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By Alfred Emanuel Smith

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RAILWAYS AND TAXATION

By Charles B. Fillebrown

The Outlook of July 20 has placed its readers under obligation by Mr. Whiting's article on The Railway Problem from a Commissioner's Point of View. Will you indulge an essay at making one more forward step in the general discussion, together with incidental rejoinder to your comment upon my recent letter on "Taxation the Cure" (Outlook of June 26)? I quote your comment for reader reference:

Taxation may serve to secure to the public its share of the wealth secured through a public franchise; but it has no effect whatever to secure either just or equal rates for passengers and shippers, none to prevent stock-watering and corporation-wrecking, and none to guard against accidents produced by underpaid or overworked employees or false economies.

Mr. Whiting concludes that of the three possible methods of solving our railway problem, the most expedient is that which he characterizes as private ownership with public regulation. In my brief letter I had suggested that an initial step in the settlement of the problem might be taken at once along the path of gradually increasing franchise taxation. Your comment on the letter suggests that Mr. Whiting's general proposal and my own are regarded by The Outlook as alternative rather than as supplementary. Since this was not at all the idea in my own mind, I beg permission to explain more fully the purport of my earlier suggestion.

Let us suppose that taxation has been operative, say for a generation; that, in accordance with The Outlook's concession quoted above, it has gradually recovered the value of the franchise to the public by a process so tentative and even cautious as to make "grim financial disaster" impossible. Let us next assume that, as a result, the triple concurrent agencies, "private ownership," "public regulation," and "taxation of franchise," are now in mutual and harmonious control of the situation, from which speculation and exploitation will have been eliminated as superfluous.

The problem of government regulation will be to harmonize the interests of capital, management, and the public: a fair profit to capital; fair rewards for skill and enterprise in management; a fair return to the public for franchise privileges. But "fair" is a fairly indefinite word. I would suggest the following as a denotation of the term.

Capital: A fair rate of return to capital invested in railways is the market rate of interest upon investments of equal security, as fixed in competitive industries, and this is all that capital (minus speculation) demands. Speaking of improvements, Mr. Whiting says: "The public must, in the

last analysis, stand the expense." In the same sense the public must stand the expense of the "fair profit" by virtually guaranteeing it.

Capital does not run the road, and hence it is not entitled to unusual profits due to the risks of an established business. Reduction of rates and taxation of franchise will have squeezed the water from the stock, and actual capital, as determined by the Commission, will be a preferred creditor to the extent of its "fair profit." The claim that a higher rate of dividend should be paid to capital on account of skill and enterprise in management is a vicious one, arising from the attribution to one factor of what clearly belongs to an entirely distinct one.

Management: The administration of the business of the public service corporation would be, as now, in the hands of agents, superintendents, and managing directors, who would profit by salaries in proportion to their skill and brains, from \$1,000 to \$50,000 or \$100,000 a year. It is these men run the road now, and it is their concern to deserve profit by so doing. Mr. Whiting well says: "Traffic men, as a whole, keen, adroit, and sensitive to every change in the industrial world, turn to with their magnificent forces and abilities and work with the Railway Commission instead of against them." Skill and enterprise, instead of selfishness and greed, would provide the initiative for legitimate extension and development

The Public: Its concern is to reap from its own business, delegated to private hands, a fair return, whether it be by lower rates or higher taxation. The Commission, composed of men of good judgment and incorruptible honesty, its functions being supervisory rather than managerial, will fix upon a fair capitalization, and determine when and what reduction should be made in earnings through reduction of rates. By the municipalization of the franchise the main motive for "stock-watering and corporation-wrecking," or for "underpaid or overworked employees or false economies," will be destroyed. Whatever "rebates," "stock-watering," and "corporation-wrecking" survive the assumption of the franchise by taxation, the Commission will prevent under statute. The value of the franchise will be gradually absorbed through reduction of rates, leaving, however, a substantial margin as the best possible index and basis for taxation and regulation. This marginal surplus would serve the purpose of equalizing conditions from year to year, bridging over lean financial periods, and thus securing more fully the stability of the fair profit to capital irv vested.

To sum up, it is the contention of this letter that, with our railways privately owned, publicly managed, and taxed approximately to the value of their franchises, public audit will increasingly protect both public and stockholder; public inspection will keep up the standard of the service; capital will get its interest; managerial skill and enterprise will get its compensation; the public will get its low rates and taxes. It will, therefore, appear that franchise taxation is proposed, not as a sole solution of the railway problem, but as a flexible, practicable, speedy supplement to the necessarily more rigid policy of regulation.

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