Michigan Law Review

Volume 36 | Issue 8

1938

CONSTITUTIONAL LAW -VALIDITY OF REGISTRATION PROVISIONS OF PUBLIC UTILITY HOLDING COMPANY ACT OF 1935

Gerald L. Stoetzer
University of Michigan Law School

CONSTITUTIONAL LAW — VALIDITY OF REGISTRATION PROVISIONS OF PUBLIC UTILITY HOLDING COMPANY ACT OF 1935 — In recognition of the abuses that arise from the monopolistic tendencies of holding companies in the public utility field and of the inability of the respective states to exert the necessary control thereof,[1] Congress has attempted to draw certain of the public utility holding companies within the inquisitorial and regulatory control of the federal Securities and Exchange Commission. The Public Utility Holding Company

[1] That the respective states have no effective means to prevent or regulate, or even promptly learn about the acquisition of control of local operating utilities by holding companies incorporated in another state indicates the need for some adequate form of federal control of utility holding companies. New Hampshire Gas & Electric Co. v. Morse, (D. C. N. H. 1930) 42 F. (2d) 490. The tenor of the congressional debates prior to the passage of the Public Utility Holding Company Act further shows that absentee and out-of-state ownership negatives the ordinary exercise of control through state utility commissions. 79 CONG. REC. 9049 (1935). In general, see Buchanan, "The Public Utility Holding Company Problem," 25 CAL. L. REV. 517 (1937).

Act of 1935,[2] reciting in great detail facts showing the necessity for control of holding companies having as subsidiaries electric and gas operating utilities, indicates that Congress regarded the uncontrolled utility holding company as "an agency which, unless regulated, is injurious to investors, consumers, and the general public."[3]

The significance of this effort to control the "super-holding company" which has tended to concentrate the control of the electric and gas operating utilities may more readily be realized when the fact is considered that thirteen large holding company groups control three-quarters of the privately-owned electric utilities in the country, and that three of these holding company groups control over forty per cent of the entire industry.[4] Still, it must be recognized that there are advantages in the holding company system. The combined technical knowledge and executive skill of its management *may* be utilized to reduce the actual costs of construction and operation and to extend and improve services.[5] But however great the advantages may be, the Federal Trade Commission and the National Power Policy Committee have found that the unsound capitalization of holding companies has operated to the detriment of investors and consumers alike.[6]

Section 1 (b) of the Public Utility Holding Company Act declares that the national public interest, the interest of investors in the securities of holding companies and affiliates, and the interest of consumers of electric energy and natural and manufactured gas, are or may be

[2] 49 Stat. L. 803 (1935), 15 U. S. C., (Supp. 1937), § 79a.

[3] 15 U. S. C. (Supp. 1937), § 79a (c). Since monopoly is accepted as the economically sound form of organization of operating utility companies, "Regulation by government rather than by the forces of competition is relied upon to insure good service at reasonable rates. . . . So far as concerns the industrials, interest in the holding companies has reference largely to their use in concentrating control and to the extent to which they have been employed to defeat the objects of the anti-trust laws. As far as concerns the public utilities, interest is centered rather in the question to what extent control by holding companies may have resulted, designedly or undesignedly, in thwarting the forces of government regulation." BONBRIGHT AND MEANS, THE HOLDING COMPANY 90-91 (1932).

[4] H. Doc. 137, 74th Cong., 1st sess. (1935), p. 4. "The desire of engineering and manufacturing groups to secure control of the maximum of utility properties in order to sell commodities and services to these utilities, and the desire of bankers to dominate utility managements in order to secure promotion and underwriting profits, has often resulted in the formation of unwieldy systems of holding companies which could not possibly be justified on grounds of engineering or managerial efficiency. The freedom of the holding company from control by the public service commissions has also been a serious menace—a menace so great that it threatens the whole American scheme of private ownership under governmental rgulation." BONBRIGHT AND MEANS, THE HOLDING COMPANY 93 (1932).

[5] S. Doc. 92 (part 24), 70th Cong., 1st sess. (1928), p. 419.

[6] S. Doc. 92 (part 72-A), 70th Cong., 1st sess. (1928), p. 327; H. Doc. 137, 74th Cong., 1st sess. (1935), p. 7.

adversely affected when the necessary information cannot be obtained to appraise effectively the financial position or earning power of the issuers, as well as when such securities are issued without approval of the respective states having jurisdiction over the subsidiary operating companies. Those interests are declared, further, to be affected when the subsidiary utilities are subjected to excessive charges for services, construction work, equipment and materials, contracts for which are not consummated as the result of arm's-length bargaining. Likewise, such interests are found to be adversely affected when holding company control of subsidiaries affects the rate, dividend and other policies of the latter as to complicate and obstruct state regulation; so, too, when growth and extension of holding companies becomes inconsistent with economical management and operation of subsidiaries.[7]

The national public interest, which necessarily is the basis of the control and regulation of such holding companies, is found to exist in that securities thereof are distributed by means of the mails and instrumentalities of interstate commerce; that their service, sales, construction and other contracts are generally made through the same means; that use of instrumentalities of interstate commerce is often made by utilities to transport gas and electric energy; that the interstate commerce of the subsidiaries is affected by the holding company control; and finally, that effective state regulation of utilities is constrained by the interstate character of the activities of the holding companies.[8]

Thus the act is directed at the holding company which controls operating utilities in states other than that of its incorporation and which makes use of the means and instrumentalities of interstate commerce and the mails to execute the holding company purposes. Congress clearly intended to regulate only the interstate holding company, and then only those holding companies which, under the provisions of the act, actually control electric or gas utilities.[9]

Since the scope of this comment is limited to a discussion of sections 4 and 5,[10] the registration provisions, suffice it to say that the other regulatory provisions expressly relate to the registered holding company and that they concern the issue and sale of securities, the acquisition of security and utility assets, corporate simplification and reorganization, service contracts and other inter-company transactions, and reports and accounts.[11]

[7] 15 U. S. C. (Supp. 1937), § 79a (b).
[8] 15 U. S. C. (Supp. 1937), § 79a (a).
[9] 15 U. S. C. (Supp. 1937), §§ 79b (a) (7), 79c (a) (1).
[10] 15 U. S. C. (Supp. 1937), §§ 79d, 79e.
[11] 15 U. S. C. (Supp. 1937), §§ 79f-79o. For a discussion of these sections of the act, see 30 ILL. L. REV. 648 (1936) and 23 VA. L. REV. 678 (1937). As to section 11, the "death sentence" provision, see in this issue: 36 MICH. L. REV. 1360 (1938).

I.

A public utility holding company for the purposes of this statute is "any company which directly or indirectly owns, controls, or holds with power to vote, ten per centum or more of the outstanding voting securities of . . . [an electric or gas] public-utility company or of a company which is a holding company by virtue of this clause."[12] Likewise, a "subsidiary" is a company actually controlled by the holding company, and not simply one in which the holding company has a substantial interest.[13] The presumption that ownership of ten per cent of the voting stock constitutes control, fixed to facilitate the administration of the act and to prevent evasion, can readily be rebutted, upon application by a mandatory procedure either by the putative holding company or the putative subsidiary, upon a showing that the company does not in fact exercise control.[14] Thus a bona fide investment company is not affected by the act.

To provide an effective means of control over utility holding companies falling within the purview of the statute, the act declares, in section 4 (a) that

> "*unless a holding company is registered under Section 5*, it shall be unlawful for such holding company, directly or indirectly—(1) to sell . . . own or operate any [electric or gas] utility assets . . . in interstate commerce; (2) by use of the mails or any means or instrumentality of interstate commerce, to negotiate . . . any service, sales, or construction contract undertaking to perform services or construction work for, or sell goods to, any public-utility company or holding company; (3) to distribute or make any public offering for sale or exchange . . . [of securities of the holding company, affiliate, or subsidiary] by use of the mails . . . (4) by use of the mails or any means or instrumentality of interstate commerce, to acquire or negotiate for the acquisition of any security or utility assets . . . (5) to engage in any business in interstate commerce; or (6) to own, control, or hold with power to vote, any security of any subsidiary company thereof that does any of the acts [above] enumerated. . . ."[15]

[12] 15 U. S. C. (Supp. 1937), § 79b(a) (7).

[13] 15 U. S. C. (Supp. 1937), § 79b (a) (8).

[14] Sections cited, notes 12 and 13, supra. The rebuttable presumption established by the act appears to be reasonable for "practical control of a corporation can be exercised, often is exercised and retained, through the ownership by those who are already in managerial control of a substantial minority of the voting power." S. Doc. 92 (part 72-A), 70th Cong., 1st sess. (1928), p. 143.

The ownership of a substantial minority of voting stock is sufficient to assure control, especially where the remaining voting stock is widely held. United States v. Union Pacific R. R., 226 U. S. 61, 33 S. Ct. 53 (1912).

[15] 15 U. S. C. (Supp. 1937) § 79d (a) (1-6) (italics added).

On the other hand, in order to engage lawfully in the activities above described, the holding company must *register* with the Securities and Exchange Commission in accord with the provisions of section 5 (a). This requires the filing of a "notification of registration, in such form as the Commission may by rules and regulations prescribe as necessary or appropriate in the public interest or for the protection of investors or consumers."[16]

While section 5 (b) expressly applies only to registered companies and hence, ostensibly, is beyond the scope of this comment, discussion thereof is indeed pertinent. This subsection requires that a registration statement be filed within a reasonable time after the notification of registration:

> "Such registration statement shall include—(1) such copies of the charter or articles of incorporation . . . bylaws, trust indentures, mortgages, underwriting arrangements, voting-trust agreements . . . relating to the registrant or any of its associate companies . . . (2) such information . . . in respect of . . . [the organization and financial structure of the companies and nature of business; outstanding securities; terms and underwriting arrangements of prior public offerings; names, remuneration, interest in securities, material contracts, and borrowings of directors and officers; bonus agreements; extraordinary service, sales and construction contracts; options in respect of securities; balance sheets and profit and loss statements] (3) such further information . . . necessary or appropriate in the public interest or for the protection of investors or consumers."[17]

Briefly, then, section 5 provides for the mechanics of registration, while section 4 outlines the penalties for non-registration.

[16] 15 U. S. C. (Supp. 1937), § 79e (a). Form of notification of registration requires the following information in reference to the registrant and the subsidiaries thereof: (1) exact name of registrant; (2) address of principal executive offices; (3) name and address of officer to whom communications may be sent; (4) classification and relation of subsidiaries—names, type of organization, state of organization and type of business. Form U5A, CCH SECURITIES ACT SERVICE, ¶ 8459, authorized by Rule 5A-3 of the Securities and Exchange Commission. S. E. C. Release 382, Oct. 5, 1936, amended by S. E. C. Release 673, May 26, 1937. CCH SECURITIES ACT SERVICE, ¶ 8369B.

[17] 15 U.S. C. (Supp. 1937), § 79e (b). This registration statement must be filed within ninety days after the filing of the notification of registration. Rule 5B-1. CCH SECURITIES ACT SERVICE, ¶ 8370. Registration is deemed to have been consummated upon receipt by the commission of such notification of registration.

Form of registration statement requires the following information: (1)-(4) the items specified in the notification of registration; (5) general character of business during the preceeding five years (including subsidiaries); (6) character and location of principal plants and equipment; (7) total sales of electrical

In order to induce other holding companies to register, the Securities and Exchange Commission, immediately prior to the effective date, filed a bill to compel the Electric Bond & Share Company and fourteen associated holding companies in its system[18] to comply with

energy and gas including interstate transactions for previous calendar year; (8) funded debts and capital structure of registrant and subsidiaries; (9) tabulation of such securities held by registrant and subsidiaries; (10) investments in holding and utility companies that are not subsidiaries of registrant; (11) indebtedness to any one person aggregating more than $50,000 or one-half of one per centum of total debit accounts, whichever is the lesser; (12) leases of like figure; (13) sales of large bond or stock issues during previous five years; (14) agreements by registrant or subsidiary as to future distribution of issues of securities; (15) list of twenty largest holders of each class of stock of registrant and the number holding, respectively, more and less than one thousand shares each and aggregate; (16) names, addresses and compensation of directors and officers in the holding company system; salaries of employees over $20,000; debts of officers and directors exceeding one thousand dollars; contracts of same with the system; what officers and directors are officials in banks or investment companies; (17) interest of trustee under indentures; (18) contracts of continuing nature; (19) existing litigation of certain types.

Exhibits to be attached to the registration statement: (A) percentage of each class of voting securities of each subsidiary held by registrant and subsidiaries; (B) charters and by-laws of registrant and subsidiaries; (C) funded debts in excess of one million dollars or ten per cent of total debit accounts; (D) consolidated statements of income and surplus of registrant and its subsidiaries for the previous fiscal year, in addition to a consolidated balance sheet; (E) for each utility in system, maps showing service area, plants, etc.; (F) copy of annual report submitted to stockholders; (G) reports filed with state commissions; (H) typical forms of service, sales, or construction contracts. Form U5B, CCH SECURITIES ACT SERVICE, ¶¶ 8459E-8459H; authorized by Rule 5B-1, adopted by S. E. C. Release 382, Oct. 5, 1936 and amended by Release 673, May 26, 1937, CCH SECURITIES ACT SERVICE, ¶ 8370.

[18] The Electric Bond & Share Company is what is known as the "top holding company" in a holding company system, being the parent corporation (first organized in 1905 by General Electric Company with a capitalization of $4,000,000) owning substantial minorities of voting securities of other holding companies which in turn own directly or through sub-holding companies substantial majorities or voting control of operating gas and electric utilities. Bond & Share was utilized in this manner for the purpose of acquiring a controlling interest in numerous operating utilities throughout the country, the voting securities of which were in turn exchanged for the securities of sub-holding companies; these, except for a minority but controlling voting interest, were sold to the public along with non-voting securities. Bond & Share in its subsidiary, American Gas & Electric Company, exercised supervision over the operations and financial affairs of all these companies, for a substantial fee; General Electric, having contractual arrangements with Bond & Share, was thereby able to obtain much of the equipment business in the Bond & Share system. The other companies in the Bond & Share system had a similar development.

The system embraces property of operating electric utilities in thirty-two states, serving ten per cent of the electric customers in the United States, while it handles more than twenty-five per cent of the total electric energy transmitted across state lines. Further, the gas business of the system extends through fifteen states, serving four hundred and fifty thousand customers, handling twenty per cent of the interstate gas business. The annual revenues from electric and gas operations in the system aggregate $259,600,000.

sections 4 (a) and 5.[19] A decree issued against Electric Bond & Share and the seven associates which continued to be holding companies within the meaning of the statute, requiring them to register, or be restrained from carrying on any of the activities in interstate commerce or through the use of the mails forbidden to non-registered holding companies.[20] The District Court for the Southern District of New York further decreed that the holding companies were free to challenge later the validity of the other provisions of the act, a declaratory judgment as to the constitutionality of the entire act having been denied. The Securities and Exchange Commission had already issued a rule that registration could be made, with full reservation of con-

As a result of pyramiding of holdings by means of numerous intermediate holding companies, Bond & Share has been able to exercise control over the operating subsidiaries through the ownership of voting securities, voting trusts, interlocking directorates and officers, management contracts, control of proxies, and service arrangements.

After the passage of the Act, Bond & Share formed the wholly-owned subsidiary, Ebasco Services, Inc., which was to continue performance of the service contracts with substantially the same service personnel of Bond & Share. Thus through Ebasco, Bond & Share continued to render expert specialized and technical services, which had netted Bond & Share nearly three million dollars annually during the previous few years. Furthermore, a wholly-owned subsidiary of Ebasco, Phoenix Engineering Corp., was thereupon organized to perform the construction contracts for the various operating subsidiaries in the system. Brief for the Government, Appendix B, Electric Bond & Share Co. v. Securities and Exchange Commission, pp. 5-100.

The violations alleged by the government and found by the district court: Bond & Share through direct and indirect control of operating subsidiaries engaged in transmission and transportation of electric energy and gas in interstate commerce, violated section 4(a) by continuing to operate such utilities in interstate commerce, perform service, sales and construction contracts, and deal in securities of holding and operating utilities; Bond & Share, a holding company within the definition of the act, refused to register under section 5. The same allegations were interposed as to the other defendants. Securities & Exchange Comm. v. Electric Bond & Share Co., (D. C. N. Y. 1937) 18 F. Supp. 131.

[19] Several days prior to the effective date of the act, the North American Co. filed a bill (similar to fifty others throughout the country) in the supreme court for the District of Columbia to restrain the Securities & Exchange Commission, the Attorney General, and the Postmaster General from enforcing the act because of alleged unconstitutionality. The Supreme Court of the United States, granting certiorari to the Court of Appeals of the District of Columbia, held that the trial court had the power to grant the stay prayed by the government. Landis v. North American Co., 299 U. S. 248, 57 S. Ct. 163 (1936). This case has been interpreted as allowing the government to initiate a test case, such as the Electric Bond & Share case, to determine the validity of legislation of a penal nature. See 50 HARV. L. REV. 655 at 658 (1937) as to the procedural aspects of litigation under the Public Utility Holding Company Act.

[20] Securities & Exchange Comm. v. Electric Bond & Share Co., (D. C. N. Y. 1937) 18 F. Supp. 131.

stitutional rights.[21] Upon affirmance by the Circuit Court of Appeals for the Second Circuit[22] and the granting of certiorari,[23] the United States Supreme Court, in *Electric Bond & Share Co. v. Securities and Exchange Commission*,[24] recently approved the disposition made of the suit in the district court. It was there held, not only that the registration provisions were separable, but that they constituted valid and sufficient regulation under the commerce clause, apart from other control provisions in the act; that the penalties for non-registration were consistent with the powers of Congress in that respect; and that the declaratory judgment as to the constitutionality of the act as a whole was properly denied.

2.

One of the primary contentions of the holding companies was that sections 4(a) and 5 are not separable from the remainder of the act and that they could not be enforced apart from the other regulatory provisions, even though the latter apply only to registered holding companies.[25] While section 32 expressly provided for separability, no more than a presumption is established thereby.[26] Hence it was argued that section 4 (a) merely decrees holding companies to register, so as to be subjected to the controls provided for in the balance of the act, that

[21] Rule 4, adopted in S. E. C. Release 4, Oct. 9, 1935, as amended by Release 23, Nov. 22, 1935. CCH SECURITIES ACT SERVICE, ¶ 8351C. See 48 HARV. L. REV. 988 (1935). Except for the test case, the government has made no effort to enforce the act, pending a determination of the constitutionality. Thus the Attorney General issued instructions that no steps be taken to enforce the same, while the Postmaster General decreed that holding companies failing to register should not be deprived of the use of the mails. 3 U. S. LAW WEEK 246 (1935).

[22] Electric Bond & Share Co. v. Securities & Exchange Comm., (C. C. A. 2d, 1937) 92 F. (2d) 580, noted in 23 VA. L. REV. 678 (1937).

[23] 302 U. S. 681, 58 S. Ct. 411 (1938).

[24] (U. S. 1938) 58 S. Ct. 678.

[25] Cf. United States v. Butler, 297 U. S. 1 at 58, 56 S. Ct. 312 (1936) (court refused to separate the A.A.A. into two statutes, one levying an excise on prices of certain commodities, the other appropriating public monies independently of the first); Schechter Poultry Corp. v. United States, 295 U. S. 495 at 554, 55 S. Ct. 837 (1935) (court refused to separate the wages and hours provisions from the balance of the N. I. R. A.); Williams v. Standard Oil Co., 278 U. S. 235, 49 S. Ct. 115 (1929) (court refused to separate informatory provisions from unconstitutional price fixing provisions).

[26] 15 U. S. C. (Supp. 1937) § 79z-6. There is a presumption that, eliminating invalid parts, the legislature would have been satisfied with what remained. Champlin Refining Co. v. Corporation Commission, 286 U. S. 210 at 238, 52 S. Ct. 559 (1932); Utah Power & Light Co. v. Pfost, 286 U. S. 165 at 185, 52 S. Ct. 548 (1932); Lynch v. United States, 292 U. S. 571 at 586, 54 S. Ct. 840 (1934); Carter v. Carter Coal Co., 298 U. S. 238 at 335, 56 S. Ct. 855 (1936).

section 5 (a) provides the mechanics of registration, and that section 5 (b) requires the submission of the basic information upon which shall operate the specified controls.[27] A further objection might be raised that the publicity required in section 5 does not regulate or relate to the activities prohibited to non-registered companies in section 4 (a), but rather furnishes information for the administration of the other controls. A query might also be raised as to whether mere registration of holding companies will carry into effect the general purposes of the act, viz. to compel the simplification and elimination of the holding company systems, in the national public interest.

In considering the separability phase of the *Electric Bond & Share* case, Chief Justice Hughes concluded not only that the presumption of separability had not been overcome, but that such registration provisions alone could have been the subject of a separate statute. The Court declared that

> "The fact that registration underlies the application of subsequent requirements of the statute does not prevent the provisions of sections 4 (a) and 5 from having a purpose and a value of their own. . . . Thus section 5 (b) is itself a 'control' provision which is immediately operative. The duty to supply the described information is separately and definitely described."[28]

While the registration provisions standing alone might accomplish less than was intended by the entire act, as exemplified by section 11, the so-called "death sentence" provision, that fact does not militate against the possibility and effectiveness of separate operation and enforcement of the former. The informatory process through registration is an effective means of regulation of interstate commerce and has often been employed,[29] as in the Pure Food and Drug Act,[30] the Federal Trade Commission Act,[31] the Interstate Commerce Act,[32] the Federal Communications Act,[33] the Securities Act of 1933,[34] and the Securities and Exchange Act of 1934.[35] The district court in the *Electric Bond & Share* case in

[27] See Brief for the Defendants-Petitioners, Electric Bond & Share Co., pp. 45, 66-68.

[28] (U. S. 1938) 58 S. Ct. 678 at 684.

[29] Interstate Commerce Commission v. Brimson, 154 U. S. 447, 14 S. Ct. 1125 (1894); Interstate Commerce Commission v. Goodrich Transit Co., 224 U. S. 194, 32 S. Ct. 436 (1912); McDermott v. Wisconsin, 228 U. S. 115, 33 S. Ct. 431 (1913); American Telephone & Telegraph Co. v. United States, 299 U. S. 232, 57 S. Ct. 170 (1936).

[30] 34 Stat. L. 768 (1906), 21 U. S. C. (1935), § 1 et seq.

[31] 38 Stat. L. 717 (1914), 15 U. S. C. (1935), § 41 et seq.

[32] 24 Stat. L. 379 (1887), 49 U. S. C. (1935), § 1 et seq.

[33] 48 Stat. L. 1064 (1934), 47 U. S. C. (1935), §§ 151-155.

[34] 48 Stat. L. 74 (1933), 15 U. S. C. (1935), § 77a et seq.

[35] 48 Stat. L. 881 (1934), 15 U. S. C. (1935), § 78a et seq.

finding that the registration sections were capable of separate and satisfactory operation said, through Judge Mack:

> "Neither the efficacy nor the workability of the registration provisions as a regulatory device through publicity is affected by the other provisions of the act; there is no essential interdependence between them." [36]

That salutary publicity results from the process of registration is indicated by the nature of information required on the registration statement summarized earlier in this comment.[37] The information regarding the interstate holding company systems, for the protection of investors, consumers and the public, is similar to that required in the Securities and Exchange Act of 1934.[38] In addition to the effect of publicity in deterring some of the objectionable practices, there is then available the information which will guide the regulatory authorities, both state and federal.[39] The fact that there are limitations on the extent of publicity as to matters of a private or confidential character, where the public interest is not involved directly, is no argument against the regulatory effect of publicity in general.[40] Finally, from the view point of statutory construction, it appears that Congress intended that the registration provisions have the capacity of separate operation, for each of the control sections contains a separate provision for the filing of reports and information requisite to the administration of the particular objective provided for.[41]

3.

Some doubt has been expressed recently as to the constitutionality of the act because it extends beyond the scope of the federal powers.[42] But the purpose of the act is not to supplant the state utility commissions in their jurisdiction over rates and operating practices of gas and

[36] (D. C. N. Y. 1937) 18 F. Supp. 131 at 140.

[37] See summary of the registration statement form in note 17, supra.

[38] 15 U. S. C. (1935), § 78f.

[39] Securities & Exchange Commission v. Electric Bond & Share Co., (D. C. N. Y. 1937) 18 F. Supp. 131. See also Smith v. Illinois Bell Telephone Co., 282 U. S. 133, 51 S. Ct. 65 (1930); Federal Trade Commission v. Smith, (D. C. N. Y. 1932) 1 F. Supp. 247 at 255.

[40] Electric Bond & Share Co. v. Securities & Exchange Commission, (U. S. 1938) 58 S. Ct. 678 at 685. Cf. § 22 of the Holding Company Act, giving the commission discretion as to disclosure of matters in the registration statement and reports, with § 6 of the Securities Act. 15 U. S. C. (Supp. 1937), § 79v; 15 U. S. C. (1935), § 77f(d).

[41] E.g., 15 U. S. C. (Supp. 1937), §§ 79f(a), 79p.

[42] See 23 VA. L. REV. 678 at 691 (1937).

electric utilities within their separate jurisdictions, but rather to regulate the financial practices of the interstate holding companies controlling them. The federal statute thus is supplementary rather than conflicting.[43] In applying the act to the particular facts in the *Electric Bond & Share* case, there appears to be little doubt that Bond & Share and its affiliates are engaged in transactions in interstate commerce.[44] Such a finding is the basis of federal control under the commerce clause.[45] Nor is such federal jurisdiction impaired by the fact that "they conduct such transactions through the instrumentality of [intrastate as well as interstate] subsidiaries."[46]

Without disregarding the corporate entity theory, effective regulation may be realized by treating the holding company system as a unit. Hence section 4(a) (6) forbids the non-registered holding company to own or control subsidiaries engaged in the acts described in section 4 (a) (1-4), also forbidden the holding company. That suggests a consideration of the penalties imposed by section 4(a) generally, for the real controversy in enforcing a regulatory statute necessarily turns upon the sanctions provided. The sanctions prescribed in this section are in the nature of a denial of a privilege which would be otherwise enjoyed, a penalty with coercive effects. In brief, as already indicated, a non-registered holding company is denied the use of the mails or any instrumentality of interstate commerce in reference to its service,[47] sale or construction contracts with its subsidiaries, the making of public distribution of its own securities or those of affiliates and subsidiaries, or efforts to acquire security or utility assets of affiliates or subsidiaries.

While it is true that the mere *use* of the mails or instrumentalities of interstate commerce is not sufficient to give Congress the right to regulate more than the use of such instrumentalities,[48] a business engaging in interstate commerce, though through subsidiaries, is nevertheless subject to the federal regulatory power under the commerce

[43] See Gibbons v. Ogden, 9 Wheat. (22 U. S.) 1 at 197 (1824). Cf. New York Central Securities Corp. v. United States, 287 U. S. 12, 53 S. Ct. 45 (1932); Federal Trade Commission v. Western Meat Co., 272 U. S. 554, 47 S. Ct. 175 (1927); United States v. Union Pacific R. R., 226 U. S. 61, 33 S. Ct. 53 (1912); Northern Securities Co. v. United States, 193 U. S. 197, 24 S. Ct. 436 (1904).

[44] See note 18, supra.

[45] U. S. Constitution, art. 1, § 8: "The Congress shall have power . . . to regulate commerce . . . among the several states."

[46] Electric Bond & Share Co. v. Securities & Exchange Commission, (U. S. 1938) 58 S. Ct. 678 at 686.

[47] There is a discussion of the servicing function of the public utility holding companies in 49 HARV. L. REV. 957 (1936).

[48] See United States Fidelity & Guaranty Co. v. Kentucky, 231 U. S. 394, 34 S. Ct. 122 (1913); 23 VA. L. REV. 678 at 686 (1937).

clause.[49] As a matter of fact, section 4 (a) *does* constitute a regulation of the mails and instrumentalities of interstate commerce as much as of the holding companies themselves, for Congress has declared in the act that it is contrary to the public policy there expressed for non-registered holding companies to make use thereof.[50]

It follows, then, that "When Congress lays down a valid rule to govern those engaged in transactions in interstate commerce, Congress may deny to those who violate the rule the right to engage in such transactions . . . [for] the imposition of such a penalty does not transgress any constitutional provision." [51]

The Court has approved penalties in exercise of the protective power of Congress in interstate commerce in *Brooks v. United States*:

> "Congress can certainly regulate commerce to the extent of forbidding and punishing the use of such commerce as an agency to promote immorality, dishonesty or the spread of any evil or harm to the people of other States from the State of origin." [52]

But the national police power under the commerce clause is not limited to articles or communications transported which are inherently harmful. In *Securities and Exchange Commission v. Crude Oil Corp.*,[53] upholding the constitutionality of the registration provisions of the Securities Act of 1933, it was declared that Congress may condition the particular use of the means and instrumentalities of interstate commerce upon certain safeguards in order to effectuate a declared policy even though there is no intrinsic harm in the article transported. Likewise, in approving provisions of the Securities and Exchange Act (which involves not only publicity features, but also forbids certain transactions in securities by the use of the mails or instrumentalities of interstate commerce), *Securities and Exchange Commission v. Torr* held that:

> "It cannot be doubted that Congress may close the channels of interstate commerce . . . to such transactions in corporate securities

[49] See note 45, supra.

[50] ". . . the power to regulate interstate commerce resides in the Congress, which must determine its own policy." Kentucky Whip & Collar Co. v. Illinois Central R. R., 299 U. S. 334 at 347, 57 S. Ct. 277 (1937). Cf. Brooks v. United States, 267 U. S. 432, 45 S. Ct. 345 (1925).

[51] Electric Bond & Share Co. v. Securities & Exchange Commission, (U. S. 1938) 58 S. Ct. 678 at 686-687. To the same effect, see Champion v. Ames, 188 U. S. 321, 23 S. Ct. 321 (1903); United States v. Delaware & Hudson Co., 213 U. S. 366, 29 S. Ct. 527 (1909); Brooks v. United States, 267 U. S. 432, 45 S. Ct. 345 (1925); Gooch v. United States, 297 U. S. 124, 56 S. Ct. 395 (1936); Kentucky Whip & Collar Co. v. Illinois Central R. R., 299 U. S. 334, 57 S. Ct. 277 (1937).

[52] 267 U. S. 432 at 436, 45 S. Ct. 345 (1925).

[53] (C. C. A. 7th, 1937) 93 F. (2d) 844.

as it has reasonably found and declared to be directly detrimental to the financial health of the public generally."[54]

The federal postal power[55] is not limited to the protection of the facilities of the mails. It is likely that the power over the mails is broader than that over interstate commerce, since the government has a proprietary as well as regulatory interest in the former.[56] Thus Congress may exercise the postal power by preventing the use of the mails for purposes which it regards as repugnant to a sound public policy.[57] The use of the postal power in the Public Utility Holding Company Act, in prohibiting the use of the mails to non-registered holding companies, is comparable with a similar exercise thereof in the Securities Act of 1933,[58] sustained in *Securities and Exchange Commission v. Jones*.[59]

The conclusion of the Supreme Court in sustaining the registration provisions cannot therefore be criticized, although the requirements for registration and the penalties for non-registration are stringent and burdensome. The need for control of interstate utility holding companies to supplement the regulation of the operating utilities in the respective states is appreciated when the pyramided structure of the "super-holding company" is examined. The regulatory effect of publicity through registration, even without enforcement of the "death sentence" provision of section 11 and the other control provisions, certainly will be salutary and beneficial to the consumer and investor alike.

Gerald L. Stoetzer

---

[54] (D. C. N. Y. 1936) 15 F. Supp. 315 at 319, reversed on other grounds, (C. C. A. 2d, 1937) 87 F. (2d) 446.

[55] U. S. Constitution, art. 1, § 8: "The Congress shall have power . . . to establish post offices and post roads."

[56] 2 WILLOUGHBY, CONSTITUTIONAL LAW, 2d ed., § 598 (1929); 30 ILL. L. REV. 509 at 527 (1935).

[57] "Whatever the limits to its power, it may forbid any such acts done in furtherance of a scheme that it regards as contrary to public policy, whether it can forbid the scheme or not." Badders v. United States, 240 U. S. 391 at 393, 36 S. Ct. 367 (1916).

[58] 48 Stat. L. 74, § 5 (1933), 15 U. S. C. (1935), § 77e.

[59] (C. C. A. 2d, 1935) 79 F. (2d) 617, reversed on other grounds, Jones v. Securities Exchange Commission, 298 U. S. 1, 56 S. Ct. 654 (1936).