital stock from time to time, either for cash or in exchange for shares of stock or bonds or other obligations of any and all railroad corporations within its district, on such basis of exchange as may be authorized by its board of directors; also to issue shares of its capital stock from time to time for such purposes (including its own expenses and disbursements) connected with or incidental to the control, acquisition, construction, management, use and development of railroads, railroad business and railroad stock, bonds or other obligations already issued or hereafter to be issued by railroad companies within its district (including the issue of Federal railroad company stock, to provide money to enable any railroad company in its district to pay or purchase outstanding obligations or to pay for past or future improvements, equipment or extensions, stock of such railroad company being issued to the Federal railroad company in consideration of such money), as may be determined by its board of directors; also to exercise the power, which is hereby given to it, of eminent domain, to acquire any shares of the capital stock or bonds or other obligations of any and all railroad corporations within its district or to acquire any railroads themselves or railroad property or property for railroad purposes, in its district whenever in its opinion it is necessary or advantageous to it to do so by condemnation under judicial process, and the United States District Court or courts of the district wherein such stock or property is located shall have jurisdiction of proceedings for such condemnation. The practice, pleadings, forms and modes of proceedings in causes arising under the provisions of this act shall conform, as near as may be, to the practice, pleadings, forms and proceedings existing at the time in like causes in the courts of record of the State within which such District Courts are held, any rule of the court to the contrary notwithstanding.

Third—To vote its own holdings of stock and to solicit proxies from other stockholders to vote their holdings of stock in any railroad corporation in its district, and such vote of such stock and proxies by the Federal railroad company for directors in said railroad corporation or corporations shall be limited to persons who shall have resided within the district for at least nine months in each of the five years prior to the election, and have been actively engaged during said five years in the district in commerce.

agriculture or some other industrial pursuit, or in the practice of a profession.

Sec. 4—At least six members of the board of directors of each Federal railroad company shall for at least nine months of each of the preceding two years have resided in the district in which they have been chosen directors. No Senator or Representative in Congress shall be an officer or director of a Federal railroad company. No director of a Federal railroad company shall be an officer, director or employee of any other railroad company. Any director of any Federal railroad company may be removed at any time for cause by the Federal Railroad Board. The board of directors of each Federal railroad company shall consist of nine members, all of whom shall be appointed by the Federal Railroad Board. Protests by stockholders or by the public shall be open to public inspection. Vacancies from any cause in the boards of directors of any Federal railroad company shall be filled by the Federal Railroad Board. The directors of each Federal railroad company shall receive such compensation as the board of directors may determine in advance in each instance, subject to the approval of the Federal Railroad Board. The board of directors of each Federal railroad company shall at its first meeting (after its first board retires from office) designate three directors to serve one year from the next first day of January, and three for two years, and three for three years, and thereafter all directors shall hold office for three years. Each Federal railroad company shall every three months make a full report of its operations to the Speaker of the House of Representatives, who shall cause the same to be printed for the information of the Congress.

STOCK ISSUES AND GUARANTY OF DIVIDENDS

Sec. 5—The capital stock of each Federal railroad company shall be divided into shares of ten dollars each. The outstanding capital stock may be increased from time to time as authorized by the board of directors. When the capital stock of any Federal railroad company shall have been increased, the board of directors shall cause to be executed a certificate to the Secretary of Railroads showing the increase of capital stock. The shares shall be represented by certificates which shall be transferable.

Sec. 6—Dividends on the stock of each Federal railroad company shall not exceed 6 per cent.

Sec. 7—The United States Government hereby guarantees the payment of 3 per cent dividends on the shares of the stock of the several Federal railroad companies, and the Secretary of the Treasury is hereby authorized and directed to sign the name of the United States of America to a guaranty to that effect on the face of the certificates of stock issued by the corporation (the guaranty on cancelled certificates to be cancelled when the certificates are cancelled by transfer), the form of said guaranty to be as follows:

“The United States of America hereby guarantees to the record holder of this certificate of stock the payment by the Federal railroad company issuing the same 3 per cent annual dividends on the shares of the capital stock represented by this certificate payable semi-annually on the first days of January and July of each year after the date of this guaranty.

“If at any time the United States of America by Act of Congress ceases to pay said guaranty, the United States of America shall pay to the holders of said certificates of stock the price at which they were originally issued or the value at the time of issue of the property for which they were originally issued.”

The said guaranteed rate of dividend may be varied by Congress from time to time, but not as to any issue already made.

Sec. 8—The United States Government shall be entitled to all the profits of the several Federal railroad companies in excess of said 6 per cent dividends, and shall apply such excess profits to extensions and

improvements, or purchase of railroad bonds or stock, or reduction of rates, or retirement of stock issued hereunder, or for any other purpose said Government may deem best in connection with the railroads.

Sec. 9—National banks and Federal reserve banks may invest and deal in the shares of stock of the said Federal railroad companies or any of them, and such shares may be transferred to and deposited with the Treasurer of the United States in lieu of United States bonds as prescribed by sections 5159 to 5189, inclusive, of the Revised Statutes of the United States as amended and by Section 4, sub-division "Eighth" of the "Federal Reserve Act," and may be deposited with the Treasurer of the United States as security for deposits by said Treasurer of funds of the United States in national banks, and may be deposited as security for and in accordance with the Act of Congress of May 30, 1908, amending the national banking laws. The board of trustees, established by Act of Congress of June 25, 1910, to establish postal savings depositories may invest postal savings funds in such shares as securities of the United States within the meaning of that act. Said shares of the capital stock of said Federal railroad companies or any of them shall be receivable at par as a satisfactory collateral security for Federal reserve notes and as a reserve available as eligible paper under the Federal Reserve Act and as investments by Federal reserve banks.

Sec. 10—The Federal railroad companies shall proceed with all reasonable despatch to acquire sufficient of the outstanding capital stock of the Pennsylvania, New York Central, Illinois Central, Chicago, Milwaukee & St. Paul, Chicago & Northwestern, Union Pacific, Atchison, Topeka & Santa Fe and Southern Pacific Railroad systems, to control those railroad companies; each Federal railroad company so to acquire the stock of any said railroad system or systems within its district. Such acquisition may be by purchase or by exchange of Federal railroad company's stock for the stock of said railroad system or systems, or by condemnation proceedings.

FEDERAL RAILROAD BOARD

Sec. 11—A Federal Railroad Board is hereby created which shall consist of six members, one to be the Secretary of Railroads and the remaining five members to be appointed by the President of the United States, by and with the advice and consent of the Senate. In selecting the said five members of the Federal Railroad Board not more than one shall be selected from any one Federal railroad district. The said five members shall devote their entire time to the business of the Federal Railroad Board and shall each receive an annual salary of twelve thousand dollars, payable monthly, together with actual necessary traveling expenses. In addition to the salaries hereinbefore provided for, each of said six members shall each year receive ten thousand dollars for each and every one of said five Federal railroad companies which pays its guaranteed dividend without resort to the guarantor, each year being taken by itself. No Senator or Representative in Congress shall during his term of office, or for five years thereafter, be a member of the Federal Railroad Board. The members of the said board shall be ineligible during the time they are in office and for two years thereafter to hold any office, position or employment in any railroad company, and shall not, during that time, hold or own stock therein. At least one of said five members shall be a person experienced in the management and operation of railroads. One member shall be designated by the President to serve for two years, one for four, one for six, one for eight, and one for ten years, and thereafter each member so appointed shall serve for a term of ten years unless removed for cause by the President. Whenever a vacancy shall occur, whether by expiration of term or otherwise, among the said five members of the Federal Railroad Board, a successor shall be appointed by the President with the advice and consent of the Senate to fill such vacancy. The President shall have power to fill all vacancies that may occur on the Federal Railroad Board during the recess of the Senate by granting commissions which shall

expire thirty days after the next session of the Senate convenes. Of the five members thus appointed, one shall be designated by the President as Governor and one as Vice-Governor of the Federal Railroad Board. The Governor of the Federal Railroad Board, subject to its supervision, shall be the active executive officer. A majority of the members at a meeting duly called shall constitute a quorum and a majority of those present at such meeting shall be sufficient for affirmative action. The salaries and expenses of the Federal Railroad Board shall be paid by the Federal railroad companies in proportion to the respective outstanding capital stock of each from time to time. The Federal Railroad Board shall annually make a full report of its operations to the Speaker of the House of Representatives, who shall cause the same to be printed for the information of the Congress. The Federal Railroad Board shall have power to examine at its discretion the accounts, books and affairs of each Federal railroad company and to require such statements and reports as it may deem necessary, and shall at all times furnish full information to the public regarding its operations and the operations of each Federal railroad company.

Sec. 12—Said Federal Railroad Board is hereby given the power to fix and determine all interstate railroad rates and service, and also such intrastate rates and service as Congress has power to regulate under the Constitution of the United States. No State or State commission or other State authority shall fix, determine or regulate any rates, service or operation of railroads owned by any of said Federal railroad companies.

Sec. 13—No stock shall be issued by any Federal railroad company except after the approval thereof by the Federal Railroad Board, which board shall also first approve the use to be made of such stock and the terms of its issue. All financial operations of every Federal railroad company shall be approved by the Federal Railroad Board before becoming effective.

Sec. 14—This act may be altered from time to time or repealed.

Inasmuch as Mr. Acworth, of London, has appeared before your Committee and given very valuable testimony, it may interest you to read the following reprint of an article by him in "The Economic Journal" of March, 1916, relative to my idea:

A New Project of Railway Control in the United States

By W. M. ACWORTH

The present writer has often said that the strongest argument for the nationalization of railways is that, if not nationalized, they must be controlled by the State; and that, so far, no State has worked out a reasonably satisfactory system of control. A few years ago it looked as though such a system might be worked out in the United States. But unfortunately they began too late. And before the wise people could make their work effective, the shortcomings of the companies in various directions—a bad breakdown of the operating organization, a series of disastrous accidents, not a few financial scandals, and so forth—and, finally, the dread that Wall Street control, as typified by the late Mr. Harriman, would establish an *imperium in imperio*, swept the public off their legs; and the fools rushed in, with the politicians of the baser sort at their head, and proceeded to smash the machine. At the present moment it would be difficult to find a human being throughout the length and breadth of

the States who is satisfied either with the methods of railway regulation at present in force or with the results that they have achieved. The recent appointment, at the urgent insistence of President Wilson, of a Congressional Commission to investigate the whole subject is one sign of the public disenchantment. Another may be found in a paper contributed to the *Michigan Law Review* of November last by a distinguished company, or, as they say in America, "corporation" lawyer, Mr. William W. Cook.

Mr. Cook is not only Standing Counsel to a group of cable and telegraph companies, but also the author of the standard textbook, *Cook on Corporations*. Mr. Cook says straight out, "Commission regulation as a complete and final remedy is an absolute failure." He proposes a sweeping change: in effect that the Federal Bank plan should be applied to the railroads. And he has drafted a bill showing the manner in which his idea might be brought into force by Congress. In outline his scheme is as follows: There would be formed five Regional "Federal Railroad Companies." The five regions would be: (1) New England; (2) what is now known as Trunk Line Territory, namely, the whole of the country north of the Ohio and the Potomac that lies between the Atlantic and the Mississippi; (3) the southeast of the Mississippi; (4) the southwest; and (5) the northwest.

Each company would issue sufficient of its own stock, which would be guaranteed a fixed rate of dividend by the United States Government, to enable it to acquire by purchase a controlling interest in the stock of the railroads within its territory. Owning a majority of the stock of the Pennsylvania Railroad, for instance, the Federal company would elect the directors of that company and control its policy, just as the Pennsylvania Railroad itself at this moment appoints the directors and controls the policy of the Pennsylvania Company, the Pan-Handle, and the scores of other corporations that nestle under the widespread Pennsylvania wings. The Board of Directors of each Federal Railroad Company would consist of nine, three appointed by the Federal Railroad Board, hereafter mentioned, and six selected by the stockholders of the Federal Railroad Company, who would be required to be residents within the district.

Mr. Cook points out quite fairly that his plan can be introduced gradually. Not only can each district be taken in hand separately, but there is no need to acquire the majority of the stock of all the railroads in the district immediately. The control of the New Haven road, for instance, would practically mean control of New England. And control of the Pennsylvania Railroad and the New York Central would practically mean control of the whole of the Trunk Line Territory. Mr. Cook makes a startlingly strong point in favor of some change in the present system when he points out that, on the one hand, the Mississippi Valley contains half the States of the Union, and is in both area and population more than half the country; while, on the other hand, out of 117 directors of the eight great systems connecting the Valley with the outside world, twenty-three are identified with the Mississippi Valley, while ninety-two are resident in the States bordering on the Atlantic seaboard. It may be fairly

answered from a company point of view that the directors represent the owners of the railroad stock. But can one be surprised that this answer does not satisfy the inhabitants of the Valley? May it not well be that this absentee ownership, typified, often unjustly, to the ordinary plain citizen by the bogie of "Wall Street," is still, as it was in the days of the Granger laws, the root cause of the hostility of the West to the railroads?

Mr. Cook's proposed Federal Railroad Board would be not a company, but an organ of the Government. It would consist of six members, five appointed by the President of the United States with the approval of the Senate, and the sixth, the Secretary of Railroads, a new member of the Cabinet. It would be apparently in Mr. Cook's scheme the one regulating authority, superseding the Interstate Commerce Commission, for it would fix and determine all interstate railroad rates and service and approve all issues of stock and the proposed financial operations of every Federal Railroad Company.

Mr. Cook's scheme, novel and revolutionary though it be, certainly deserves respectful consideration. And it will doubtless receive it from the newly-constituted Congressional Commission. Financially, it is sober and conservative; for there would be no need for any great sums of money, as presumably a very large number of shares of the existing railroads would be gladly surrendered to the Federal companies in exchange for their own stock. And it is certainly arguable that the working out of the scheme might even show a financial surplus. Moreover, the principle of Government control by means of stockholding was in practical effect in Mexico for a good many years, and looked like being quite a success till government in Mexico went to pieces. Certain criticisms seem obvious. Can forty-five directors plus six supervisors really direct 250,000 miles of railroad? Will not the various districts fight each other? Texas has notoriously enacted local protection by means of its Railroad Commission. And other States have done the same, to a less frequent extent. Might we not well see the Southern Federal Railroad Board, for instance, elected on a ticket of protection of Birmingham, Ala., against the competition of Youngstown and Pittsburg? Most serious of all—and Mr. Cook has attempted to provide against the danger—is this: Is it to be hoped that the appointments for Federal Boards and Federal Directorate could be kept out of politics? And has any dispassionate outsider, however badly he may think of railroad men, ever rated the average American railway man, either in intellect or integrity, as low as the average American politician? Jay Gould was an exceptional phenomenon. He died very many years ago, and, as a journalist wrote next morning, "is still dead." But Tammany still lives and flourishes. And the methods and morals of Tammany are still not without frequent and successful imitators outside New York. Unless Mr. Cook felt sure that his scheme would keep the railroads out of politics, in the American sense, we feel sure that he himself would not be among its advocates. And as we do not ourselves feel sure, we fear that his remedy would be worse than the disease. Undoubtedly the disease is serious. Undoubtedly a remedy, and a drastic one, must be found. For the American people, who have for some years been busily engaged in throttling their railroads, are already discovering that they have at the same time been throttling the prosperity of their country.

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