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THE PRINCIPLES OF GOVERNMENT CONTROL OF BUSINESS

Annual Address of the President

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The circumstances of the present financial crisis (1907) have emphasized the importance of the much debated question of the relation of government to business. A few months ago the President of the United States was in many quarters enthusiastically praised for his assertion of the power of the federal government to make business men and corporations amenable to law. A few weeks ago the voices of most of these acclaimers were silent in doubt, while another group of people, on account of these same assertions, were declaiming vigorously against the President as the immediate cause of the panic. The question has likewise arisen in our different states in connection with the Government control of insurance companies, of savings banks, and other business corporations, some of these of a more or less philanthropic nature, while, besides the socialists, thousands of our most unselfishly patriotic citizens have urged upon the public the desirability of municipal ownership and management of the water works, lighting plants, street railways and other so-called public service industries.

It seems a fit time to inquire whether any fundamental principles in connection with this question can be recognized as having some permanent application. If there are such principles, they must naturally be found in the

nature of government and in that of business. A brief review of so broad and complicated a question, even though it contains little that is new, may still be useful in bringing together some old and well-worn but perhaps partly forgotten truths that may prove suggestive. In making the attempt in the very brief period of time allotted, I shall not argue points; I shall simply state them as settled, even though I am aware that the statement is debatable. It is often perhaps as great a service to state a question for discussion as to argue it.

THE AUTHORITY AND CONTROL OF GOVERNMENT
NECESSARY.

2. In all civilized states, whether government be personal or popular, a fundamental condition of political stability and of social and economic prosperity is that under the constitution and customs of the country, so far as the individual members of society need control, they must be controlled by government and the government must direct these activities of the citizens as it thinks best. In a democracy, and it is chiefly of a democracy that I shall speak, if the people think that the views or the acts of their representatives, either in the legislatures, in the courts, or in the executive chair, are wrong, they may endeavor to secure a change of the law or a change in the personnel of their rulers; but in either event, the law, while it stands, must rule, and the office-holders actually in power must use their discretion. The interests of the people, of course, should be safeguarded, and in the long run, if the people have judgment, they will be safeguarded; but in any event there cannot be business success without stable government. The doings of the people in cases where the government acts, must be through the hands of officials and these acts must be put into effect in the man-

ner and in the degree that the officials for the time being think best. The only legal right that the citizens have, so far as government activity goes, is that of having their will carried out through their officials.

IMPRACTICABILITY OF THEORY OF NATURAL RIGHTS.

3. Large numbers of our people find a basis for argument and apparently much personal comfort in a discussion of their "natural rights", as if they had rights opposed to the legal rights given them by the state. Such an expression is, of course, an excellent talking point as a basis for argument to convince people, and perhaps through them to change the opinion of the government as to what ought to be done. But, as an immediate principle to direct governmental action, the theory of natural rights, as interpreted by the individual beyond what is laid down in law, is a vagary of enthusiasts, a breeder of fanatacism; and it is harmful, because it turns aside from practical means the minds of many of our most unselfish, high-minded, public-spirited citizens. The only sound basis for advocating a change in governmental policies is that the welfare of society will be improved by the change advocated. Let all arguments for social reform be made on this basis; let the weight of argument show the practicability of securing the desired benefit; convert thereby as many of the citizens as possible; thus you may convert the government. The whole question of governmental activity in business matters is not one of the "natural right" of an individual as against his government or against his fellow citizens; it is one of the thoughtful judgment of the few men who are directing the affairs of political society as to the practicable means for doing their duty under the powers laid down in the constitution and laws.

CITIZENS MUST RECOGNIZE THE AUTHORITY OF
GOVERNMENT.

4. Too little emphasis is often laid upon the importance of having fixed in the minds of the citizens of every country the fundamental principle that the only way in which citizens can act politically on any social question is through the government. There exists of course the so-called right of revolution, but this may be ignored as foolishly impracticable in this connection. In all countries, though most easily in a democracy, the will of the citizens may comparatively easily be brought to expression if people are thoughtful and active, and not one proposed reform in a thousand is important enough in its effect upon the welfare of the citizens to justify any setting aside of the authority of government for its accomplishment. People sometimes foolishly, on account of the slowness of governmental action or the corruption of a few government officials, apparently despair of the success of popular government. How many times within the last ten years we have heard wild talk about the ownership of our government by the moneyed classes, and of the impossibility of having a wealthy malefactor brought to justice. Some of our late governmental actions, such as the judicial decision in the Northern Securities case, the investigation of the insurance companies in New York, and the exposure of the Trusts by the Bureau of Corporations, have been chiefly valuable, not for their immediate results, but for showing the public clearly and conclusively the very simple but all important truth that government can and does rule. How far then the government of any state shall control business and business men and in what manner, is a matter within the determination of the government itself, keeping always the welfare of the citizens in view.

GOVERNMENT CONTROL WILL VARY UNDER INFLUENCES
OF VARIOUS KINDS.

5. The extent and method of its control of industry will vary in different countries and under differing circumstances. There can be no general rule laid down but this: The action of the government ought to be based on the special circumstances of each individual case. All comparative studies of the experiences of different countries in different lines of industry can be only suggestive. For the settlement of any such question, however, various factors will always be found which must be taken into careful consideration.

POLITICAL CONDITIONS AFFECT CONTROL.

a. The political circumstances of the country, determined quite possibly by geographical considerations, will often be a dominating factor. Germany, for example, is so situated geographically between France and Russia that, in order to be certain that it can maintain its independent existence under threatening circumstances, it must be prepared to concentrate its military power in overwhelming force with the greatest rapidity at the shortest notice. Under such circumstances, considering modern methods of warfare, its railroads should be built primarily to serve promptly its military needs, although, of course, its network of lines will probably in the long run serve this need best if it also serve well economic ends. Likewise the management of these roads must be such that the government without materially lessening their efficiency, can take immediate control and direct the traffic to military ends with little loss of energy. The government of Germany then must so control its railways as to keep them always in readiness for war. It must own and manage them, even though in so doing it were to weaken

their economic efficiency. A similar line of argument, altho entirely different in detail, might well apply to Russia, to France and to many other countries, while it would have application in only a slight degree to Canada, to Brazil, or to the United States.

CONTROL ULTIMATELY NOT A MATTER OF LAW, BUT OF
ECONOMICS AND POLITICS.

b. The question has of late often been discussed, sometimes in a rather heated way, whether the control of the railways of the United States should be state or federal, and in what degree our cities should, of their own motion, control their lighting plants, and the answers to these questions have often been sought along the line of legal precedent. The question is ultimately not one of law, but of economics and politics. Considering our form of government, a court decision of fifty years ago may, to be sure, for the present, be a determining factor; but in the long run, such a question is not to be answered by legal precedent; it is a matter of economic and political benefit. As the decades pass by, industrial inventions and economic conditions bring about changes so important that our legislatures and our courts are gradually forced to recognize them. The clause in the Constitution of the United States concerning commerce between the States, in the minds of the members of the Constitutional Convention of 1787, referred to local tariffs, to commerce on a small scale by water, or to petty traffic in wagons over state boundary lines. If our Constitution is to do its work, it must gradually have its meaning adapted by Congress and the courts to new conditions as they arise, and no technical interpretation in a judicial decision can ultimately stand against the interests of the community as they are affected by economic

changes. Our courts declare the law, it is true, but in declaring the law, they must keep in mind the fact that the intention of prime importance in the minds of our forefathers was the welfare of the people throughout the coming generations; and they will not rigidly insist upon an unchanging application of old words to new conditions. The Courts will of course be slow and careful in their adaptations of laws to new conditions, but eventually the conditions will force the reasonable interpretation. Some people are of the opinion that our Courts of last resort would be strengthened in this kind of work if one or two members were men trained primarily not in law but in the principles of business. The suggestion is worth careful consideration. In the discussion of such questions as these just asked, therefore, the point chiefly to be kept in mind is this: Are the local and state governments so organized that they can meet the new economic conditions? We need not now inquire what specific conditions the founders of our government had in mind when they wrote the Constitution, with the added thought, perhaps, that we must, so far as possible, attempt to hold ourselves back to the conditions of a century ago. With present conditions in mind, federal control of interstate railroads seems the only reasonable control.

CONTROL DETERMINED BY PEOPLE'S ECONOMIC HABITS
AND CHARACTER.

c. We must keep continually in mind also as important factors, determining the extent and nature of government control, the character and industrial habits and temper of the people. If the citizens of a country are ignorant, unenterprising, poor, weak, they will have little initiative and the government must take into its own hands the organization, financing and management of

important industrial enterprises until the people can themselves be trained by observation and gradually increasing experience to undertake them. It may be that in many instances, the government which thus controls and directs large industrial enterprises, and which should act for the benefit of the people as a whole, will be corrupt, and that considerable profits, even great fortunes, will be turned into the pockets of the corrupt officials. But even granting that this may be done (for I wish to blink no truth, however unseemly), the evil is probably only temporary and one that is perhaps in some countries almost to be expected. Even under the most adverse circumstances the benefit to the people from the industries and from the training which they get along industrial and political lines will in all probability bring them further forward in civilization and will enable them sooner to get both the honest control and the economic benefit than if the undertaking of the enterprise were delayed until among the people themselves were found men with the initiative and the capital to direct a great industrial enterprise, like, for example, the building of the Assouan dam in Egypt or the Trans-Siberian railway, or the Panama Canal.

On the other hand, if the people are intelligent, enterprising, wealthy, in very many instances they will develop the industries of a country without political danger far more rapidly by themselves under merely slight governmental supervision than such enterprises could possibly be developed by the government itself.

BY PEOPLE'S HABITS OF POLITICAL INDEPENDENCE OR
SUBSERVIENCE.

d. Again, if a people have been for generations under rigid governmental control, being used to dictation and subservience, the government management becomes both

easier and more necessary, while a people that is alert, ambitious, and used to self-direction, will, in general, prefer to do its own work and can successfully do it.

BY NATURE OF INDUSTRIES CONCERNED: THOSE CONNECTED WITH GOVERNMENT.

e. 1. The character of the industry, too, affects strongly the extent and nature of governmental control over it. Certain industries are so closely associated with the government that it is practically essential that the government manage them. The necessity of careful and rapid transmission of intelligence on government business led governments, even in ancient times, to establish post roads and relays of messengers by whom orders could be sent from the central government to outlying provinces. Gradually out of this necessity of government has grown our post-office system which seems now to exist primarily for the conduct of private business; but if, as at times has been suggested, the post-office business were to be put into private hands, the government would still need to exercise control so rigid that its own messages would certainly be carried promptly and secretly. For similar reasons governments as a rule erect their own forts, maintain their own arsenals, and usually build their own warships. Entirely aside from the question of relative cost, most governments will prefer to build their own war-ships; and even where this is not done in their own yards, the government control must be absolute.

THOSE OF PRIME IMPORTANCE TO THE PEOPLE.

e. 2. Even some industries that are not practically a part of the government's business, may yet be of so fundamental concern to practically all citizens that it would be considered dangerous to leave them in private

hands, provided the individuals concerned could make of the business a matter of personal profit. For this reason the coinage of money is considered a function of sovereignty. Banks are put more strictly than most other lines of industry under government control. In our own country, since education is looked upon as the foundation of good government, our schools have become public schools and the element of personal profit has been almost entirely eliminated from our educational system. It may seem odd to class schools with industries, but some schools, I fear, grind out graduates for profit. Still schools run for private profit now occupy a very subordinate position and are to be considered only as supplementary to our public schools for the benefit of those who have liberal means of support. The extension of our post-office facilities into remote country districts, where the receipts do not nearly cover expenses, is justified on the same grounds. The cheap and rapid transmission of information, as a means of education, must be carried even into districts where a private corporation could not afford to do the work.

THOSE REQUIRING GREAT CAPITAL WITH RETURNS LONG
DELAYED.

e. 3. In earlier times, before the financial resources of the leading countries were so great, and before the corporation as a method of business organization had become common, all enterprises requiring great capital had to be in the hands of the government in order that the resources of the country could be tapped by taxation to undertake them. Under modern conditions in Europe and America this is no longer necessary, but wherever the returns from the investment are only remote, governments still sometimes need to undertake such enterprises.

Several of the most important governmental activities in the United States to-day, although industrial in nature, are of this type, especially those which relate to the development and conservation of our national resources. Foremost in the public eye is the Panama Canal; but of scarcely less importance are the noble plans of the present administration for the development of our great inland water-ways, the bringing under cultivation through irrigation of vast tracts of territory otherwise arid and useless, the reclamation of swamps and bayous through the building of levees and drainage ditches, and the rapidly developing movement for the conservation and eventually the profitable cultivation of our forests. All these enterprises are of such a nature that, although they are fundamentally industrial and ultimately enormously profitable, the government, to protect the interests of coming generations, must exercise immediate control and in most cases must carry on the industry as a government enterprise. Most of these colossal undertakings, however, are of such a nature that the larger part of the direct work can be done, if necessary, through the aid of private corporations, the government retaining ownership and exercising control in the careful inspection and supervision of contracts.

THOSE MENTIONED BY JEVONS: MONOPOLISTIC, SIMPLE,
PUBLIC, NEEDING LITTLE CAPITAL.

e. 4. It has been the usual experience that wherever the element of private profit enters into the management of industry, the work of administration is likely to be more efficient and the cost of production decidedly lessened, so that we need to note what kinds of industries may be managed by the government with least waste. In 1867, in his address before the Manchester Statistical So-

ciety, defending the direct management of certain lines of business by the state, Professor Jevons laid down in his suggestive way the following principles concerning the industries, and the only industries, he thought, which could wisely be managed by the state :

1. Where numberless widespread operations can only be efficiently connected, united and co-ordinated, in a single and extensive government system.
2. Where the operations possess an invariable routine-like character.
3. Where they are performed under the public eye or for the service of individuals, who will immediately detect and expose any failure or laxity.
4. Where there is but little capital expenditure, so that each year's revenue and expense account shall represent, with sufficient accuracy, the real commercial conditions of the department.

The post-office is perhaps the best example of such an industry. Professor Jevons thought these principles applied fairly well to the telegraph and parcels post, but not to railways. As applied to England thirty years ago his opinion was probably sound. The experience of the last few years would probably permit in several countries some extension of these principles; but they are still extremely suggestive and useful in testing industries which the government contemplates managing.

GREAT EXECUTIVE TALENT BEST PAID BY PRIVATE
COMPANIES.

6. The success of all great industrial enterprises depends largely upon the executive head—he must be interested and be as intelligent and as skilful as possible. Such men must ordinarily be chosen only for the sake of the business itself. The experience of centuries has shown that, take it by and large, the motive of self-interest is the one that can best be counted upon to

secure the best executive talent. Under our present stage of civilization private corporations will give higher pay and better facilities for individual initiative and skill in work than is possible for the State in the present condition of public opinion. It is generally conceded here as well as in England that lawyers and captains of industry receive far greater rewards in private life than in public. Some striking examples have been afforded in recent years by the men who abandoned the greatest engineering enterprise of the present century, the Panama Canal, in order to enter the service of private corporations.

BUT MEN SERVE ALSO FROM SENSE OF DUTY.

And yet, on the other hand, the attractiveness of public service for its own sake and for the sake of the distinction of office or from the sense of patriotic duty, is likewise not wanting. Men now in the Cabinet, on the bench of the Supreme Court of the United States and in the Courts of Appeal in our states, have sacrificed tens and scores of thousands of dollars a year to enter the public service. Every person of wide acquaintance can mention instances from among his own list of friends. It is perhaps most usual to find instances of devotion to public service among men who have been especially trained for that, as in our officers in the army and navy. The only possibility of special reward for men of this type is the added reputation of doing excellent work in a position of great responsibility and the consciousness of duty well done. The spirit inculcated at Annapolis and West Point stands ready to sacrifice self if necessary for the sake of duty. I am glad to say that I have found not a little of this same spirit of devotion to duty in the civil service. I think it is rapidly extending and that this will soon materially affect our government work. On the other hand, men trained to rigid unquestioning obedience,

whose entire life is placed at the disposal of their superiors from day to day, are, I think, likely to lack somewhat in the personal initiative demanded of those whose way from obscurity to success must be fought through stern competition. In private management of business the weak are ruthlessly cut out, the strong move forward. In public life men are much more likely to receive positions through political pressure or through a type of examination that does not give the best test of efficiency, or through routine work and length of service. For these reasons we ordinarily expect to find, and experience shows that the expectation is well-founded, that enterprises will generally be carried through more promptly and with less expense in the hands of private managers than under public management.

ATTITUDE TOWARDS SOCIALISM.

7. These circumstances indicate clearly the wise attitude toward socialism, if by socialism we mean the policy of taking into the hands of the state for ownership and management the capitalistic industries. Possibly such a policy may be best in some ages and climes; such a policy, however, could be successful in modern industry only by a change of human attributes or of social conditions so great as to be practically revolutionary. An avaricious man is not likely to become public-spirited in office; he will rather prostitute his office to personal gain.

We need not, however, be frightened by a name. It may well be, that, under certain circumstances, a city may find it wise to own and manage its water works and its street railways; under other circumstances for special reasons, usually political, a state must administer its railway system; again, a great manufacturing enterprise or a gigantic work of public betterment may wisely be carried through by the state. Experience, however, in

various ways and under differing circumstances will show that for the present at any rate such instances are, relatively speaking, rare. Wherever it is made clearly probable that the policy of public management is wise, it should be adopted; but it would be unwise to declare off-hand that all capitalistic enterprises at any time in any future, however remote, can best be managed by the state. It is unsound even to put that forward as a desirable end. The end looked for is the welfare of the citizens. Wherever and whenever that can best be secured by public ownership and management there can be no objection to such form of enterprise. Under present conditions such a policy is relatively seldom wise, for both economic and political reasons. The burden of proof in each case rests upon those advocating it.

AND TOWARDS ANARCHY.

The other extreme of governmental policy, scientific anarchy, or the practical abandonment of all governmental control, is still less often possible; but we may freely concede that either socialism or scientific anarchism in special ages and in special countries might be wise.

CONTROL BY COMMISSIONS OR INSPECTORS.

8. Less rigid and less difficult than direct management is the control that governments may have in connection with the system of private enterprise. A legislature or the executive may lay down fixed rules for certain lines of industry, and a commission or an inspector may apply these rules in special cases. We have in many states railway commissions and bank inspectors whose work is largely judicial in nature. This kind of work does not demand so ambitious a talent, nor a talent so high-priced, although the judicial gift is no less useful to the public, and possibly no less rare than those of the captains of

industry. Even, therefore, where it seems best to abandon the idea of direct public management of industry, it is well within the power of the government and may much more frequently be found advisable to adopt a system of rigid public control.

EFFECTS OF GOVERNMENTAL MANAGEMENT UPON THE
PEOPLE.

9. Of vastly more importance than the immediate economic result, whether good or ill, of the government management of industry, are the indirect effects upon the temper and intelligence and development of the people. The effects of government activity in industry are some of them good, some bad. It is desirable to discriminate carefully, and in determining a government's policy to perform so far as possible only acts that will have a good effect upon the people.

IT MAY SET AN EXAMPLE TO PRIVATE ESTABLISHMENTS.

As has already been explained, the government activity in behalf of the general welfare can at times be carried out on lines impossible for a private company. It is possible for the government, if necessary, to support an industry in part by taxation, as, in order to increase the general intelligence, we in part support our post-office. For the same end the Government may in certain lines make experiments, industrial as well as political. With careful regard for cost of work and justice to the taxpayer the Government in its industrial enterprises should lead and educate public opinion in promoting the welfare of society. In all government enterprises, a standard of excellence should be set in the quality of work done, in the conditions of work of the laborers, in strictness of accounting, in upright management.

IT SHOULD FIX LIMITS OF COMPETITION.

It may sometimes be desirable, in order that the benefits of private enterprise may be secured without giving to private corporations the unreasonable profits which under certain monopolistic circumstances they might be able to secure, that the government compete directly with private enterprise in order to hold prices within reasonable bounds. It might become best for the post-office, for example, to extend its parcel post in competition with the express companies. Ordinarily, however, the government can best direct the private management of public enterprises through inspection and supervision rather than by direct competition. We must recognize the fact that competition affords on the whole the best stimulus to effort, to originality of thought, and to the development of personality in enterprise. The government may thus, as already intimated, speaking generally, secure the public welfare best by encouraging private enterprise, simply fixing the limits of competition within standards of honesty and efficiency of service. This principle of competition, too, it should be recognized, is found not merely in business where the reward is money profit, but likewise in all other fields of endeavor, where the reward may be fame or merely a spirit of self-satisfaction over good work well done. There is competition in football, even in philanthropy, as well as in money making. The government should simply see to it that the competition in all directions is kept within fair and just limits.

THE GOVERNMENT CANNOT ESCAPE THE RESPONSIBILITY OF CONTROL.

10. Whether the government will or no, it cannot throw off the responsibility of supervision and control over such industrial enterprises as we have considered,

and it seems certain that, unless business men learn to recognize more fully their obligations to the general public, the government must extend the range of its control.

IT MUST EXTEND ITS CONTROL UNLESS BUSINESS
PRACTICE CHANGES.

II. Many of the business men of the country do not yet fully recognize their obligations to the public, nor do they see clearly the fiduciary character of their business. They are trustees for the public in no small degree. They excuse themselves for many acts inimical to the interests of the public on the ground that they may prove beneficial to their stockholders—and this in all good faith. With the increase in the size and complexity of business organizations, however, the principle of *caveat emptor* ought not to be made to apply in general. The common man cannot care for his own interests. A depositor in a bank, for example, cannot of himself judge the risks he is taking. If the banker will not carefully protect his depositor, the Government should compel him to do so by more rigid control.

RELATION OF THE PANIC TO GOVERNMENT CONTROL.

The fact is that the late widespread suspension of cash payments throughout the country, disguised somewhat by the use of clearing house certificates and other devices, and by the fact that bank notes were safe, is a public calamity due less to the activity of any government official than to the need of more rigid government control. Failure to honor a check in cash is enough of the nature of failure to redeem a bank note so that such an act ought not to be passed over lightly. Our bankers, in order to pay high returns to their stockholders, had in some instances gone much beyond the limit of safety in reducing

their reserves. They had too often resorted to practices doubtful for a fiduciary business; they had counted deposits in other banks as part of their own resources, a practice which, though legal, is of doubtful wisdom, and when the storm came, each looking to his own need (with the exception of some of the larger establishments whose own close relations with the market compelled action), got what cash he could and retained it in his vaults, thus increasing the tension of the stringency. Unless the bankers can devise better plans than they now practice for checking the reckless among their fellows and heartening the over-cautious, the Government must play a more active part in control. I do not mean that the Treasury is to be more active in an emergency. The government must do more to prevent the emergency's arising. And this principle applies, not only to banks, but with greater emphasis to all great companies, railroads and trusts, whose stocks are at the mercy of the directors, and the prices of whose products within rather broad limits are only slightly regulated by competition. What does a stockholder in a great corporation like the American Tobacco Co., or the American Sugar Refining Co., or the Standard Oil Co., or any of the 50 largest Trust companies, know of the real value of his holdings and of what may be done within three months to increase or lower the value? And what does the public know of the measures that may be taken to increase or lower the prices which the grocers must pay the manufacturing companies for their goods? Business men in these important positions will in time learn their duty toward the public, but probably the Government must lead the way. The change from small industrial conditions to large has come so swiftly that the business men in most cases are not morally to blame for their lack of adjustment to new con-

ditions, but they will be blameworthy, if they delay, and the Government does well to stimulate their activity.

SUMMARY.

12. It would be beyond my purpose at the present time to apply these general principles to specific cases in the United States, and to give my opinion as to exact rules that the Government should lay down or as to the industries which the public should own or control. I consider only a few general principles. This much may be said in summary. In the discussion of such questions as public control of public service corporations we ought not to be swayed at all by the fear that we shall be called either socialists or scientific anarchists. We should recognize that there is much truth in the teachings of those who advocate government ownership and management; perhaps an equal amount of truth in the teachings of those who advocate the let-alone policy carried to the extreme. The public and scientific thinkers owe a debt to both classes. It is our duty to judge each individual case on its own merits, taking into account local conditions, industrial, political, and personal. Moreover, we should recognize the fact that society and political institutions are changing and progressing and that a policy wise to-day may be unwise twenty years hence; that a policy successful in Europe will probably not be equally successful here; that in no case can we accept as conclusive the experience of others or even our own present experience; and that on the whole the government probably needs to extend its control especially over the larger companies, unless their managers take the public more fully than now into their confidence. In every case our final appeal is to common sense, good judgment, and an unselfish regard for the public welfare.