

BOOK REVIEWS

TRANSFORMING PUBLIC UTILITY REGULATION. By John Bauer. Harper & Bros., New York, 1950. Pp. xi, 367. \$5.00.

For more than three decades Dr. John Bauer has been a diligent student of public utility economics. During that period no one has done more than he to penetrate the fog of regulation and to bring to the problem an incisive and penetrating analysis. And, despite any criticism of his theories and his regulatory views, he has at all times been provocative to thought and has consistently championed the side of the consuming public in matters concerning public utility operation. This latest book by Dr. Bauer reflects a trained intelligence which has been enriched by experience. No student of public utilities, whatever his economic views or his emotional predilections, should fail to give serious thought and consideration to the views expressed here.

So much of what Bauer says is sound and constructive that the reviewer is reluctant to adopt a critical attitude. But progress in controversial fields lies in an attempt to distil truth out of the crucible of divergent views. Limitations of space make it necessary to pass hurriedly over the contributions Bauer has made and to concentrate on matters which are open to question. At the risk of seeming ungracious, I shall concentrate on these controversial aspects of the book.

Bauer divides his book into two principal sections. In the first section, he reviews utility regulation of the past and attempts an explanation for the failures to give adequate protection to the public interest. In the second part of the book, he gives his blueprint for adequate regulation, made possible now, he claims, by recent decisions of the U. S. Supreme Court, especially that in the *Hope* case of 1944.¹ Bauer states categorically that he prefers "outright public organization of actual public functions" (p. vii), but that effective regulation of private utilities is a workable alternative if his pattern becomes the accepted basis for control. If the acceptance of his proposals is the only means to avoid public ownership, it is entirely probable that Dr. Bauer will get his first choice, because his plan has little chance of adoption and, if accepted, would, in the opinion of this reviewer, prove unworkable.

Few will be inclined to disagree with Bauer's conclusion as to the objective of regulation: "The basic objective is to provide proper service at minimum available cost, so as to promote maximum economic and social advancement in the localities served, and for the county at large" (p. 19). Nor will students of economics dissent from the analysis of the reasons for inadequate regulation of the past, namely, the absence of

1. *FPC-v. Hope Natural Gas Co.*, 320 U.S. 591 (1944).

established standards, the selection of incompetent members of regulatory commissions for political reasons rather than for demonstrated capacity, niggardly appropriations from legislatures which have produced technical staffs inadequate in number and in competence and, perhaps most significant of all, the judicial emasculation of constructive administrative policies and programs.

Bauer shows effectively the degree to which decisions of the courts have hampered adequate regulation. Most of the leading cases are analyzed in such manner as to leave little doubt that the consumer has frequently become the sacrificial lamb to corporate gain. With so comprehensive a discussion of the role of the judiciary, it is difficult to understand a number of significant omissions. First, Bauer shows that the regulated company can appeal to the courts upon the allegation of a violation either of the Fifth or of the Fourteenth Amendments to the Federal Constitution. If, for example, the state courts decide against the utility, the case can be appealed to the federal courts upon a claim of a violation of property rights. But Bauer fails to show that, in contrast with the utility which has two strings to its litigation bow—state courts and federal courts—the consuming public, if the case is lost in the state courts, cannot appeal to the federal courts because, rightly or wrongly, the courts have held that the consumer has no property right in utility service. Hence, if the public loses in the state courts, that is the end of the matter.

Missing also is a discussion of the *West* case,² in which the Supreme Court rejected the use of index numbers in an attempt to establish a rate base. This omission is all the more strange in view of the fact that Bauer indicates (pp. 157, 168) the desirability of adjusting rate bases by index numbers in cases of serious inflation or deflation. True, there were other factors in the *West* case, but, so far as this reviewer knows, this case is the only one in which the Court has expressed itself as to the acceptability of index numbers for this purpose.

The third significant gap in the analysis of court decisions arises from the failure to discuss the so-called *New York Telephone* case³ in which the Court closed the door to the recovery by the public of any excessive charges that had been camouflaged as depreciation. Here, it will be recalled, the court held that excessive charges in the past did not warrant inadequate payment in the future any more so than inadequate collections of the past gave justification to added charges in the future.⁴ True, this long-accepted principle has been weakened somewhat by court sanction for so-called "temporary" rates and by such devices as the "sliding scale" of rates. In the main, however, accepted legal doctrine points to the necessity, if all groups are to be protected, of computing depreciation as an operating expense with a high degree of accuracy.

2. *West v. Chesapeake & Potomac Tel. Co.*, 295 U.S. 662 (1935).

3. *Board of Public Utility Comm'rs v. New York Tel. Co.*, 271 U.S. 23 (1926).

4. See *Galveston Elec. Co. v. Galveston*, 258 U.S. 388 (1922).

In this analysis of depreciation Bauer is less than convincing and, apparently, not entirely clear in his own views. Despite the fact that he insists upon prudent investment as a rate base, he makes considerable concession to those who lament the limitation of the depreciation charge to an amount necessary to recover investment, a concession inconsistent with his major premise. "Management and the commission should closely watch replacement needs during periods of rising prices and costs, and use their reasoned judgment as to whether to include in operating account supplementary provisions . . ." (p. 263). This reviewer has shown elsewhere⁵ why he believes this view both economically unsound and inequitable. Bauer seems to regard the function of depreciation that of replacing the plant rather than that of recovery of the investment.

Likewise inconclusive is the assertion that, in general, small and medium sized utility consumers have been discriminated against (p. 270). As a matter of fact, if cost rather than some sociological standard be accepted as the beginning for rate fixation, most informed regulators would insist that it is the very small consumer who is subsidized. In many instances the minimum monthly charge, especially with gas companies, is less than the service cost imposed upon the utility. Possibly on grounds of public relations or of political expediency this subsidy can be defended. But this does not alter the fact that subsidy there is.

Another generalization of doubtful validity is Bauer's claim that telephone rates have discriminated against subscribers in densely populated sections, such higher charges having been defended upon the theory of the value of service rendered, a theory which Bauer holds not to have been proved. Does one need proof to show that a subscriber on an exchange with one thousand stations has a wider range of service than does one on an exchange with only one hundred stations? But more significantly, it is generally believed that the telephone industry is unique among utilities in that increasing unit costs accompany an increased number of subscribers on any one exchange. In that event, perhaps a better basis for the higher charge to the urban than to the village subscriber can be found in costs, not in the value of the service.

The essence of Bauer's program is that the rate base, now that the Court has spoken in the *Hope* case, be definitely the net investment in the plant and that the rate of return be fixed so as to pay interest on bonds, dividends on preferred stock, and a definite, rather than a fluctuating, dividend on common stock. In his blanket approval of the *Hope* decision, Bauer fails to show that the Court, as well as the Federal Power Commission, reached a verdict in which conflicting conclusions were accepted.⁶ Apparently Bauer approves the elimination from the rate base of some 17 million dollars that had actually been expended in drilling, but which

5. Fisher, *Should Price Levels Affect Depreciation Accrual?*, 45 P.U. FOR. 683 (1950).

6. See Fisher, *State Public Service Commissions Comment on FPC Decision by U.S. Supreme Court—Connecticut*, 93 GAS AGE 26 (1944).

had been charged to and recovered as an operating expense; likewise, he approves the deduction from investment of a sum equal to accrued depreciation rather than the much larger sum reflected in the depreciation reserve, despite the fact that all the depreciation reserve, like the 17 million charged to drilling, had been recovered as an operating expense. In the language of an old negro philosopher whom I knew in my youth, "Consistency, thou art a plumb daisy." Obviously the "end result" is a nebulous conception if what constitutes a fair return on the 30 million dollar plus rate base is identical with what would be proper if another 17 million were added and the rate base were fixed as 50 million dollars. One may well question whether this decision has contributed to the program to make utility regulation definite, as Bauer believes.

The objective of a definite rate base is again complicated by an apparent willingness on the part of the author to have the base modified so as to take account of inflation or of deflation (pp. 157, 168), index numbers being used for this purpose. While there may be good arguments for such adjustment, a definite rate base of fixed dollars is not one of them.

The most significant proposal made by Bauer is that the rate of return, that is, the dividend payable to common stock be made a definite, stipulated sum of money (pp. 167, 172, 174, 199, 209). In an illustrative case (p. 213), he gives a capital structure consisting of 3% bonds, 4% preferred stock and 5% common stock. Rates would be fixed in such manner as to enable the company to pay the 5% dividend on common, rates being raised or lowered as circumstances might require. The 5% dividend on common would be secured by the establishment of a dividend equalization reserve that would not become a part of the rate base.

The "64 dollar" question is to find investors who would purchase such common stock. Further, would bond holders and preferred stock holders be content to invest money, the interest and the dividend on which had a covering so narrow as suggested? Of even more significance, what assurance is there that an adjustment of rates would produce the desired amount of revenue? Does Bauer not envision a mature but a static economy, not the dynamic economy that has evolved in the United States and in which obsolescence of plant and of community has been a frequent occurrence rather than an exception? How does Bauer know that investors would place funds on his proposed basis?

This suggestion becomes more questionable upon the admission by Bauer that it might not work in such cases as that of street railway transportation and perhaps of manufactured gas (p. 224). How does he know that new discoveries may not place electric utilities in a similar category? What will atomic energy do to the investment in generating plants? What may not develop in the form of much improved diesel engines that will eliminate the necessity for high cost distributive systems? Is it assumed that the investor, without the compensating higher return presently offered by successful ventures, to say nothing of the possibility of declining communities in which the traffic will not bear higher charges, will release

his funds in the face of such hazards? Furthermore, the whole problem of incentive on a rigid cost plus system raises numerous questions which space does not permit one to discuss. Bauer may solicit funds from common stockholders, but the reply may well be the one given by Hotspur when Glendower boasted that he could call "spirits from the salty deep." "So can I, but will they come?" Any acceptance of the plan of this book will lead to a situation in which Bauer may well get indirectly what he prefers, public ownership and operation, by the mere fact that under present conditions of change and uncertainty the common stock investor will decline to accept this honor bestowed upon him and there will be no alternative to government financing. In other words, "transforming public regulation" may mean a transformation of a segment of the economy from private to public ownership.

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LAWYERS' TAX MANUAL—PROCEDURE, TRANSACTIONS, FORMS. By Alfred S. Pellard. Clark Boardman Company, Ltd., New York, 1949. Pp. xxiii, 582. \$10.00.

SUCCESSFUL TAX PRACTICE. By Hugh C. Bickford. Prentice-Hall, New York, 1950. Pp. xx, 428. \$5.65.

Here are two books which should be welcome additions to the library of every general law practitioner. The changing nature of the federal tax laws makes it essential that tax practitioners be aware of regulations, rulings and decisions that issue from day to day. The massive amount of material and the constant revisions require continuing examination of the necessarily detailed reports issued by publishers of the tax services. It is literally impossible for the general practitioner to find sufficient time to follow these services. Still, he cannot render complete service to his clients unless he is at least able to recognize the tax questions that lurk in most everyday legal problems. Once the tax question is recognized, he can pursue it further in the tax services. Pellard's treatise is invaluable in providing him with the necessary background so that he can recognize the tax question.

Following the opening sections which discuss procedures, there are thirteen chapters, each dealing with a special topic. Subjects covered include wills, inter vivos trusts, life insurance, real estate transactions, the sale of a business by a sole proprietor, corporation problems, and alimony. In each chapter, the author deals with the numerous tax implications which may exist in transactions in the particular field. While the discussion is necessarily limited with respect to each question, there are very few points that are not touched upon. It is much more than a mere check list. Each problem is explained in sufficient detail so that its full import is made clear. At the end of most of the chapters the author has set forth

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suggested forms, which may be used to accomplish the client's purpose with the expected tax results.

A typical chapter which illustrates Pellard's approach is Chapter 11, entitled "Sale of a Business by a Sole Proprietor." Every lawyer, whether or not he is engaged in tax practice, may be consulted by a client who wishes to sell or buy a business. Pellard suggests these problems: Will there be a gain or loss to the seller? If a gain, and the purchase price is payable in installments, how can the seller avail himself of the installment basis for reporting the gain? Will the gain be considered ordinary income, capital gain, or a combination of the two? Since the sale of a business is not the sale of a single unit, but of the respective assets, how should the contract of sale and bill of sale be worded so that the purchase price may be allocated for the most favorable tax consequences to the client? What specific assets are considered capital assets? Since the question of allocation of purchase price to various types of assets may present a conflict of interest between seller and purchaser, what is the best position to take in representing your client with respect to the sale or purchase of good will, inventories, fixtures, land, etc.? Finally, Pellard sets forth a suggested clause which can be included in the agreement or bill of sale to carry out the parties' intentions as to allocation.

Invaluable as this book may be in raising problems, caution must be exercised if it is to be relied upon as providing definitive answers to the problems. As of the date the book was written, the answers were sound enough. Already, however, there have been statutory changes made by the "Technical Changes" Act.¹ As this review is written, Congress is enacting a new revenue act which makes radical changes in many of the substantive tax provisions. This, of course, is the reason why a short concise hornbook on federal tax law must inevitably have its limitations. All the more credit is due to Mr. Pellard, who must recognize that his book will soon be outdated, but who has nevertheless furnished a treatise which, if prudently used, may save grief for many practitioners.

It is not enough that the general practitioner be aware of tax problems which may arise from transactions into which his clients enter. More and more because of the complexity of the questions that arise, it is becoming necessary to litigate matters before the Bureau of Internal Revenue or the courts. In his opening chapters, Pellard reviews the procedures ordinarily followed in such litigation and sets out the forms in common use. He does not attempt to discuss tactics however, but merely outlines established procedures. Comprehensive guidance in the highly technical and involved process of tax controversy is not within the scope of this handbook.

For the general practitioner who wishes to get the feel of actual tax litigation, Bickford's *Successful Tax Practice* goes far to answer his needs. The experienced tax lawyer as well should benefit by many of the practical suggestions covered by the author. Unlike Pellard, Bickford

1. Pub. L. No. 378, 81st Cong., 1st Sess. (Oct. 25, 1949).

does not attempt to deal with substantive law. After an introductory chapter, he devotes the next six chapters of his book to stressing the importance of the facts.

Two of these six chapters, for example, are devoted to proof of value. While every tax practitioner is aware that value may be proven by the comparative sales method, the replacement cost method, or the capitalization of earnings method, there exists very little source material which is helpful to the attorney who wants to know what to do in a specific valuation case. Bickford carefully discusses which of the various methods are suitable to particular types of property, why they are suitable, and how the proof should be offered. It is to be regretted that space limitations did not permit Mr. Bickford to give us as thorough a treatment of the innumerable other types of factual questions which arise in tax litigation.

After stressing the importance of facts in every tax case and demonstrating some of the methods of developing them, the author presents a series of excellent chapters on the source materials of tax practice, how to find the law of the case, and how to write opinions and briefs.

Perhaps the most unique chapter in Bickford's book is one entitled, "The Bureau of Internal Revenue." Many tax practitioners today have had valuable experience as employees of the Bureau of Internal Revenue. With this past experience, they are fully familiar with the administrative procedures within the Bureau and the manner in which the Bureau is organized. For those who have not had the benefit of this experience, the chapter devoted to the Bureau of Internal Revenue and the following chapter entitled, "The Audit Processes" give as complete and concise a picture of the Bureau's interworkings as the reviewer has seen.

The last nine chapters of the book take the reader in chatty style through the usual procedures which follow the receipt by his client of the 30-day letter. Shall the deficiency be protested? What is the function of the Technical Staff? Shall his client proceed to the Tax Court, the United States District Court, or the Court of Claims? If he decides on either of the latter courts, the asserted deficiency must, of course, be paid and a claim for refund filed. How should the claim be filed and what must be done to avoid the many pitfalls attendant upon the filing of a claim?

As does Pellard's, Bickford's book contains specimen forms relating to practice. In the appendix there is included a complete copy of the rules of practice of the United States Tax Court. These rules, however, do not contain the revisions beyond December 15, 1948, so that, as set out in the appendix, they should not be relied upon without further checking. This again illustrates the practical impossibility of writing or publishing a tax treatise which can be relied upon as entirely authoritative. Despite this, and notwithstanding the constant changes in the law, Bickford's practical suggestions in the handling of tax cases will in all probability be applicable for years to come.

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BOOK NOTE

FOUL, FALSE AND INFAMOUS. By Clark Gavin. Abelard Press, New York, 1950. Pp. xv, 237. \$2.75.

Herein are accounts of seven famous libel cases, ranging all the way from the prosecution of Socrates for slandering the gods to the notorious Collier's v. Grape Nuts battle. (Also included: cases involving Peter Zenger—political critic of British colonial government, Thomas Cooper—Jeffersonian and character critic of John¹ Adams, *Whistler v. Ruskin*—the art feud, William Wilde (Oscar's father)—who tangled with one too many a wild Irish rose, the Prince of Wales—the famous Baccarat scandal.) These are reported for popular consumption, not professional legal analysis, and hence make vivid and entertaining if not awe-inspiring reading.

The author, using available records, attempts to recreate actual trial scenes. He succeeds well in this respect although excitement may lag where some of the accounts become too prolonged and detailed. For the student of social sciences the author sketches the historical background and significance of each case. He tries to show how plaintiffs may bring libel actions to achieve a wide variety of purposes—from the silencing of religious or political dissenters to the gaining of personal revenge for wounded vanity.

Undoubtedly the publishing of this book comes at a time when there is an increased popular interest in libel law, caused in part by the widening range of congressional investigating activity and in part by such publicized matters as the Victor Kravchenkov (*I Chose Justice*) case in France. In view of this, it is perhaps unfortunate that there was not more of an attempt to integrate the material with current problems in the law. But for a readable survey of the highlights of defamation, past and present, this book should prove quite adequate.

1. Not John *Quincy* (the son), as the author thinks, who had his own troubles with character critics among the Jacksonians.

BOOKS RECEIVED

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