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REGULATING FRANCHISE RATES

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The Dartmouth College case\(^1\) established that a state may make a contract, which will, by force of the federal Constitution,\(^2\) be protected against impairment. But such a contract may deal with matters which are within the field of the state's governmental powers. The courts, and particularly the Supreme Court of the United States, have frequently had to determine whether a contract dealing with such matters prevents the state's subsequent exercise of the governmental powers insofar as such exercise may affect the rights and duties arising from the contract in question. In other words, how far may a state make a contract protected from impairment by the federal Constitution, by which it surrenders its governmental powers?

In New Orleans Gas Company v. Louisiana Light Company\(^3\) it appeared that an exclusive franchise for a period of years had been granted by the state for the vending of gas in New Orleans, and that after such grant an amendment had been added to the state constitution abolishing all monopolies. It was claimed that a state legislature can not, by contract prevent the subsequent exercise by the state of its police power; that the adoption of this constitutional amendment was the exercise of the police power, and that such amendment was, therefore, effective notwithstanding the franchise contract. The court said that "police power" is a very broad term and may include

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\(^1\) Trustees of Dartmouth College v. Woodward (1819, U. S.) 4 Wheat. 518.


\(^3\) (1885) 115 U. S. 650, 6 Sup. Ct. 252.
substantially all governmental activities. But the court had no doubt that the state may by contract restrict the exercise of some of its powers—that it is not correct to say that a state may not by contract restrict the exercise of its police power, when the term is used in its broadest sense. Applying these conclusions to the case in hand, the court held that the grant of the exclusive franchise was protected by the constitutional prohibition against the impairment of contractual obligations, and to that extent restricted the state in the exercise of governmental powers, even by constitutional amendment. The court also pointed to the well established doctrine that a state may by contract limit its governmental power of taxation. But the court clearly recognized bounds to the power of one legislature to limit the discretion of its successors, declaring that they may not be so limited in the enactment of laws necessary to the protection of public health and morals.

In line with the suggestions just referred to, a series of cases in the Supreme Court of the United States makes it clear that certain governmental powers cannot be affected by contracts entered into by the state, and that contracts which attempt to abridge such powers are to that extent void, and, therefore, not within the protection of the federal Constitution against the impairment of contractual obligations. A state may provide for the suppression of nuisances, or pass other legislation in the interest of public health, even though this will infringe franchise privileges and rights. Franchises for the manufacture of alcoholic beverages, or for the conduct of lotteries, do not prevent later legislation, which may be justified as protective of public morals. Legislation requiring railroads to carry their tracks over or under highways, or to go to other expense or inconvenience for the safety of the public, is not unconstitutional, though immunity from such legislation may have been contracted for.

It is clear, then, that a state cannot make a contract so as to limit the exercise of its police power for the protection of the "peace, good order, health or morals of its inhabitants." But in the case in which

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4 The earlier cases of Bridge Proprietors v. Hoboken Co. (1863, U. S.) 1 Wall. 116, and the Binghamton Bridge (1865, U. S.) 3 Wall. 51, were relied upon.


6 New Orleans Gas Co. v. Louisiana Light Co., supra, 659.


8 Beer Co. v. Massachusetts (1877) 97 U. S. 25; Stone v. Mississippi (1879) 101 U. S. 814; and see Comment (1920) 29 Yale Law Journal, 437.


this declaration was made it was decided that a term in the franchise contract of a water company, that no water works would be constructed by the city, was protected by the federal Constitution, and would exclude the exercise of the governmental power to construct such water works. The court said that

"where a contract for a supply of water is innocuous in itself and is carried out with due regard to the good order of the city and the health of its inhabitants, the aid of the police power cannot be invoked to abrogate or impair it."

The legislative power to fix rates of public utilities is recognized as part of the police power, being the power to enforce the liability which rests upon public utilities to serve at reasonable rates. This is a power distinctly for the protection of the public, and affecting vitally their welfare. Yet the Supreme Court has declared that the state may contract away this power for a fixed period, and may authorize a municipal corporation to do so. The question as to what governmental powers can be abdicated by contract, even temporarily, is, of course, merely a question of public policy, where it is not controlled by the provisions of state constitutions. It is a question of what powers need to be so continually available that public policy imperatively forbids their abdication by contract. In view of the continual necessity and constant practice of governmental regulation of rates, it seems regrettable that the Supreme Court of the United States gave currency to the doctrine that a state may contract away this power of regulation. And in fact we see now a very decided tendency to limit this doctrine.

Most of the cases in which the state has attempted to abrogate contract rates over the objection of the public utility, have been cases in which the contract was made, not between the utility and the state legislature, but between the utility and the municipality. In

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38 Ibid., 17.
41 We shall come later to the abrogation of contract rates over the objection of the municipality.
42 There is, of course, a third possibility, namely, a contract between the utility and a private person purporting to fix rates. Because of the common-law duty to serve at reasonable rates resting upon public utilities, and the authority of the state to control the performance of that duty under its police power, courts do not hesitate to hold that such contracts are made subject to the police power, and that legislation which impairs the obligations of such contracts is, therefore, not unconstitutional, whether such a contract be with a consumer. Leiper v. Baltimore & Philadelphia Ry. (1918) 262 Pa. 328, 105 Atl.
such cases it is necessary to determine whether the municipality has power to make such a contract. The Supreme Court of the United States has declared that a municipality not only has no inherent or implied power either to regulate rates or to contract away the state's power of rate regulation, but that the delegation of authority to the municipality to make such a contract must be perfectly clear. In some cases the power to contract as to rates has been found clearly vested in the municipality, and the utility has, therefore, been protected in its contract rates; but in others that clear power has not been found, and the contract has, therefore, been held to be no protection against the exercise of the police power in the form of rate regulation. An examination of these cases makes two things clear. The first is that there is a strong presumption against the abrogation by contract of governmental powers over rates, and a consequent strong presumption against the delegation by the state to the municipality of the authority to abrogate such powers by contract. The second is that, although when a case is presented to the Supreme Court of the United States under the contract clause of the Constitution, it will itself determine whether there is a contract, as well as whether there has been a breach of it; that Court, nevertheless, in determining whether there is a contract, will give much weight to decisions of the highest court of the state on the question whether the statutes of the states do in fact delegate to the municipality power to contract as to rates. A most striking example of this policy is found in Freeport Water Company v. Freeport, where the majority of the court, following the interpretation put upon the state statute by the Illinois court, held that there had been no delegation. Also in the case of Vicksburg v. Vicksburg Waterworks Company, the Supreme Court

20 See cases in notes 18 and 19, supra.
21 Supra.
22 Supra. Similarly in Milwaukee Electric Ry. v. Railroad Commission, supra, careful consideration was given to decisions of the state court.
examined with care the Mississippi cases in which the state court had interpreted the statutes of that state, and followed its interpretation to the effect that there had been legislative delegation of authority to make rate contracts with utilities.23

Granted a binding contract as to rates made between municipality and utility, still a mere breach of the provisions of such a contract will not give the federal courts jurisdiction—there must be legislation impairing the contract obligations. So a municipal ordinance declaring an intention not to be bound by a rate contract, and not to perform it, does not raise a federal question.24 But an attempt by ordinance or statute to change the rights and duties under a valid rate contract, constitutes legislation impairing the obligation of a contract, and the claim that legislation has that effect does raise a federal question.25

As already pointed out, it may also be true that there is express authority to a municipality to make a certain contract with a utility company, and yet that such contract does not prevent subsequent legislation which clearly impairs the obligations of the contract. This is the case if the contract attempts to exclude the state from the exercise of such governmental powers as have been declared by the Supreme Court of the United States to be inalienable—namely, its police power for the protection of the “peace, good order, health and morals of its inhabitants.”26 This would be equally true of a rate contract if the constitution of the state expressly forbade the state to contract away its power to regulate rates.27 But there are some

23 State courts have not infrequently implied such delegation of authority from constitutional or statutory provisions that a public utility may only have the privilege to enter a municipality with the latter's consent. Matter of Quinby v. Public Service Commission (1918) 223 N. Y. 244, 119 N. E. 433; Salt Lake City v. Utah Light Co. (1918, Utah) 173 Pac. 556; St. Louis v. Public Service Commission (1918, Mo.) 207 S. W. 799; or from a charter power to grant franchises. Portland v. Public Service Commission (1918, Ore.) 173 Pac. 1178. But other courts have required clearer evidence of an intention to delegate such authority. See, for instance, the decisions of the state courts reviewed in Freeport Water Co. v. Freeport, supra, and Milwaukee Electric Ry. v. Wisconsin Railroad Commission, supra. The position is taken in some cases that while the state may apparently delegate to a municipality authority to contract away its power to regulate rates, authority to permit and regulate the use of streets is not a grant of authority to contract away the rate-regulating power, though it is a grant of authority to contract as to rates subject to the state's police power. Milwaukee Electric Ry. v. Railroad Commission (1913) 153 Wis. 592, 142 N. W. 451; Travers City v. Michigan Railroad Commission (1918, Mich.) 168 N. W. 481; State ex rel. Billings v. Billings Gas Co. (1918, Mont.) 173 Pac. 799; Winfield v. Public Service Commission (1918, Ind.) 118 N. E. 531.


25 The distinction is well explained in Northern Pacific Ry. v. Duluth, supra.

26 See notes 7 to 11, supra.

27 Detroit v. Detroit Citizens Ry. supra, 38a. The Oklahoma constitution provides in part: "Nor shall the power to regulate the charges for public service be
states in which the highest courts have declared, without the aid of express constitutional provision, that it is unconstitutional for the legislature, itself or through the agency of a municipality, to contract away the power of rate regulation—that such power is as necessary, and, therefore, as inalienable, as the power to protect the physical and moral well-being of its inhabitants. If in such a state the legislature made a rate contract with a public utility company, and later fixed lower rates by statute, would the Supreme Court of the United States hold such later legislation an unconstitutional impairment of the rate contract? Mr. Justice McKenna, speaking for the majority of the court in Freeport Water Company v. Freeport, after stating that a state may contract away its power to regulate rates for a fixed period, said:

"We do not mean to say that if it was the declared policy of the State that the power of alienation of a governmental function did not exist, a subsequently asserted contract would not be controlled by such policy." Such a policy as to rate regulation had been intimated, he said, but not asserted in the decisions of the state court, and was not relied upon in the case under consideration.

But further, in the case of Chicago & Alton Railroad Company v. Tranbarger, we seem to find a distinct change of emphasis with regard to the capacity of states to limit the exercise of their govern-

surrendered." Art. 18, sec. 7. Pawhuska v. Pawhuska Oil Co. (1919) 250 U. S. 393, 39 Sup. Ct. 526. The Missouri constitution provides that, "The exercise of the police power of the State shall never be abridged, or so construed as to permit corporations to conduct their business in such a manner as to infringe the equal rights of individuals, or the general well-being of the State." Art. 12, sec. 5. The Supreme Court of Missouri has declared that "Under such a constitutional restriction, the Legislature would be powerless to enact a valid law by the terms of which the right of the state in the exercise of its sovereign police power in the fixing of reasonable rates for public services could be limited or abridged." State ex rel. Sedalia v. Public Service Commission (1918, Mo.) 204 S. W. 497, 499. The Pennsylvania constitution contains the same provision. Art. 16, sec. 3. The Pennsylvania public service commission held that the constitutional provision against impairment of contracts does not prevent regulation of contractual rates under the police power. Wilkinsburg v. Pittsburg Rys. (1918) P. U. R. 1918F 131; and see Leiper v. Baltimore & Philadelphia Rys., supra, 332.


"Supra, 593.

mental powers by contract. A statute of Missouri passed in 1907 required railroads to make suitable openings in embankments on their "rights of way" for water drainage. The company in question had constructed its embankment long before the passage of this statute, and the company contended that the statute impaired its rights secured from the charter contract, and took its property without due process. After consideration of other points, the court said:

"But a more satisfactory answer to the argument under the contract clause, and one which at the same time refutes the contention of plaintiff in error under the due process clause, is that the statute in question was passed under the police power of the State for the general benefit of the community at large and for the purpose of preventing unnecessary and wide-spread injury to property. "It is established by repeated decisions of this court that neither of these provisions of the Federal Constitution has the effect of overriding the power of the State to establish all regulations reasonably necessary to secure the health, safety, or general welfare of the community; that this power can neither be abdicated nor bargained away, and is inalienable even by express grant; and that all contract and property rights are held subject to its fair exercise. *Atlantic Coast Line v. Goldsboro*, 232 U. S. 548, 558, and cases cited. And it is also settled that the police power embraces regulations designed to promote the public convenience or the general welfare and prosperity, as well as those in the interest of public health, morals, or safety.

"We deem it very clear that the act under consideration is a legitimate exercise of the police power, and not in any proper sense a taking of the property of plaintiff in error."

Clearly we have here a change of emphasis. It seems now that it is not only the power to protect the safety, health and morals of its inhabitants which the state cannot abdicate; "the power of the state to establish all regulations reasonably necessary to secure the health, safety and general welfare of the community . . . is inalienable even by express grant." If the power to protect land from being flooded is so necessary for the "general welfare of the community" that it cannot be abridged even by express grant, what should we say at the present time with regard to the power to regulate rates of public utilities? Is it not more necessary for the purpose of securing the "general welfare" of the community that the state should have the inalienable power to protect its inhabitants from unreasonable and discriminating rates for transportation, water, gas, electricity and sewerage facilities, than it is that it should have such an inalienable power to protect the land of its inhabitants from being flooded because of the use made of their lands by others? Possibly the doctrine that a state may contract away its power to regulate public utility rates is not yet too firmly fixed in the adjudications of the Supreme Court to be shaken by well-directed argument.

*Ibid.,* 76-77.
Since 1914 we have seen a most interesting reversal of parties in efforts to get away from contract rates. Due to the vast increase in the cost of service, public utilities all over the country have been urging the necessity of legislation increasing their charges to the public; and frequently they have been opposed by municipalities, claiming that rates have been fixed by franchise contracts, and that any legislative change would constitute an unconstitutional impairment of the contractual obligations.

If it were held that the state cannot restrict the exercise of its police power to regulate rates by contract with public utilities, the difficulty would disappear in this class of cases, as well as in the class where it is the utility which seeks to prevent the alteration of contract rates, which we have just discussed. In fact, as is pointed out above, in several states it is expressly declared, or judicially held, to be unconstitutional to contract away the rate-making power, with the result that the impairment of such contract does not contravene the federal Constitution. Nevertheless, we must still, in most jurisdictions, assume that the state can make a rate contract with a public utility which is protected by the federal Constitution from impairment; and that, if clearly authorized to do so, a municipality may make such a contract on behalf of the state.

Here, then, the first question is, granted a contract has been made between the municipality and the utility, which is within the protection of the federal Constitution, may the municipality invoke the constitutional guaranty against threatened impairment by the state? The answer to that question will be found in the answer to the further one, has the state made any contract with the municipality abdicating its police power, or has the state simply made such a contract through the municipality as its agent, with the utility? If the only contract is between the state and the utility, and the state and the utility agree to rescind it, clearly no contractual obligation has been impaired.

Fortunately the same question which arises when the state at the request of the utility raises franchise rates, was presented to the Supreme Court of the United States before the war in Worcester v.

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Notes 27 and 28, supra.

In at least two recent cases in the federal courts public utility companies, finding their franchise rates inadequate, have attempted to get relief from them in equity: Knoxville Gas Co. v. Knoxville (1918, E. D. Tenn.) 253 Fed. 217; Columbus Ry., Power & Light Co. v. Columbus (1918, S. D. Ohio) 253 Fed. 499, affirmed in (1919) 249 U. S. 399, 39 Sup. Ct. 349, (1919) 28 Yale Law Journal, 826-827. In each case it was found that the city was within its delegated powers in making the ordinance, that the ordinance and its acceptance constituted a valid contract, and that the court of equity had no power to set it aside in absence of fraud or duress. This is, of course, to be distinguished from an appeal for equitable relief from statutory rates. Municipal Gas Co. v. Public Service Commission (1919) 225 N. Y. 89, 121 N. E. 772, (1919) 28 Yale Law Journal, 592.
Street Railway Company. A Massachusetts statute provided that a street railway wishing permission to enter a municipality should apply to the municipal authorities for the location of its tracks, and that such a privilege might be granted under such restrictions as seemed in the interest of the public. The city granted this privilege in certain locations under condition that the company should lay and keep up a certain part of the pavement, and this grant was accepted and acted upon. Several years later a state statute was passed providing that street railways should not be required to keep pavements in repair. The proceedings which reached the Supreme Court were to enforce the duty to repair according to the grants made, it being contended that the grants constituted contracts protected by the federal Constitution. Admitting for argument that the grants were contracts, and that the company's rights and privileges could not be impaired without its consent, the Court held that since the restrictions were of a public and governmental nature, the legislature would have all the power to terminate them that the city itself would have, since the city is but a creature of the state for governmental purposes.

This last year the Circuit Court of Appeals for the ninth circuit applied these principles to the rate case of Salem v. Salem Water, Light & Power Company, expressing them even more clearly than the Supreme Court had done. The city was incorporated under a charter by which it had authority to provide for water and lighting, or to grant the privilege to use the streets for these purposes "upon such terms and conditions as the council may prescribe." The council fixed a maximum hydrant rate, which was later increased by the public service commission. The court declared that the charter and powers granted to a municipality do not constitute a contract between the municipality and the state protected by the Constitution. In making a contract as to rates to be charged the public, a municipality acts merely as agent for the state, and with the consent of the company the contract may be changed by the state. In other words, the grant to the municipality of power to contract as to rates, is not itself a contract between the municipality and the state protected by the federal Constitution, but is merely a delegation of a certain power by the legislature to a political subdivision of the state, which may be revoked at any time; and any rate contract which a municipality has authority to make is in fact a contract between the state on the one hand, acting through its agent, the municipality, and the utility on the other hand, which can not be said to be "impaired" when in fact it is modified.

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\(^{35}\) (1919, C. C. A. 9th) 295 Fed. 295; and see Pawhuska v. Pawhuska Oil Co., supra.

by the actual consent of both parties. These principles have been recognized and acted upon by the state courts in controversies precipitated by the raising of franchise rates. As said by the Supreme Court of New Jersey, if the ordinance be viewed as a contract, it is well settled that a municipal corporation, an agency of the state, is not protected by the contract clause of the Constitution against its own creator, the state.

Still, it would be possible for municipalities to be given power by the state constitution to make rate contracts which would be beyond the power of the legislature and the utility to alter even by mutual agreement. A number of our state constitutions provide that a street railway may not be constructed or operated within a municipality except with the consent of the local authorities. It has been claimed that this gives municipalities constitutional authority to contract as to rates as a condition of consent, and that such contract being authorized by the constitution is safe from legislative control. This claim has, however, been held to be unsound by the state courts of last resort to which it has been presented. It is clear that under such constitutional provisions municipalities have the absolute power to choose whether to exclude street railways or to admit them, and it is conceded that such power carries with it the power to consent only upon the conclusion of a contract incorporating conditions laid down by the municipality. But it is denied that there is here more than an authorization to contract on behalf of the state, leaving as the contracting parties the state and the utility, and leaving such parties the power, therefore, to change the terms of the contract by mutual consent. In the Matter of Quinby v. Public Service Commission, the New York court did not pass upon the question, and left it uncertain whether it would take the view just set forth, if the question were brought before it for decision.


City of Chicago v. O'Connell, supra; St. Louis v. Public Service Commission, supra; Kansas City v. Public Service Commission (1918, Mo.) 210 S. W. 381; Salt Lake City v. Utah Light Co., supra; Virginia-Western Power Co. v. Commonwealth ex rel. Clifton Forge (1919, Va.) 99 S. E. 723. Such a claim does not raise a federal question. Kansas City v. Public Service Commission (1919) 40 Sup. Ct. 54. See the citation to the case in the Missouri court just above in this note.

(1918) 223 N. Y. 244, 119 N. E. 433.
REGULATING FRANCHISE RATES

The intimation in support of the above view is clear in *International Railway Company v. Public Service Commission*; but the New York court in that case also raises, but does not answer, the question as to what would be the result of the exercise by the legislature of its power to raise rates which had been fixed by contract under a consent clause of a state constitution. Its language is interesting:

"It is one thing to annul an independent covenant, which, though part of the consideration for the grant, does not condition the grant itself. It is another thing to annul a condition which operates, by way of defeasance of the franchise, to terminate the grant. . . . A municipality may be willing to have an electric railroad in its streets; it may be unwilling to have a railroad run by steam. It may be willing to have a railroad that can furnish cheap transportation; it may be unwilling to have another. . . . The Legislature may say that, subject to the condition subsequent annexed to the consent of the locality there shall be a change of motive power or an increase of the rates. It may say that if the local authorities do not promptly manifest the election to revoke, the condition shall be waived. The doubt is whether, going further, it may wipe out the condition altogether, and transform a consent that was qualified into one that is absolute. . . . In deciding the Quinby Case, we left the question open, as we leave it open now. On the one hand, it is argued that the condition admits of no exception, since none has been expressed . . .; on the other, that by implication its binding force is to continue only in default of legislation that shall cover a like field. We assume that much may be said in favor of each view." 42

The question which is raised here is a very interesting one, but it would seem fair to answer it in this way: The city might have excluded the company. Instead it chose to let it in, offering to make a contract on behalf of the state, and requiring the company to join in the contract as a condition precedent to permission to enter. The city impliedly had authority to make this contract for the state, but like every other contract made for the state, it could be changed by the two contracting parties, the state, through the legislature, and the company. There is nothing in the Constitution prohibiting the exercise by the legislature of this inherent power. This question which troubles the New York court does not seem to have presented itself as a substantial difficulty to the courts which have actually passed upon the power of the legislature to raise rates fixed by contract under a consent clause of a state constitution. 43

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42 Ibid. In *Village of Long Beach v. Long Beach Pr. Co.* (1918) 104 Misc. 337, it appeared that not only use of highways, but also private easements had been granted to the company, rates for gas being fixed by the terms of the grant. The company raised its rates with the consent of the public service commission, and a preliminary injunction against their enforcement was granted on the ground that the company could not retain the private easements under the contract and repudiate its part of the contract as to rates.
43 Cases in note 39, supra.
Contracts made by municipalities with public utilities may deal with rates to be charged the public, or they may deal with rates to be charged the municipality; or they may deal with the case of public property; or the municipality may have a proprietary interest in the property used by the utility, the earnings from which may be affected if the contract rates are changed. There is substantial unanimity to the effect that the state with the consent of the utility can change contract rates affecting the public. But in several cases where the contract rates sought to be raised were to be paid by the municipality, the municipality has sought to persuade the court that the legislature could not interfere with the contract rates. In *State ex rel. Sedalia v. Public Service Commission* the question was as to the validity of an increase made without the city's concurrence in a franchise hydrant rate. It was held to be valid. In *Sandpoint Water & Light Company v. City of Sandpoint* the city attacked the validity of increases in rates for hydrant and sprinkling service over those previously fixed in a franchise contract. The court said that in granting a franchise in which rates are fixed, a municipality is exercising only powers conferred upon it, and these powers may be withdrawn at any time.

"A municipality has no vested right to the continued exercise of such powers, nor can it obtain a vested right in any contract entered into or property acquired through the exercise of such powers as against the right of the state, its creator, to assume complete control of its affairs." The case of *Salem v. Salem Water, Light & Power Company*, already considered, takes the same position with regard to hydrant rates.

In *People ex rel. Village of South Glens Falls v. Public Service Commission*, the court had before it the question of raising gas rates fixed by franchise contract. It held that such rates could be raised, but in the opinion there is a dictum that, if the franchise provides the rate at which the municipality is to be served, such may constitute a contract which the legislature cannot change. To support that dictum the court cited *Kings County Lighting Company v. City of New York*. There the claim was that a contract rate for street lighting had been lowered by the legislature. The decision was that the statute invoked was not intended to affect the contract rate in question. It was declared, however, by way of dictum, that if it had been intended to do so, it would have been unconstitutional as impairing the obligation of a contract; which is, as we have seen, the view supported by the majority of cases at the present time, when

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"Supra."  
"Ibid., 973."  
"Supra."  
"Supra."  
"(1919) 225 N. Y. 216, 121 N. E. 777."  
"(1916, N. Y.) 176 App. Div. 175, affirmed (1917) 221 N. Y. 500."
an attempt is made to lower contract rates. In this connection the court said,

"In no sense was it [the statute lowering rates for street lighting] an exercise of the police power, as it was not for the general public, but for the defendant's relief, standing apart from general local consumers."\(^{50}\)

Notwithstanding these dicta, it is believed that the following propositions are sound. The duty to serve at reasonable rates exists equally whether the service is rendered to the municipal corporation, or to the inhabitants of the municipality; it follows that the police power extends to the enforcement of that duty in each case; and that the municipality if authorized to contract in this field of police power as to rates for either kind of service, does so only as agent of the state; and that the contract can, therefore, in each case be modified by agreement between the state and the company.

The case of *Worcester v. Street Railway Company*, already considered,\(^ {44}\) is instructive in this connection. The franchise under which the company was allowed to use the streets of the city required the company to lay and to keep up certain parts of the pavements in the streets through which its tracks were laid. Later a Massachusetts statute provided that street railways should not be required to keep pavements in repair. Actions being brought to enforce the duty to repair according to the franchise provisions, the Supreme Court of the United States held that, granting the franchise was a binding contract, the restrictions in it were of a public or governmental character and the state could, therefore, change its requirements without the consent of the city. Here the contract called for the upkeep by the company of property in which the municipality had the fee or an easement, to the financial advantage of the municipality. Yet the legislation was held constitutional—it neither unconstitutionally impaired the obligation of the contract, nor deprived the municipality of its property without due process.

The court in the *Worcester* case does say that a municipality may own property, not of a public or governmental nature, which would be protected by the federal Constitution from legislative action. The only illustration given by the court of property which is excepted from legislative control is the following:

"Property which is held by these corporations upon conditions or terms contained in a grant and for a special use, may not be diverted by the legislature."\(^ {42}\)

\(^{41}\) *Supra.*
But this inhibition would seem to be based rather upon the duty to observe the trust in favor of the public upon which the property was granted, than upon the prohibition against impairing contractual rights and privileges or taking property. In the field of legislative control of municipal property the law is still in a very unsettled state, but the following statements are reasonably safe: (1) Power granted to a municipality may be withdrawn by the legislature at will; (2) when it is feasible to use property acquired by the municipality for the purpose for which it was acquired, the legislature may not divert the same to some wholly different use; (3) there has been a rather persistent attempt to distinguish between property held by a municipality for public purposes, and for quasi-private purposes, and to claim an immunity for the latter from state control somewhat analogous to that enjoyed by privately owned property, while recognizing a greater degree of state control over the former, though very satisfactory progress has not been made in such classification; (4) all municipal property, even of quasi-private character, is at least as subject to control by the legislature under the police power as is private property devoted to a public use.55

If a municipality owns a public utility, there seems no reason to doubt that the state may exercise its police power in the regulation of the rates of such utility. This it may do under the police power where the project is privately owned, though it reduces the income from such property, and a fortiori should it have the power to do so if the property is owned by one of its political subdivisions for the benefit of the public.54

Where the municipality builds and owns a public utility system, as is the case in New York City with the subways, and leases such system to an operating company, contracting for a definite per cent. of the gross or net earnings, and fixing by contract the fare which the company may charge, it would seem to have no right to object if the legislature, with the consent of the company, changes the rate of fare. As we have seen above, the contract as to fare being in fact a contract between the state and the company, the state and the company may agree as to its alteration and such alteration is not an impairment of any contractual obligations. If it can be shown that the change as to fare will lower the return which the city will receive on its property represented by the utility system (which would generally not be true, the change being made with the consent of the operating company), still, this could not be viewed as taking the city’s property without due process, because whatever taking there might be would be merely the indirect result of a legitimate exercise of the

54 1 Dillon, op. cit., sec. 116.
police power. In principle the case is not different from the *Worcester*
case, considered above. In that case the contract made by the city
with the company was changed, and property interests of the city
were affected, but the legislation which had these effects was held
constitutional.

Let us consider for a moment the possibility of complaint by a
patron of a public utility that the rate to be charged by the utility
has been unreasonably raised, whereby he is compelled to pay rates
that are unreasonably high. In an Indiana case,** in which the ques-
tion before the court was the constitutionality of certain reductions
of rates, the court said:

"To allow a carrier, for the use of its road, a rate less than is
necessary to save it from actual loss in its operation, is to take the
property without just compensation and without due process of law;
and to require of shippers a greater charge than is reasonable, under
the circumstances, is to treat them in the same way. In either case
the act is confiscatory."

As to the shipper, this is mere dictum. On the other hand, in *Brook-
lyn Union Gas Company v. City of New York*,† where it was con-
tended that the legislative rate was unreasonably high, the court
declared that there is no property right in a rule of law and that it is,
therefore, not unconstitutional for the legislature to take away the
advantage of the rule of law that a public utility must serve at a
reasonable rate. When the company is allowed to charge more than
reasonable rates, a patron's money is not thereby taken—his patronage
is voluntary and he is not forced to part with his money.‡

Generally at the present time legislatures do not act directly in
lowering or raising rates, but act through public service commissions.
That they may delegate such power, if they lay down general principles
for the guidance of the commissions, is now axiomatic.§ Such
authority generally extends to the changing of preexisting legislative

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**Southern Indiana Ry. v. Railroad Commission** (1909) 172 Ind. 113, 87 N. E. 966.


‡(1906) 90 Misc. 450, affirmed (1906) 115 App. Div. 69, and (1907) 188 N. Y. 324, 81 N. E. 141.

§In *Consolidated Gas Co. of New York v. City of New York* (1908) 126 App. Div. 950, 111 N. Y. Supp. 1115, the judgment in the court below was affirmed in a memorandum opinion, on the authority of *Brooklyn Union Gas Co. v. City of New York*, discussed in the text. There is an interesting comment upon the *Brooklyn Union Gas Co.* case, in *Business Men's Association of Ticonderoga v. Delaware & H. Co.* (1909, 2d Dept. of N. Y.) 2 Pub. Serv. Com. 78, 85.

One of the problems in connection with franchise rates has been the extent of the power to raise such rates possessed by public service commissions.

The much-cited case of Matter of Quinby v. Public Service Commission,61 decided that there was no evidence of an intention to delegate to the commission authority over franchise rates established in pursuance of the provision of the New York constitution that street railways may not be constructed or operated in municipalities except with the consent of the local authorities. But in People ex rel. Village of South Glens Falls v. Public Service Commission,62 where the franchise contract was with a gas company instead of a street railway, it was held that the commission had authority to raise the franchise rates. The difference was in this, that the requirement that gas companies shall get the consent of local authorities before entering a municipality is statutory, while the similar provision with regard to street railways is constitutional.63 Thus in New York the general authority given to the public service commissions over rates is held to give them authority to raise franchise rates, except when those franchise rates are a condition of a consent which is required by the constitution.

Courts of other states, having consent provisions with regard to street railways in their constitutions similar to that in New York, have not made the distinction made by the New York courts, but have interpreted the power of the commissions over rates to include the

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62 Supra, two judges dissenting.
63 Supra, three judges dissenting.
64 See the ground of the decision in the Quinby case as stated in International Ry. v. Public Service Commission, supra. In that case it was held that where a franchise contract with a street railway reserves the power of the legislature to regulate fares, it will be inferred that the power to so regulate them was delegated to the commission. In International Ry. v. Rann (1918) 224 N. Y. 83, it was held that though a street railway enters a city under franchises fixing rates, the commission may raise rates if the municipality consents. In Koehn v. Public Service Commission (1919, N. Y.) 107 Misc. 151, the Supreme Court at special term decided that the constitutional requirement that a street railway shall get the consent of municipal authorities before entering the municipality, does not give the municipality authority to contract as to rates to be charged outside of the municipality. The court, by way of dictum, suggested that where a street railway was permitted after the enactment of the public service commission law to enter a city upon condition of agreeing to certain rates, the rates are subject to the commission's power. This seems very doubtful. But if the rate contract is not a term of the consent required by the state constitution, the Quinby case does not apply, and the commission may raise the rates. Niagara Falls v. Public Service Commission (1919) 177 N. Y. Supp. 861.
power to raise franchise rates of street railways, as well as the franchise rates of other utilities. Where the contract as to rates is made by the municipality with the utility, as the result of legislative rather than constitutional authority, there is substantial unanimity in the conclusion that the commissions have authority to raise such rates, unless a contrary intention is apparent. The only discordant note in this group of cases seems to be from Ohio, in *Interurban Ry. & Terminal Company v. Public Utilities Commission*. There it was held that, municipalities having by statute "the power to fix the terms and conditions upon which such railways may be constructed, operated, extended and consolidated," a franchise ordinance which is accepted, embodying terms as to rates, is a contract, and that the general power over rates vested in the commission did not give it power to raise such franchise rates. The court in reaching this conclusion relied upon the *Quinby* case, which we have seen has been interpreted as standing for no such broad proposition.

Of course, however, the commission may by the clear intent of the legislature be excluded from all control over franchise rates, as under the Georgia statute defining the power of the commission, which expressly provides that nothing therein shall be construed to impair any valid, subsisting contract relations between any municipality and company, or to repeal any ordinance.

The recent economic crisis in public utility enterprises, which has changed the general effort to reduce rates into a general effort to raise them, has on the whole found the law sufficiently elastic to meet the new demands. There have only been occasional setbacks. Furthermore, the machinery of public utility commissions has fortunately been in general operation. The crisis has again demonstrated how much better fitted they are to deal with rate regulation than are the state legislatures.

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*St. Louis v. Public Service Commission, supra; Kansas City v. Public Service Commission, supra; Salt Lake City v. Utah Light Co., supra; Virginia-Western Power Co. v. Commonwealth ex rel. Clifton Forge, supra. In City of Chicago v. O'Connell, supra, the commission was held to have authority to change regulations for running cars embodied in a franchise under a consent provision of the state constitution.*


*Supra.*

*Georgia Ry. & Power Co. v. Railroad Commission, supra; and see Virginia-Western Power Co. v. Commonwealth ex rel. Clifton Forge, supra.*