INTEGRATION UNDER SECTION 10(c) OF THE PUBLIC UTILITY HOLDING COMPANY ACT

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FROM its inception in 1935 to the present time the Public Utility Holding Company Act has been noted chiefly for its "death sentence" provisions. These provisions are found in section 11(b) of the act, and require (1) geographical integration and (2) corporate simplification of public utility holding companies.\(^1\) Section 11(b)(1) stipulates that it shall be the duty of the Securities and Exchange Commission, as soon as practicable after January 1, 1938, to require that each registered holding company and subsidiary thereof shall take action to limit the operations of the holding company system of which such company is a part to a single integrated public utility system,\(^2\) and to such other businesses as are reasonably incidental, or economically necessary or appropriate to the operations of such integrated public utility system. The commission may permit, as reasonably incidental or economically necessary or appropriate to the operations of one or more integrated public utility systems, the retention of an in-
terest in any business (other than the business of a public utility company as such) which the commission shall find necessary or appropriate in the public interest or for the protection of investors or consumers and not detrimental to the proper functioning of such system or systems. Furthermore, the S. E. C. is required to permit a holding company to control one or more integrated public utility systems in addition to the principal system referred to above if it finds that (A) each of such additional systems cannot be operated as an independent system without the loss of substantial economies which can be secured by the retention of control by the holding company of such system; (B) all of the additional systems are located in one state, or in adjoining states, or in a contiguous foreign country; and (C) the continued combination of such systems under the control of such holding company is not so large, considering the state of the art

3 The “other businesses” clauses of § 11(b)(1) have caused considerable difficulty. Briefly, they require substantially more than a showing that no positive harm will result from the retention of such businesses. The phrases “public interest” and “proper functioning” of an integrated system, when considered in their context, refer to the stated policy of the act to limit the activities of public utility systems to enterprises related to “economy of management and operation” of the public utility system, and the “integration and coordination of related operating properties.” Compatibility with that interest, even if that is all that need be shown, requires a showing that the public interest will be furthered by retention of a nonutility interest by reason of its relation “to economy of management and operation” of a public utility system or systems or “the integration and coordination of related operating properties.” The commission cannot make the affirmative statutory finding necessary to permit the retention unless the record contains such a showing. In the Matter of North American Co., S. E. C. Release No. 3405, pp. 25-27 (April 14, 1942).

The first “other businesses” clause refers to any activity other than that of an electric or a retail gas utility, the same as the second clause, and also to such latter activities if they are merely investments, i.e., if they do not come within the definition of statutory subsidiaries laid down in § 2(a)(8). In the Matter of United Gas Improvement Co., S. E. C. Release No. 2692 (April 15, 1941).

4 This has been interpreted to mean that the holding company must show that important economies, i.e., something substantially more than nominal economies, would be lost if its control of the additional system were severed. And the phrase “substantial economies” in clause (A) refers to economies which may be secured by the systems themselves rather than to economies which may be secured by the holding company. In the Matter of North American Co., S. E. C. Release No. 3405 (April 14, 1942).

5 The commission has decided that the plain meaning of this clause is unsatisfactory when compared with the purposes and history of the act. Consequently, it has construed the clause to lay down this requirement: in addition to the “single integrated public-utility system” otherwise permitted, a company may, if it meets the factual standards of clauses (A) and (C), keep additional systems located in one or more states adjoining the states in which such “single integrated public-utility system” is located. See Memorandum of January 8, 1941, from the Public Utilities Division to the Commission, In re Interpretation of Section 11(b)(1)(B).
and the area or region affected, as to impair the advantages of localized management, efficient operation, or the effectiveness of regulation.\(^6\)

It is apparent, then, that the provisions of section 11(b)(1) prescribe standards by which scattered utility systems are to be carved into geographically integrated organizations. These provisions are operative only after the evil has been done, only after vast empires have been completely constructed. Utility companies are continually changing the scope of their operations—buying new properties and selling old ones, building extensions, making improvements, etc. It would seem that here is a fertile field in which to apply the principles of geographical integration before purchases are made and before systems are set up which will be very difficult to tear down at a later date. The framers of the act did not overlook this point, and in section 10(c) we find that the requirements which are laid down in 11(b)(1) for existing systems are applied in moderated form to acquisitions by registered companies of securities or assets of a public utility company. Thus we have in addition to the remedial provisions of section 11(b)(1) the preventive provisions of section 10(c).\(^7\)

Section 10(c) has been invoked many times since 1935,\(^8\) and the developments under this section have foreshadowed the progress of integration under 11(b)(1). It is the purpose of this article to examine the nature of the requirements of section 10(c), and to indicate the extent of their effectiveness in accomplishing the integrational objectives of the act.

\(^6\) Clause (C) prevents retention of additional systems where such retention would result in control by the same interests of unrelated properties in widely separated areas. Similar requirements are laid down in § 2(a)(29).

Note that the ABC clauses are in the conjunctive; all three must be met for an additional system to be retainable.

\(^7\) It has been pointed out that the “regulatory purposes” of the act cannot properly be isolated from the “integration purposes” thereof, and that many of the so-called regulatory provisions are so keyed to the integration provisions that they must be regarded as largely incidental to and in aid of the statutory objectives of ultimate simplification and integration. For example, § 7(d)(1) is keyed to § 11(b)(2), and §§ 10(c)(1) and 10(c)(2) are keyed to § 11(b)(1). All of the underlying purposes of the act must be considered in each case. In the Matter of Virginia Electric & Power Co., S. E. C. Release No. 2791 (June 3, 1941).

\(^8\) Sec. 9(a) provides that unless the acquisition has been approved by the commission under § 10, it shall be unlawful for any registered holding company or any subsidiary thereof to use the mails or any instrumentality of interstate commerce to acquire any securities or utility assets or interest in any business. This section therefore requires companies and persons coming within the scope of the act to meet the financial, integrational, and other standards set up in § 10 before any acquisitions can be made. Sec. 10(c) imposes two of the most important standards of that section.
I

Comparison of Sections 10(c)(1) and 10(c)(2)

Section 10 sets up standards according to which the S. E. C. shall approve acquisitions of securities and utility assets and other interests by registered public utility holding and operating companies. Section 10(c) provides, in substance, that the commission shall not approve (1) an acquisition of securities or utility assets, or of any other interest, which is detrimental to the carrying out of the provisions of section 11, or (2) the acquisition of securities or utility assets of a public utility or holding company unless the commission finds that such acquisition will serve the public interest by tending towards the economical and efficient development of an integrated public utility system.9

The Public Utilities Division of the S. E. C. has urged the so-called "articulated interpretation" of these two clauses of section 10(c) upon the commission, and this interpretation has been followed to a considerable extent in the more recent cases.10 An explanation of this theory will be of value in demonstrating the differences between the two clauses, although it must be remembered that it has not been consistently and strictly followed by the commission, especially in the earlier decisions. Section 10(c)(1) forbids the approval of acquisitions detrimental to the carrying out of the provisions of section 11 (requiring integration and simplification), and 10(c)(2) requires the commission to find that acquisitions of securities or utility assets of a public utility will serve the public interest by tending towards the economical and efficient development of an integrated public utility system. Eliminating the question of simplification under section 11, the two clauses appear to have much the same import; the first seeks to prevent acquisitions detrimental to integration, while the second requires the acquisitions to tend towards integration. The latter seems

9 Sec. 10(c): "Notwithstanding the provisions of subsection (b), the Commission shall not approve— (1) an acquisition of securities or utility assets, or of any other interest, which is unlawful under the provisions of section 8 or is detrimental to the carrying out of the provisions of section 11 of this title; or (2) the acquisition of securities or utility assets of a public-utility or holding company unless the Commission finds that such acquisition will serve the public interest by tending towards the economical and efficient development of an integrated public-utility system. This paragraph shall not apply to the acquisition of securities or utility assets of a public-utility company operating exclusively outside the United States." 49 Stat. L. 819 (1935), 15 U. S. C. (1940), § 79j(c).

10 A detailed discussion of this interpretation will be found in pp. 17-27 of the brief of counsel to the Public Utilities Division of the S. E. C., In the Matter of Central U. S. Utilities Co., 8 S. E.C. 691 (1941).
to include the former. The "articulated interpretation" makes the two subdivisions serve separate and distinct functions, however. The interpretation of 10(c)(1) is that it refers directly to the requirements of section 11(b)(1) in the limitation of holding companies to one or more integrated public utility systems and "such other businesses," and that under it acquisitions should be tested as a whole with an eye toward possible or pending 11(b)(1) proceedings against the larger system involved. In other words, 10(c)(1) is to be used primarily as a device to promote the \textit{ultimate} objects of integration, and is not so much concerned with the immediate effect of the acquisition involved. On the other hand, 10(c)(2) is interpreted to refer not so much to the dictates of section 11(b)(1) as to the development of the \textit{property being transferred} into an integrated system or a part thereof. It is the immediate group of properties involved in the transfer that is important, and not all the groups in the system.\textsuperscript{11} Under this interpretation of section 10(c) there are two different tests that must be met, and an adverse finding as to either one will prevent approval of the transaction.

A large number of cases have been presented to the commission in which difficulty has arisen over the application of section 10(c), especially clause (2). One of the main difficulties is that 10(c)(2) merely stipulates that the acquisition shall tend towards the development of an integrated system, and does not specify which system it refers to. A literal interpretation would lead to the conclusion that if such a tendency could be found as to any one of the systems involved, a favorable decision should follow. Some of the decisions have emphasized to a minor degree the effect of a proposed acquisition upon the system of the vendor, while looking principally to the effect on the properties being combined.\textsuperscript{12} Further, a sizeable number of cases have applied 10(c)(2) both to the vendor and to the properties being combined (often including the entire system of the vendee) as if one was

\textsuperscript{11} The term "group," as used here, refers to one geographical subdivision of all the properties controlled by the top holding company. The latter are generally collectively called the "system" of the holding company. This terminology should be distinguished from the technical language used when § 11(b)(1) is being considered. There a single holding company may be allowed one integrated system and one or more additional integrated systems if certain tests are met; obviously, one top holding company may control several integrated systems. A "group" may well constitute an integrated "system," but it is used here instead of "system" in order to avoid confusion of the technical and nontechnical uses of the latter word.

\textsuperscript{12} In the Matter of Northern Indiana Public Service Co., S. E. C. Release No. 3145 (Nov. 25, 1941); In the Matter of Central U. S. Utilities Co., 8 S. E. C. 829 (1941); In the Matter of Central U. S. Utilities Co., 8 S. E. C. 469 (1941).
as important as the other. And finally, many S. E. C. opinions have considered principally the system of the vendor. The inconsistency of the decisions is evident.

In the Central U.S. Utilities Company case this problem concerning the proper application of section 10(c)(2) was squarely presented. The facts in that case showed that the intervenors proposed to acquire five scattered utility properties located in the southwest, belonging to Central U.S. Utilities Company, a subsidiary holding company in the Associated Gas & Electric Company system. These properties were to be combined into one company and operated as a group, but were not to be joined at the time of the acquisition with any other properties. The Associated system, of course, was far from meeting the integrational requirements of the act, and the sale of these five properties would enable it to eliminate outlying "peripheral" utilities, a definite step towards the integration of the system. On the other hand, it was not contended by the intervenors that the five properties, operating as a separate unit, would constitute an integrated system. It was argued that the commission should make the affirmative finding required by

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In the Columbia Gas & Electric Corporation case, for example, Panhandle Eastern Pipe Line Company proposed to acquire the stock and debt of Michigan Gas Transmission Company and of Indiana Gas Distribution Corporation from its parent, Columbia Gas & Electric Corporation; and it also proposed to purchase certain pipelines in Indiana and Ohio from Ohio Fuel Gas Company. The transactions were approved under §§ 10(c)(1) and 10 (c)(2) because (1) these properties together constituted an interrelated gas production, transmission, and distribution system, and (2) they were not related to the remainder of the Columbia system and this was a step toward the economical and efficient development of the system of the vendor, Columbia Gas & Electric Corporation.

14 In the Matter of Walnut Electric & Gas Corp., 7 S. E. C. 229 (1940); In the Matter of Sioux Falls Gas Co., 6 S. E. C. 1104 (1940); In the Matter of United Light & Power Co., 6 S. E. C. 670 (1940); In the Matter of Walnut Electric & Gas Corp., 6 S. E. C. 338 (1939); In the Matter of Commonwealth & Southern Corp., 5 S. E. C. 665 (1939); In the Matter of International Utilities Corp., 5 S. E. C. 309 (1939); In the Matter of Republic Electric Power Corp., 3 S. E. C. 992 (1938); In the Matter of States Electric & Gas Corp., 2 S. E. C. 392 (1937).


16 The Public Utilities Division would not concede this point (brief of counsel to the Public Utilities Division, p. 28), but it is clearly evident from the admitted facts.
IO(c)(2) because the proposed acquisition tended to effectuate the integration of the Associated system, without regard to whether the acquisition tended towards the integration of the southwestern properties, and cases clearly placing the emphasis of IO(c)(2) on the effect of the transaction upon the vendor system were cited. The Public Utilities Division advanced the articulated interpretation of section IO(c), by virtue of which it was contended that IO(c)(2) applied chiefly to the property being transferred. The interpretation was supported by two arguments, the meaning of the section when considered as a whole and the legislative history of the provision. The Public Utilities Division counsel admitted that this interpretation had not been strictly followed in all the cases, but cited the recent decision of In the Matter of Hudson River Power Corporation as the latest

17 In the Matter of Sioux Falls Gas Co., 6 S. E. C. 1104 (1940), and In the Matter of States Electric & Gas Corp., 2 S. E. C. 392 (1937).

In the Sioux Falls case Central U. S. Utilities Company, a holding company in the Associated Gas & Electric Company system, proposed to acquire the assets of Sioux, an operating gas utility and one of its direct subsidiaries, and then to sell these assets to Central Electric & Telephone Company, a nonaffiliated corporation. These transactions were approved, the commission stating that “Our [favorable] findings with respect to Section 10(c)(1) and 10(c)(2) are predicated upon the fact that the respective acquisitions are but steps in the disposition by the Associated system of an isolated property, which will tend to the economical and efficient development of such remaining portion of the Associated system as may be found to constitute an integrated public utility system.” 6 S. E. C. 1104 at 1110.

In the States Electric case International Utilities Corporation proposed to organize a new holding company (States Electric & Gas Corporation) to which several of its scattered properties were to be conveyed for the purpose of eventual, though not immediate, liquidation. It was admitted that the plan would not achieve any integration of the utility properties being conveyed to States nor in any other respect conform with the objectives of § 11(b)(1) at that time. The contention merely was that it provided the machinery which would make it easier to effect such dispositions and rearrangements of properties that might be necessary to comply with § 11(b)(1). The commission reached the conclusion that “Under all the circumstances of this case, including the essentially private character of the undertaking, and the fact that the transaction may be regarded as a reorganization, in compliance with the policy of Section 11, of the utility interests of the vendor companies, we find that the proposed acquisition of securities by States from the vendor companies and the proposed issuance of securities by States are consistent with the requirements of Sections 10 and 7.” 2 S. E. C. 392 at 399 (italics added).

These two cases were distinguished in the Central U. S. Utilities case on the ground that the records in each of these decisions showed that the acquiring company had indicated a definite plan for the future development of an integrated public utility system of which the property acquired would be a part, or proposed to take further action in order to comply with the integrational requirements of the act.

18 Brief of counsel to the Public Utilities Division, pp. 17ff.

19 8 S. E. C. 254 (1940). In this case International Hydro-Electric System proposed to consolidate two of its wholly owned subsidiaries, Hudson River Power Cor-
fully articulated interpretation of section 10(c). The commission there held that section 10(c)(2) requires the applicant to establish affirmatively that a proposed acquisition meets the standard of that clause, and proceeded to test the effect of the transaction on the two subsidiaries being combined, and also on the larger holding company system of which those properties were a part. The conclusion was that neither test was met. The most important innovation of this case was the alteration of the earlier conception that any remote step in the right direction satisfied the standard of 10(c)(2), and the substitution of the new idea that this standard requires substantial and tangible evidence of integration.20 This new approach is not concerned with the articulated interpretation of 10(c)(2), however. That interpretation deals with the separation of the functions of the two clauses of section 10(c) and specifies what groups of properties each is applicable to; the Hudson River case deals principally with the amount of evidence required under 10(c)(2) as to integration, and not with the problem of articulation raised by the Central U.S. Utilities Company case. It is true that particular attention was paid in the Hudson River case to the effect of the combination on the two subsidiaries being united, and secondarily to its effect on the larger utility system of which they were a part, all in accord with the articulated interpretation. But the difficulty of articulation which arises when the system of a third party vendor is also involved was not presented in this case, since the proposal was merely to consolidate properties which were part of the same system. Therefore the Hudson River case was not a precedent for the Central U.S. case, and the latter involved a wholly different situation.

The holding of the commission in the Central U.S. case closely followed the arguments of the Public Utilities Division. A few excerpts from the opinion will show the position taken by the commission.

It was pointed out by counsel for the Public Utilities Division that the commission has held the standard of § 10(c)(2) to be met when the following findings were made: (a) a saving to the company making the acquisition; (b) substantially reduced rates to consumers; (c) physical and geographical interconnection of underlying properties; (d) better position of these operating companies to serve the public; (e) part of transaction for refunding; (f) possibility of the use of idle funds; (g) aid in compliance with § 11(b)(1); or (h) steps in the disposition by the vending company of isolated property. These special situations will be discussed more fully later. With the exception of (c), these are examples of deviation from the stricter requirements advocated by counsel, and are merely “remote steps in the right direction.”
In substance, counsel [for applicants] argues that we must make the affirmative finding under Section 10(c)(2) if the proposed acquisition tends to effectuate the integration of the Associated system without regard to whether the acquisition tends towards the integration of the Southwestern properties. We think this construction of 10(c)(2) is unsound.

"In a recent discussion of Section 10(c)(2), we indicated our view that the consideration of the standard under that provision must be based primarily on an analysis of the property which is the subject of the acquisition. See Hudson River Power Corporation. . . .

"The legislative history furnishes additional support for this view that 10(c)(2) is directed primarily to the effect of the acquisition on the property being acquired and that the particular acquisition to be approved must tend towards the development [sic] of the economical and efficient development of an integrated public utility system. . . . The reports of the Senate and House Committees show that under Section 10(c)(2) primary concern is with the effect of the acquisition from the point of view of a single integrated public utility system in regard to economies in operation and management of the properties, and effectiveness of regulation. . . .

"We do not mean to imply that the effect of the transaction on the disposing company is not also a factor to be considered under Section 10(c)(2). We do hold, however, that the primary impact of 10(c)(2) is on the property being acquired and the acquiring company." 21

The caveat quoted in the last paragraph above is not in strict accord with the articulated interpretation of 10(c)(2), but was undoubtedly inserted as a device to reconcile past decisions and to provide freedom of action in the future. Under this decision the commission can either follow the theory of articulation or ignore it. The case would have been much more valuable as a guide to future applicants if the S. E. C. had committed itself completely to one position or the other. The articulated interpretation is a method of approach to the standards of section 10(c) entirely different from that originally pursued and requires new elements of proof. In all fairness to parties who desire to make acquisitions or disposals of utility properties, the commission should make it clear which approach is to be considered the correct one; as it is now, much loss of time and money may be incurred by appli-

cants who have promoted a transaction on one theory if the commission sees fit to adopt the other theory. The commission should not be in a position to jump from one interpretation to the other at will. The utility business can adapt itself to either one of the theories, but it will often be unable to adapt itself to both.

Since March 1, 1941, when the Central U. S. Utilities case was decided, where similar problems under 10(c)(2) have arisen the commission has been careful to use language which conforms with the holding in that case. As indicated in that opinion, however, the effect of a proposed acquisition on the vendor has been given some consideration, although the precise question which arose there has not been presented. The tendency of the commission seems to be toward the complete adoption of the articulated interpretation of 10(c)(2), and this tendency will undoubtedly become more pronounced as the proceedings under section 11(b)(1) reach a more advanced stage.

II

SECTION 10(c)(2)

We now turn to an examination of the affirmative standards of section 10(c)(2) which must be met by a party proposing to acquire utility assets or securities. The provisions of this section in substance require that such an acquisition shall tend towards the economical and efficient development of an integrated public utility system. Referring to section 2(a)(29) we find that an "integrated public-utility system," as applied to electric utility companies, is defined to be one in which the various properties "are physically interconnected or capable of physical interconnection and which under normal conditions may be economically operated as a single interconnected and coordinated"


24 The primary impact of this section being, as we have seen, upon the property being acquired and the acquiring company, and only secondarily upon the disposing company, In the Matter of Central U. S. Utilities Co., S. E. C. 691 (1941).

25 The term "coordinated" has not been referred to frequently in the cases involving § 10(c), and its meaning is not clear. A recent case under § 11(b)(1) held
system confined in its operations to a single area or region, in one or more states, not so large as to impair . . . the advantages of localized management, efficient operation, and the effectiveness of regulation; \textsuperscript{26} and as applied to gas utility companies, an “integrated public-utility system” means a system in which the gas utility companies “are so located and related that substantial economies may be effectuated by being operated as a single coordinated system confined in its operations to a single area or region, in one or more states, not so large as to impair . . . the advantages of localized management, efficient operation, and the effectiveness of regulation, [and] gas utility companies deriving natural gas from a common source of supply may be deemed to be included in a single area or region.” \textsuperscript{27}

It will be noted that there are four main requisites for an integrated electric utility system: (1) the units must be interconnected or capable of physical interconnection; (2) they must be capable of being economically operated as a single interconnected and coordinated system; (3) this system must be confined in its operations to a single area or region in one or more states; and (4) this system must not be so large as to impair the advantages of (a) localized management, (b) efficient operation, and (c) the effectiveness of regulation.

There are three standards in the final analysis which must be met by an integrated gas utility system, as follows: (1) the properties must be operated as a single coordinated system confined in its operations to a single area or region in one or more states, and gas utility companies deriving natural gas from a common source of supply may be deemed to be included in a single area or region; (2) such a system must be capable of effecting substantial economies; and (3) the system must not be so large as to impair the advantages of (a) localized management, (b) efficient operation, and (c) the effectiveness of regulation.

A. Acquisition of Electric Utility Assets under Section 10(c)(2)

To begin with, it must be pointed out that a proposed acquisition under section 10 does not have to meet all the standards of an inte-
grated system; it is enough if the acquisition "tends" toward the development of such a system. The following analysis is designed to show what factors, as enumerated above, or what combinations of factors are necessary to satisfy 10(c)(2).

1. Requirement of Physical Interconnection

The first requirement of an integrated electric utility system is physical interconnection of properties or possibility of such interconnection. No case has been found in which mere physical interconnection alone, without the presence of at least one of the other main factors, has been held to be a sufficient showing under 10(c)(2). However, interconnection or the possibility thereof between the acquirer and the property to be acquired is a very strong element in favor of a proposed transaction. Interconnection necessarily means that the properties involved are contiguous or adjacent to each other, usually confined to a single area, since the distance electric energy can be transmitted is physically limited, and these are additional favorable features.

The interconnection among the properties involved is not always complete, but the commission looks with much favor upon even partial interconnection. In addition, the fact that the properties to be acquired are capable of being connected with the lines of the acquiring party is a sufficient showing under the requirement of interconnection. It has been considered significant that the properties to be acquired were not capable of connection with any utility system other than that of the applicant. And a proposal for immediate, or even eventual, inter-

29 In the Matter of United Light & Power Co., S. E. C. Release No. 3285 (Dec. 31, 1941); In the Matter of Wisconsin Electric Power Co., S. E. C. Release No. 2950 (Aug. 19, 1941); In the Matter of Peoples Light Co., 4 S. E. C. 19 (1938). The advantages of interconnection are reflected in the Commission's Public Utility Holding Company Act Rule 41(a), 6 Fed. Reg. 2021 (1941), which exempts certain limited acquisitions of utility assets made by electric utility companies in registered holding company systems from the provisions of § 9(a)(1) (requiring approval of acquisitions by such companies under § 10), when the "electric utility assets to be acquired are, prior to the acquisition, or will be immediately thereafter, connected with electric utility assets already owned and operated by the acquiring company, excluding connections over lines not operated by the acquiring company."
31 In the Matter of Utility Service Co., 1 S. E. C. 966 (1936).
33 In Matter of Texas Utilities Co., 1 S. E. C. 944 (1936), the applicant, which was engaged in the power business in west Texas, proposed to acquire additional electric
connection after the acquisition in question is accomplished is enough to bring the blessings of physical interconnection to the transaction involved.\(^4\)

On the other hand, in the first case refusing approval of a proposed acquisition of electric utility assets under section 10(c)(2), the absence of physical interconnection among the properties was the determining factor of the decision.\(^{35}\) In this case International Hydro-Electric System proposed to consolidate two of its subsidiaries, Hudson River Power Corporation and System Properties, Inc. With respect to the properties of Hudson River, the record showed that the only interconnection between its three principal developed properties (all located within a small area) was over the transmission lines of a nonaffiliated utility company. The assets of System Properties were not interconnected among themselves, nor were they connected with those of Hudson River. The commission pointed out that the proposed acquisition, in and of itself, would not produce any physical interconnection of these utility assets, and, assuming that such interconnection might be practicable (a fact not supported by the record) the consolidation would not cause these assets to be any more capable of interconnection after the acquisition; and further, the record disclosed no definite plan for bringing about any such interconnection. It was concluded that since the acquisition would not produce any physical interconnection, there could be no efficiency change and hence no operating economies. The result was that the transaction had to be disapproved because Hudson River and International Hydro-Electric failed to show that the proposed acquisition would serve the public interest by tending towards the economical and efficient development of an integrated public utility system. Apparently, therefore, the absence of physical interconnection or the possibility thereof is a very strong objection to approval under 10(c)(2).\(^{36}\)

utility properties, located in eastern New Mexico. In finding that the requirements of § 10(c)(2) were met since, among other things, the properties involved were already physically interconnected and operated as a single system with those of the applicant and were in other respects within the definition of an integrated public utility system, as defined in § 2(a)(29)(A), the commission relied upon the fact that these utility assets were located at a considerable distance from the facilities of companies other than the applicant, and that interconnection with any other company did not appear to be consistent with an economic or efficient development of an integrated system.

\(^4\) In the Matter of Iowa Public Service Co., 6 S. E. C. 435 (1939); In the Matter of Cumberland County Power & Light Co., 2 S. E. C. 989 (1937).

\(^{35}\) In the Matter of Hudson River Power Corp., 8 S. E. C. 254 (1940).

\(^{36}\) Further evidence of governmental belief in the merits of interconnection is found in § 824a(a) of the Federal Water Power Act, enacted as Title II of the Public
2. Requirement of Economical Operation as a Single System

Next, the units in the system must be capable of being economically operated as a single interconnected and coordinated system. The emphasis here is on the economy of operation, and again it may be said that an acquisition which results only in such economy probably cannot be approved under section 10(c)(2), but it is a material factor in securing approval of the acquisition. This is demonstrated more emphatically where approval under 10(c)(2) is denied. An acquisition of bonds, part of a refunding program, which will result in a materially lower interest rate produces desirable economies under this subsection. And an acquisition producing tax economies is also looked upon with favor by the commission. The possible ways in which a public utility may effect economies are legion, and the examples given here are only suggestive of the methods in which the requirement of economical operation can be met.

Along the same lines, the S. E. C. has looked with favor upon transactions under section 10(c)(2) which tend to put the utility in question in a better financial or operating position. For example, the improvement of capital structure by capitalization of earned surplus, or by conversion of debt held by the parent into common stock of the subsidiary warrants an affirmative finding under 10(c)(2). The same

Utility Act of 1935. 49 Stat. L. 848 (1935), 16 U. S. C. (H)40, § 824a(a). The Federal Power Commission is empowered and directed to divide the country into regional districts for the voluntary interconnection and coordination of facilities for the generation, transmission, and sale of electric energy. Since the proposed interconnection and coordination of facilities is voluntary, the Federal Power Commission does not have the means for enforcing integration on a large-scale plan throughout the United States.

It would seem that a nation-wide plan for interconnection and integration would promote efficiency, economy, etc., much more than the piecemeal programs of integration which are now being pursued. The government probably realizes, however, that large-scale integration would be so difficult and revolutionary that its accomplishment would be practically impossible of attainment. Is not this an indication of the economic fallacy of integration under present conditions?

In the Matter of Public Service Co., of New Hampshire, 1 S. E. C. 505 (1936).

In the Matter of Hudson River Power Corp., 8 S. E. C. 254 (1940). The commission brought out the fact that the acquisition would not produce any physical interconnection which might bring about an efficiency change, and that therefore no operating economies were possible. It also appeared that the acquisition in and of itself would bring about no reduction in general administrative expenses.


In the Matter of General Public Utilities, 4 S. E. C. 308 (1938) (capitalization of surplus); In the Matter of Dayton Power & Light Co., 3 S. E. C. 1098 (1938)
ruling is frequently found in reorganization cases which involve acquisitions that must meet the standards of 10(c)(2). If the proposed transaction tends to facilitate reorganization of the parent company, those standards are met.\textsuperscript{42} Again, they are met if the acquisitions substitute a solvent company with a more appropriate capital structure for an insolvent company with an unbalanced capital set-up,\textsuperscript{48} or if the proposed reorganization will readjust the company's obligations so as to place it in a better position to render services as a public utility.\textsuperscript{44} The commission has put the proposition in these words:

"... The financing and construction operations, to which the proposed acquisitions are incidental, will place the operating companies in a better position than at present to render services as public utility companies. The Commission therefore finds that such acquisitions will serve the public interest by tending toward the economical and efficient development of an integrated public utility system."

3. Requirement of Operations in a Single Area

The third requirement for an integrated electric utility system is that the system must be confined to a single area or region in one or more states. This standard of limited geographical size is closely related to the requirement of interconnection; an interconnected system must of necessity be restricted to a rather small area due to the technical impossibility of transmitting electric energy over long distances. Several phases of this problem have been discussed under (1) above.

It will be noticed that the "single area or region" may be located in one or more states. Our first premise consequently is that the location of an integrated system need not conform to state boundaries nor need it be located entirely within one state. This does not mean that the


\textsuperscript{44} In the Matter of Middle West Corp., 1 S. E. C. 514 (1936).

\textsuperscript{48} In the Matter of Community Power & Light Co., 4 S. E. C. 951 at 962-963 (1939). This and like decisions are discussed by Commissioners Mathews and Healy in their concurring opinion in Matter of Consumers Power Co., 6 S. E. C. 444 at 488 (1939). They consider these decisions economically sound and worthy of being followed as precedents.
commission will not look with favor upon a proposed acquisition where the properties involved are all located in the same state. Quite the contrary is true. A number of cases have noted with evident satisfaction that both the properties of the acquiring system and the properties to be acquired were situated within one state, and the smaller the state the better.\textsuperscript{46} Interconnection, contiguous location, localized management, efficient operation, and effective regulation are usually concomitant features of such systems. In other cases, in which the major part of the properties involved were located in one state, although some operations were carried on in adjoining states, approval of the proposed acquisitions has been greatly facilitated by the intrastate nature of the utility businesses conducted by the applicants.\textsuperscript{47} The commission has never refused to approve a transaction under 10(c) where these conditions were present.

Our first premise does not carry us far, however. Most of the modern utility systems are sprawled over two or more states, and the limits of the "single area or region" have not yet been established. How far may they be extended?

Acquisitions of utility stock or assets have been permitted under section 10(c)(2) when the properties to be acquired and the systems immediately involved, all interconnected or capable of physical interconnection, were located in the following areas: extreme eastern New Mexico and west Texas;\textsuperscript{48} southeast Texas and Louisiana;\textsuperscript{49} eastern Missouri and western Illinois;\textsuperscript{50} eastern Iowa and western Illinois;\textsuperscript{51} eastern Wisconsin and the northern peninsula of Michigan;\textsuperscript{52} northwestern Pennsylvania and New York;\textsuperscript{53} and California, Nevada, and

\textsuperscript{46} In the Matter of Cumberland County Power & Light Co., 2 S. E. C. 989 (1937) (Maine); In the Matter of Massachusetts Utilities Associates, 2 S. E. C. 98 (1937) (Massachusetts); In the Matter of Utility Service Co., 1 S. E. C. 966 (1936) (Ohio).

\textsuperscript{47} In the Matter of Commonwealth Edison Co., 2 S. E. C. 709 (1937) (Illinois); In the Matter of Public Service Co. of New Hampshire, 1 S. E. C. 762 (1936) (New Hampshire); In the Matter of Public Service Co. of New Hampshire, 1 S. E. C. 505 (1936) (New Hampshire).

\textsuperscript{48} In the Matter of El Paso Electric Co., 8 S. E. C. 366 (1940); In the Matter of Texas Utilities Co., 1 S. E. C. 944 (1936).

\textsuperscript{49} In the Matter of Engineers Public Service Co., 3 S. E. C. 580 (1938).

\textsuperscript{50} In the Matter of Union Electric Co. of Missouri, 2 S. E. C. 421 (1937).


\textsuperscript{53} In the Matter of NY PA NJ Utilities Co., 3 S. E. C. 553 (1938).
Arizona. In each of these cases the commission indicated that the properties involved were to be considered confined to a single area or region, within the meaning of the act.

However, restriction of operations to a single area or region is not an absolute criterion under section 10(c). Acquisitions may be approved on other grounds, and often are. In this respect section 10(c)(2) has only a limited function in fixing the extent of a "single area or region." Many acquisitions have been approved when even the immediate systems concerned were spread over a considerable number of states. In these cases, however, it is clearly recognized that the properties are not confined to a single locality, and approval has been forthcoming for other reasons.

The adverse decisions under section 10(c)(2) are somewhat more illuminating. In the Central U. S. Utilities Company case, where the properties were located in Arkansas, Louisiana, Oklahoma, Texas, and Arizona, with interconnection between them impossible, the S. E. C. noted that they were a thousand miles apart from one end to the other and pointed out that even the applicants did not contend that they constituted an integrated public utility system. In the Hudson River Power Corporation case, International Hydro-Electric System proposed to consolidate two of its wholly owned subsidiaries, Hudson River Power Corporation and System Properties, Inc., as we have already seen. The principal power plants of Hudson River were located in New York within fifteen miles of each other, but they were not interconnected except over the transmission lines of a nonaffiliated company, a subsidiary of another utility system. The developed plants of System Properties were located within one hundred miles of those belonging to Hudson River. The utility assets of System Properties were not interconnected with those of Hudson River, and the proposed consolidation would not have produced any physical interconnections. The consolidation was disapproved under 10(c)(2) both as to the properties immediately involved and also as to the larger operating system of International Hydro-Electric. The commission did not deny that the principal assets of the two subsidiaries were located within a single area

54 In the Matter of Nevada-California Electric Corp., 1 S. E. C. 553 (1936); In the Matter of Nevada-California Electric Corp., 1 S. E. C. 459 (1936).
55 See discussion of the special situations in which acquisitions have been permitted, infra, p. 28 ff.
57 In the Matter of Hudson River Power Corp., 8 S. E. C. 254 (1940), discussed supra at note 19.
or region; the question merely was not discussed. The controlling consideration was the lack of interconnection between the properties. We are thus led to the conclusion that in a close case this third requirement of integration will be subordinated to that of the first, physical interconnection.\textsuperscript{58}

The economic propriety of limiting the size of utility systems is also doubtful. It has been shown that the larger the company the lower its cost, the greater the economy, and the greater the efficiency; and size as such is not detrimental to the public interest, whether size relates to company operations or holding company systems.\textsuperscript{59} However, the commission has not been ardent in enforcing this requirement in the 10(c) cases, and the most that can be said is that it serves in a supplementary capacity to the other standards of integration.

4. Requirement of Size Consistent with Local Management, Efficient Operation and Effective Regulation

Finally, the system must not be so large as to impair the advantages of (a) localized management, (b) efficient operation, and (c) the effectiveness of regulation. Each of these three items needs to be discussed separately, although they are interrelated to a large extent.

Government economists in 1935 were deeply concerned over the distance intervening between the general management headquarters of public utilities and the operating properties, and their views on absentee management are reflected in the above provisions of the act.\textsuperscript{60} The S. E. C. has compiled elaborate maps and charts showing how the various holding company systems fail to meet the requirement of “localized management.”\textsuperscript{61} The statistics given by the commission re-

\textsuperscript{58} But cf. In the Matter of Eastern Shore Public Service Co., 6 S. E. C. 776 (1940).
\textsuperscript{59} Waterman, Economic Implications of Public Utility Holding Company Operations 64-109 (1941) (Michigan Business Studies, Vol. 9, No. 5).
\textsuperscript{60} “An operating system whose management is confined in its interest, its energies, and its profits to the needs, the problems, and the service of one regional community is likely to serve that community better, to confine itself to the operating business, to be amenable to local regulation, to be attuned and responsible to the fair demands of the public, and, more often, to get along with the public to mutual advantage. . . . Essentially local systems will tend to operate utilities rather than to play with high finance; and essentially local enterprise is far less likely to accumulate a disproportionate amount of political and economic power.” S. Rep. 621, 74th Cong., 1st sess. (1935), p. 12, quoted in In the Matter of North American Company, S. E. C. Release No. 3405, p. 44 (April 14, 1942).
\textsuperscript{61} S. E. C. Public Utilities Division, Report, Charts Showing Location of Operating Electric and/or Gas Subsidiaries of Registered Public Utility Holding Companies (1939).
reveal a number of interesting facts. Six holding companies have subsidiaries at a distance of 3000 miles or more from their management headquarters.\(^{62}\) The average distance between headquarters and all subsidiaries of five systems is equal to 2000 miles or more.\(^{63}\) The average maximum distance for the 54 systems included in the report was 1343 miles, and the overall average distance was 816 miles. Thirty-one of these systems have operating companies located 1000 miles or more away from general headquarters. The businesses of 92 per cent of all the operating companies covered by the report are run from only four metropolitan areas, New York City-Newark-Jersey City, Chicago, Philadelphia, and Boston-Cambridge.

These figures are interesting, but what do they reveal? They certainly show that the management of public utilities is not localized near the operating properties. This alone, however, is no condemnation of the utility systems. The question remains, does this state of affairs affect the proper and efficient functioning of such systems? The author of a recent study of the economic aspects of the question has this to say:

"Mere distance of operating companies from the main office of their respective holding companies in and of itself does not tend to be related in any way to the character and quality of the protection accorded to the investors in the securities of such operating company. Nor does this variable show any connection with any of the objectives of the Holding Company Act. Subsidiary company customers are not charged significantly different average electric bills depending upon where they live in relation to the situs of management and control; in relation to their geographical location, perhaps, but that factor is an independent variable over which no utility management has control. The costs of management seem completely disassociated from the distance from management element as do the protections afforded to investors.\(^{64}\)"

In the 10(c) cases the S. E. C. has seldom stressed the localization of management. A few decisions have noted with approval that the transactions involved would lead to more localized management.\(^{65}\)


\(^{64}\) Waterman, Economic Implications of Public Utility Holding Company Operations 126 (1941).

\(^{65}\) In the Matter of Massachusetts Utilities Associates, 2 S. E. C. 98 (1937); In the Matter of Fall River Electric Light Co., 1 S. E. C. 465 (1936).
Others have looked with favor upon consolidation of contiguous properties where the result would be common management of all the plants concerned. None of the decisions under section 10(c)(2) adverse to the applicants have made an issue of the lack of localized management. The conclusion to be drawn is that this element is relatively unimportant in the application of 10(c)(2).

The system must not be so large as to impair the advantages of efficient operation. Precisely what is meant by the term "efficient operation" is not specified; apparently it is within the discretion of the commission to say when operation is efficient and when it is not. The commission has held that the acquisition by a subsidiary of a short power line that connects it with another subsidiary in the same system, the effect being to reduce some of the costs of operation, tends toward the efficient operation of the system as a whole and is proper under 10(c)(2). In a different type of case, the issuance and sale of bonds to finance the construction of additional generating facilities for a subsidiary was held not objectionable since the efficient operation of the system required the proposed additions. One of the adverse decisions under 10(c)(2) stresses the fact that the proposed acquisition would not produce any physical interconnection, and therefore there could be no efficiency change and hence no operating economies.

This element of "efficient operation," though seemingly of more importance than that of "localized management," suffers greatly from the obscurity of its meaning. "Efficiency" may refer to transmission of electricity with little loss of power; it may refer to efficient operation of the generating facilities; it may refer to efficient technical management; it may refer to efficient general management; or it may refer to all of these. The act does not specify which, and the commission has not clarified the situation to any extent. Consequently, this provision has little value as a standard for integration.

66 In the Matter of Wisconsin Electric Power Co., S. E. C. Release No. 2950 (Aug. 19, 1941); In the Matter of Utility Service Co., 1 S. E. C. 966 (1936). There may also be several divisions of management, e. g., a main administrative office in New York and an office for local management near the operating properties. So far as appears, the commission has never recognized such a distinction, and if the holding company has a central office in a large city that is the one and only management center the commission takes into consideration, despite the fact that there is a large degree of direction of operations by officials with offices close to the utility properties. It cannot be denied that the holding companies have been guilty of much abuse by way of long distance management, but a blanket condemnation of all systems with no regard for the actual management set-up of each should be avoided.

67 In the Matter of Fall River Electric Light Co., 1 S. E. C. 465 (1936).
69 In the Matter of Hudson River Power Corp., 8 S. E. C. 254 (1940).
Finally, the system must not be so large as to impair the advantages of effective regulation. The "regulation" involved means that of state public utility commissions or the equivalent thereof. Size, of course, supposedly makes no difference as to the effectiveness of federal regulation, which extends everywhere. One great concern of Congress in 1935 was to restore to local regulatory bodies the power that they lost by virtue of the vast interstate expansion of utility companies, and the cases under the act have shown that the commission will look with favor upon a system confined to a single area or region or to a single state, because companies of such limited size may be effectively regulated.10

In an economic study of public utility holding company operations, already cited,71 this problem of the effectiveness of regulation is analyzed at length. The author, Mr. Waterman, in his conclusion indicates that there has been a substantial change in the effectiveness of the regulation of operating subsidiaries of holding companies in the last decade. This means that the powers of state commissions have been considerably increased in recent years, and that many of the weaknesses of these bodies, which existed before the act was passed and which were important factors in causing federal regulation, have now been eliminated. Mr. Waterman then goes on to say,

"... Based on study and observation, it is the considered opinion of the writer that at the present time there is no evidence of any more lack of reasonable cooperation with state regulatory authorities on the part of holding companies and holding company subsidiaries than there is on the part of independent utilities; nor is there any evidence that the effectiveness of state regulation is impeded in any important manner by the existence of holding companies. The indications are that state regulation of holding company subsidiaries is at the present time as efficient and effective as state regulation of independent utilities, and there is no logical reason why state regulation of the one need be less effective or efficient than of the other. . .

"Looking at the overall picture of public regulation of utilities, that is, both state and federal regulation, it is quite clear that at the present time the activities of the operating subsidiaries of holding companies are more comprehensively and effectively regulated than the corresponding activities of independent utilities."72

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10 In the Matter of Massachusetts Utilities Associates, 2 S. E. C. 98 (1937); In the Matter of Fall River Electric Light Co., 1 S. E. C. 465 (1936).
71 WATERMAN, Economic Implications of Public Utility Holding Company Operations (1941).
72 Id. 136-137.
The net result is that effective regulation of holding company subsidiaries is no longer a major problem, and consequently there is little likelihood that any acquisition will be denied under section 10(c)(2) on the ground that it impairs the effectiveness of regulation.

B. Acquisition of Gas Utility Assets under Section 10(c)(2)

The definition of an integrated gas utility system under section 2(a)(29)(B) is much the same as the definition of an integrated electric utility system under section 2(a)(29)(A), and in many respects they are identical. The only substantial difference between the two subsections is that an electric system must be physically interconnected or capable of physical interconnection in order to be integrated, while a gas system need only be operated as "a single coordinated system confined in its operations to a single area or region," and gas utility companies deriving natural gas from a common source of supply may be deemed to be included in a single area or region. This distinction is based upon the physical differences between gas and electricity and the methods of conveying or transmitting them. In most instances where several artificial gas plants and distributing systems are located within a limited area, interconnection of the pipe lines would be very expensive and would serve no useful purpose, since storage tanks are generally available to meet peak loads. On the other hand, where several electric power plants are situated close to each other interconnection is not as expensive and serves a very useful purpose in that interchange of energy is frequently necessary. The peak load problem is much more acute in the power business than in the gas industry.

The special provision for natural gas systems should also be noted. A "gas utility company" is defined to be any company which owns or operates facilities used for the distribution at retail of natural or manufactured gas for heat, light, or power. The usual holding company arrangement includes a separate company or companies for the production of natural gas and for its conveyance to consumption centers. These companies sell their gas at wholesale to the local distributor, another member of the holding company system. Since there are no retail sales of the gas until it has arrived in the general locality where it will be used, the producing and pipe line companies are not utilities within the definition of the act and do not have to meet the standards of integration. In addition, section 2(a)(29)(B) gives further protection to long-range natural gas utilities by providing that such companies de-

73 Public Utility Holding Company Act, § 2(a)(4).
riving natural gas from a common source of supply may be deemed to be included in a single area or region.

We shall now proceed with our analysis of acquisitions of gas utility assets and securities under section 10(c)(2), applying the standards of section 2(a)(29)(B). It should be remembered that the analysis under 2(a)(29)(A) is also applicable here to a large extent.

I. Requirement of Coordinated System in Single Area

The properties within a gas utility system must be operated as a single coordinated system confined in its operations to a single area or region in one or more states, with the proviso that gas utility companies deriving natural gas from a common source of supply may be deemed to be included in a single area or region. The basic requirement here is not interconnection, for the reasons given above, but the presence of interconnection is a favorable factor. The acid test is location within a limited territory. Where the properties operate in only one section of a state, approval will generally be given. Further, a combi-

74 Acquisitions of interconnected gas utility properties, both those distributing artificial and those distributing natural gas, are met with ready approval by the S. E. C. In the Matter of Massachusetts Utilities Associates, 5 S. E. C. 88 (1939); In the Matter of Hoosier Gas Corp., 4 S. E. C. 904 (1939); In the Matter of Southern Natural Gas Co., 2 S. E. C. 354 (1937). Even partial connection is a favorable factor. In the Matter of Lone Star Gas Corp., 2 S. E. C. 911 (1937). Although the properties to be acquired are not interconnected with each other or with the acquiring system, the fact that they are easily capable of connection may be adequate grounds for approval. In the Matter of Arkansas Western Gas Co., 8 S. E. C. 286 (1940); In the Matter of Peoples Natural Gas Co., 6 S. E. C. 166 (1939). These grounds are even stronger if the acquiring company expresses its intention to build connecting lines immediately after the acquisition is consummated. In the Matter of Northern Indiana Public Service Co., S. E. C. Release No. 3145 (Nov. 25, 1941); In the Matter of Central States Edison, 7 S. E. C. 268 (1940); In the Matter of Lone Star Gas Corp., 2 S. E. C. 911 (1937). The commission has frequently referred to the effect of a proposed transaction under § 10(c)(2) on the disposing system, and looks with approval upon the disposition of gas utilities not interconnected with the system of the vendor. In the Matter of Great Lakes Utilities Co., S. E. C. Release No. 3207 (Dec. 22, 1941); In the Matter of Central U. S. Utilities Co., 8 S. E. C. 829 (1941); In the Matter of Central U. S. Utilities Co., 8 S. E. C. 469 (1941); In the Matter of Walnut Electric & Gas Corp., 7 S. E. C. 229 (1940); In the Matter of Walnut Electric & Gas Corp., 6 S. E. C. 338 (1939).

75 In the Matter of Northern Indiana Public Service Co., S. E. C. Release No. 3145 (Nov. 25, 1941) (northwest Indiana); In the Matter of Wisconsin Electric Power Co., S. E. C. Release No. 2950 (Aug. 19, 1941) (eastern Wisconsin); In the Matter of Houston Natural Gas Corp., 7 S. E. C. 323 (1940) (southeast Texas); In the Matter of Central States Edison, 7 S. E. C. 268 (1940) (southeast Kansas); In the Matter of Iowa Public Service Co., 6 S. E. C. 435 (1939) (northern Iowa); In the Matter of Hoosier Gas Corp., 4 S. E. C. 904 (1939) (southwest Indiana); In the
nation of scattered and noninterconnected gas properties within the confines of a small state has been permitted. A gas utility system operating in more than one state may also be considered confined to a single area or region. The usual situation is where the properties operate on both sides of the boundary line between two states and do not extend far beyond that line, although proximity to the boundary line is not an absolute requisite. And an interconnected natural gas production, transmission, and distribution system extending from Texas through Oklahoma, Kansas, Missouri, Illinois, Indiana, Michigan, and Ohio has been held to be a functional unit and an interrelated system.

We now turn to the proviso that gas utility companies deriving natural gas from a common source of supply may be deemed to be included in a single area or region. It must be noted that the language of the statute is permissive; such companies may be deemed to be located in a single area. Apparently the commission is not bound in all cases to make such a finding. The degree to which the permissive character of the provision diminishes the force of the protection afforded widespread natural gas utilities depends, of course, upon how the S. E. C. chooses to exercise its discretion in the matter. The cases decided so far shed little light on this question. It is reasonable to believe, however, that the commission will honor the obvious Congressional purpose of protecting far-flung natural gas utilities with a common source of supply, and will refuse to apply the proviso in a proper case only where...
such action is plainly necessary to effectuate the objectives of the act.

Another problem raised by this provision relates to the definition of "a common source of supply." The commission has held that several contiguous fields may constitute a common source of supply. One decision has indicated that a system which taps noncontiguous gas fields in Texas and Kansas and distributes the gas in Indiana, Ohio, and Michigan is to be deemed to derive its gas from a common source of supply. Furthermore, the system need not be connected with the gas field or fields by transmission lines owned by the system, and it is sufficient if the system, comprised only of local distribution facilities, purchases all of its gas from the same pipe line company. And finally, where the various properties in the system purchase gas from different pipe line companies, which secure gas from a common locality but are not affiliated with each other or with the system, the system may be considered to have a common source of supply. From these decisions it can be seen that the commission has adopted a liberal attitude as to what constitutes a common source of supply, and the natural gas companies have been given all the protection in this respect that could be expected. This protection, of course, is not extended to artificial gas utilities, but the distinction in the treatment of the two kinds of gas utilities is well justified by the physical differences between these types of properties.

2. Requirement of Substantial Economies

Section 2(a)(29)(B) requires that an integrated gas utility system shall be so located and interrelated that substantial economies may be effectuated thereby. The decisions often refer with approval to economies of operation or reductions in expenses which will result from

80 The Monroe field in Louisiana is a good example of a common source of supply. Gas from the various wells in that field is carried by pipe lines through Louisiana, Mississippi, Alabama, Georgia, and Tennessee, in which states the gas is distributed to consumers. See In the Matter of Southern Natural Gas Co., 8 S. E. C. 432 (1941); In the Matter of United Light & Power Co., 6 S. E. C. 670 (1940); and In the Matter of Southern Natural Gas Co., 3 S. E. C. 264 (1938).

81 In the Matter of Central Power Co., 8 S. E. C. 425 (1941). The natural gas utilities in this case, located in Nebraska, sold gas piped in from the Otis field and contiguous fields in Kansas.


84 Id.

85 The corresponding requirement for electric systems is worded differently (the units must be capable of being "economically operated"), but the two requirements are substantially the same.
proposed acquisitions. Particular economies which have been noted are those resulting from local control of the operating units, rather than long-distance control; also managerial economies and reduction of legal and administrative expenses. Economies which lead to a reduction of rates to consumers are certain to produce a favorable reaction.

Approval has been more readily forthcoming where the proposed transaction results in the parent company's having a more simplified capital structure, a more uniform spread of debt maturity and carrying charges, and a more favorable ratio of debt to plant and property accounts, or where the current asset position of the parent will be improved. In other words, where the transactions will materially improve the economic position of the companies involved and will enable them to serve the public better, they are looked upon with approval by the S. E. C.

On the whole, however, it seems that the requirement of substantial economies or economical operation takes a definitely subordinate position to the requirement of operations in a single area or region, the same relation we found to exist in the electric utility decisions with reference to the standards of economical operations and interconnection. Attention is chiefly directed to the geographical elements, and this is consistent with the theory of integration, which is that all the benefits of economical and efficient operation, effective regulation, lower rates, sounder financial conditions, etc., will naturally and inevitably flow from the concentration of utility systems within limited areas.

3. Requirement of Size Consistent with Local Management, Efficient Operation and Effective Regulation

Finally, to be integrated a gas utility system must not be so large as to impair the advantages of (a) localized management, (b) efficient operation, and (c) the effectiveness of regulation. The discussion of

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88 In the Matter of American Light & Traction Co., 3 S. E. C. 969 (1938).
90 In the Matter of Lone Star Gas Corp., 3 S. E. C. 787 (1938).
91 In the Matter of Southern Natural Gas Co., 8 S. E. C. 432 (1941).
92 In the Matter of Laclede Gas Light Co., S. E. C. Release No. 3376 (Mar. 6, 1942); In the Matter of St. Louis County Gas Co., 7 S. E. C. 286 (1949).
these identical requirements for electric utility systems applies with
equal force at this point. And the remarks just made, to the effect
that the requirement that the system be operated in a single area or
region predominated over the second standard, likewise apply to this
third set of standards. If a system is located within narrow confines it
is assumed that localized management, efficient operation, and effective
regulation will automatically result, and specific findings on these
points are not necessary. On the other hand, if the system is not con­
fined to a single area or region, the presence of one or more of these
three elements will be of considerable assistance in securing approval
of an acquisition under 10(c)(2). Let us examine a few of the cases.

A subsidiary of the Associated Gas & Electric Company system,
Central U. S. Utilities Company, made application in two cases to sell
parts of its nonintegrated Indiana gas properties to local interests.98
Both applications were granted, one of the grounds for approval in
each being the substitution of localized management for the distant
control exercised by Central U. S. Utilities Company. Similarly, the
disposition by Great Lakes Utilities Company of two isolated gas
properties in Iowa to another utility system operating principally in
Iowa and adjoining states, Sioux City Gas & Electric Company, was
approved under section 10(c)(2), one of the principal reasons being
that these two properties were near the main offices of the acquiring
system, where experienced operating organizations were maintained.94

The gas utility cases under 10(c)(2) do not throw any additional
light on the meaning of “efficient operation.” The tendency of a pro­
posed acquisition towards efficient operation is a favorable feature,95
but the cases have never said specifically what constitutes nonefficient
operation. Perhaps this is due to the fact that the operations of no two
systems are alike, and what constitutes efficiency in one would not in
another. A more realistic explanation, however, is that the commission
is far more concerned with the first requirement of integration, geo­
graphical condensation, from which is supposed to flow the benefits of
efficient operation, effective regulation, etc., than with the other factors.

Effective regulation is the last element required by section 2(a)
(29)(B). The increasing effectiveness of the control exercised by state
public utility commissions, as a result of enlarged jurisdiction and

98 In the Matter of Central U. S. Utilities Co., 8 S. E. C. 829 (1941); In the
22, 1941).
95 In the Matter of Lone Star Gas Corp., 2 S. E. C. 911 (1937).
powers given such commissions, has offset the importance of this re­
quirement of the act to a considerable extent. And further, it has been 
subordinated along with the other elements to the requirement of 
operations in “a single area or region.”

III
SPECIAL SITUATIONS ARISING UNDER SECTION 10(c)

The S. E. C. early recognized that the problem of bringing about 
complete integration under the act was “an evolutionary rather than a 
revolutionary process,” and that as a practical matter it would often 
be necessary to accomplish the ultimate objectives of the act by a series 
of steps rather than by one direct and final step. One of the first 
public statements made by the commission’s general counsel was to the 
effect that any acquisition which made for the economical development 
of the property acquired as an efficient and self-sustaining operating unit 
or system might be regarded as tending towards the economical and 
efficient development of an integrated utility system, and that it was not 
essential that the property acquired be interconnected or capable of 
terconnection with some other property under the control of the com­
pany making the acquisition. Piecemeal progress towards integration 
is all that is required under section 10(c). However, in a 1939 case

96 In the Matter of Community Power & Light Co., 6 S. E. C. 182 (1939); 
In the Matter of Peoples Light & Power Co., 2 S. E. C. 829 at 836 (1937). The 
latter case was concerned with a reorganization of Peoples Light & Power Corporation 
and its seven scattered subsidiaries. The commission held that “Consummation of the 
plan will effect a substantial reduction in debt, substitute a solvent holding company 
for an insolvent one, and while not resulting in a simple capital structure will at least 
bring about more simplicity than now exists. Thus the acquisition will have the tendency 
required by clause (c)(2) of Section 10. It must be observed, however, that it is 
nothing more than a tendency. The system is obviously not an integrated one and the 
proposed capital structure is far from ideal. No contention has been or could be made 
that following the consummation of this plan the system will measure up to the re­
quirements of Section II. The tendency, however, required by clause (c)(2) of 
Section 10 is present, and such being the case the applications under Section 10 can be 
and are approved. ... Preservation of the system for the time being may facilitate 
eventual integration on terms which may at least protect security holders from the 
sacrifice which anything resembling forced selling at this stage might involve. ... If 
consummation of the plan be viewed as merely one step to be followed toward com­
plete compliance with the Act, at least some of the objections which can be made to the 
plan lose a good deal of force.” 2 S. E. C. 829 at 835, 836.


98 In the Matter of American Utilities Service Corp., 7 S. E. C. 789 (1940); 
In the Matter of Consumers Power Co., 6 S. E. C. 444 (1939). Since 1940, § 
11(b)(1) proceedings have been instituted against the major systems of the country, or
arising under section 11(b)(2), Chairman Frank in a dissenting opinion denounced certain aspects of the policy of making haste slowly. And the more recent decisions, especially those denying applications on the ground of noncompliance with section 10(c), indicate that this "evolutionary process" is being accelerated, and that more substantial steps towards integration will be required in the future than in the past.

This corresponds to the tendency which now exists as a result of the adoption of the articulated interpretation of section 10(c). In spite of this clamping down on the requirements of the act, special problems have arisen in the past and will continue to arise in the future which could not and cannot be treated mechanically, as a strict interpretation of the act would necessitate. Many proposed transactions falling under section 10(c) have not had any immediate tendency towards the development of integrated systems and in some respects may have been detrimental to the carrying out of the provisions of section 11, but the commission has found various grounds upon which to base a favorable decision if the transaction in question appeared to be reasonably necessary to the proper functioning of the applicant's system. A discussion of some of these nonstatutory grounds for approval created by the commission will indicate how far that body will go in this respect.

Preliminary steps towards integration, such as the disposition of the systems have filed plans for integration under § 11(e), or both, and therefore in most cases which arise under § 10(c) it is unnecessary to attempt the overall integration which will be taken care of in the § 11(b)(1) and 11(e) proceedings. In the Matter of Louisville Gas & Electric Co., S. E. C. Release No. 3300 (Jan. 30, 1942); In the Matter of Wisconsin Electric Power Co., S. E. C. Release No. 2950 (Aug. 19, 1941); In the Matter of Philadelphia Company, S. E. C. Release No. 2816 (June 11, 1941); In the Matter of El Paso Electric Co., 8 S. E. C. 366 (1940). Or if proceedings under § 11 are not pending, the commission reserves jurisdiction under that section. The cases are legion; see, for example, In the Matter of Pacific Power & Light Co., S. E. C. Release No. 3505 (May 2, 1942); In the Matter of Ohio Public Service Co., S. E. C. Release No. 3428 (April 3, 1942); In the Matter of Maine Seaboard Paper Co., S. E. C. Release No. 3294 (Jan. 26, 1942).

99 In the Matter of North American Co., 4 S. E. C. 434 (1939). This case involved the approval of a plan of simplification submitted under § 11(e), under which plan certain preferred stock was to be issued with several protective provisions inserted as safeguards to investors. In protesting against the issuance of the preferred stock, Chairman Frank referred to the contention of the majority that the safeguards provided for the preferred shareholders were an improvement and that Rome was not built in a day and that half a loaf was better than none, and proceeded to point out that a more relevant image than the loaf of bread was that of a bridge. "As some wag has remarked, it is not true that half a bridge is better than none." This was, of course, a special case, but it is indicative of the changing attitude of the commission toward the rate of progress which must be made in the direction of compliance with § 11.

100 In the Matter of Central U. S. Utilities Co., 8 S. E. C. 691 (1941); In the Matter of Hudson River Power Corp., 8 S. E. C. 254 (1940).
isolated properties or the combination of interconnected companies, even though very minor in character, have been approved under \(10(c)\).\(^{101}\) These cases present little difficulty under the terms of the act. Some trouble has arisen where a highly nonintegrated company proposes to convey miscellaneous properties to a trustee or to a corporation for the purpose of liquidating such properties over a period of time. Obviously, no immediate integration is accomplished, nor are the objectives of section \(11(b)(i)\) achieved in any other respect. However, proposals such as this have met with approval as being steps in the direction of ultimate compliance with the act.\(^{102}\) The acquisition of nonintegrated or nonutility assets by a parent company from a subsidiary has been permitted where the purpose of the transaction was merely to facilitate the sale of these properties to an outsider.\(^{103}\)

A number of acquisitions have been approved on the ground that the acquirer would soon cease to be subject to the jurisdiction of the S. E. C. For instance, where the acquirer proposed to become solely an operating company, or where the properties sold would not be controlled by a registered holding company the commission raised no objections.\(^{104}\) The same is true where the holding company applicant

\(^{101}\) In the Matter of Sioux Falls Gas Co., 6 S. E. C. 1104 (1940); In the Matter of Iowa Public Service Co., 6 S. E. C. 435 (1939); In the Matter of Republic Electric Power Corp., 3 S. E. C. 992 (1938); In the Matter of Massachusetts Utilities Associates, 2 S. E. C. 98 (1937).

\(^{102}\) In the Matter of International Utilities Corp., 5 S. E. C. 309 (1939) (liquidating trustee); In the Matter of States Electric & Gas Corp., 2 S. E. C. 392 (1937) (liquidating corporation).


\(^{104}\) Acquirer to become solely an operating company: In the Matter of Houston Natural Gas Corp., 7 S. E. C. 323 (1940); In the Matter of States Electric & Gas Corp., 2 S. E. C. 392 (1937); In the Matter of Nevada-California Power Co., 1 S. E. C. 773 (1936).

Properties sold not to be controlled by a registered holding company: In the Matter of Walnut Electric & Gas Corp., 7 S. E. C. 229 (1940); In the Matter of Sioux Falls Gas Co., 6 S. E. C. 1104 (1940); In the Matter of Walnut Electric & Gas Corp., 6 S. E. C. 338 (1939).

Operating gas and electric utilities which are not associated or affiliated with any holding companies do not come within the scope of the act and are not subject to the integrational requirements thereof. However, a large number of states require utilities operating in such states to be incorporated therein. This situation, of course, necessitates holding companies to control properties scattered over several states. The vicious circle is then completed because the act covers all utility holding companies and subsidiaries. The point is that an independent operating company doing business in several states is practically nonexistent.
proposed to dispose of its statutory electric or gas utilities and to operate utilities in the future which were not covered by the act, such as water properties, telephone systems, and the like.\textsuperscript{105} This ground of approval was, however, rejected in the \textit{Central U. S. Utilities Company} case.\textsuperscript{106} It was there argued by the applicants that the proposed plan called for the ultimate transfer of scattered properties to an operating company outside the jurisdiction of the S. E. C. The commission construed this as a request to put "its blessing upon scatteration—in connection with a transaction which the Commission could not approve if the properties were to remain subject to our jurisdiction—because the scatteration will ultimately be the problem of a company outside our jurisdiction." The holding of the commission was completely contrary to the decisions reached in the cases mentioned above, as this further quotation from the case will show:

\begin{quote}
"We conceive it to be our duty under the Act to exercise our jurisdiction over the transactions which come before us to effectuate the expressed policies of the statute. We think it would be directly contrary to these policies to permit scatteration \textit{merely} because that scatteration may ultimately be the problem of a public utility company beyond our jurisdiction. An analysis of the Act and a study of our function under Section 11 in the light of the preamble to the Act—particularly Sections 1(b)(5) and 1(c)—make it clear that integration and the elimination of scatteration is not an end in itself but rather that it is required under the Act in order to eliminate various abuses and evils which are inherent in scatteration. ... In effect, the argument amounts to the suggestion that Congress contemplated the elimination of certain abuses and evils in the holding company system by the creation of abuses and evils outside the holding company system."\textsuperscript{107}
\end{quote}

Although this case was more difficult than any which preceded it, there was a complete reversal of form on the part of the commission. This ruling has not been extended to cases where the acquirer is principally a nonutility holding company and proposes to dispose of its electric and gas subsidiaries in the near future,\textsuperscript{108} but apparently where the

\textsuperscript{105} In the Matter of American Utilities Service Corp., S. E. C. Release No. 2706 (April 18, 1941); In the Matter of Northeastern Water & Electric Corp., 8 S. E. C. 64 (1940); In the Matter of Northeastern Water & Electric Corp., 3 S. E. C. 823 (1938).

\textsuperscript{106} In the Matter of Central U. S. Utilities Co., 8 S. E. C. 691 (1941).

\textsuperscript{107} Id. at p. 702.

applicant is to become an operating utility company the S. E. C. will closely scrutinize the transaction, even though those utilities will soon pass beyond its jurisdiction. This is another indication of the tightening of the requirements of the act.

Quite frequently the parent company in a system desires to acquire more of the stock of its subsidiaries. Such acquisitions have consistently been approved on the grounds that if the subsidiary is retainable under the act the increased working control of the parent will make for better articulation of the system, or if the subsidiary will have to be disposed of under the requirements of the act, eliminating some of the diverse owners will make divorcement more practicable of attainment. In other words, the acquisition of outstanding minority interests makes it easier for the parent company to comply with the requirements of section 11.

Construction and expansion programs, involving the development and improvement of presently owned properties, are generally approved under section 10(c). The theory is that they will place the operating companies in a better position to render service as public utility companies, thereby serving the public interest by tending towards the economical and efficient development of an integrated utility system. And proposals for the construction of additional facilities needed for the war effort will undoubtedly be consistently approved.

The purchase of additional properties by a nonintegrated system has been approved on the ground that increasing the size and scope of operations of properties already owned would increase the salability of those properties and facilitate a sale thereof in the future, although the acquisition did not tend towards the immediate integration of the system or was in fact a step in the opposite direction.

110 In the Matter of Southern Natural Gas Co., 8 S. E. C. 432 (1941); In the Matter of Columbia Gas & Electric Corp., 7 S. E. C. 801 (1940); In the Matter of Consumers Power Co., 6 S. E. C. 444 (1939); In the Matter of Community Power & Light Co., 4 S. E. C. 264 (1938).
112 In the Matter of Pennsylvania Gas & Electric Corp., S. E. C. Release No. 2726 (April 28, 1941); In the Matter of Southern Union Gas Co., 8 S. E. C. 801 (1941); In the Matter of California Public Service Co., 8 S. E. C. 302 (1940); In the Matter of National Gas & Electric Corp., 8 S. E. C. 197 (1940); In the Matter
commission believes that transforming scattered utilities into complete operating units, or increasing the financial strength of such properties, makes them more attractive to potential buyers and thus makes divestment under section 11 more feasible. Furthermore, acquisitions resulting from programs of reorganization, recapitalization, refunding, or revision of security structures have been approved for the reason that any disposition of subsidiaries which might be required under the act would be facilitated thereby, or because the properties would be more marketable. These grounds for approval are clearly not included in the act, but are merely additional examples of how far the commission will go to meet special situations. In all of these cases the proposed transactions were essential to the proper management of the systems involved, yet they did not meet the requirements of the act if strictly construed. The elastic application of the act by the commission in such situations is commendable.

Another nonstatutory factor that the commission has considered when passing upon proposed acquisitions is the size of the property to be acquired. It is clear that a large purchase should be examined more closely than a small one under section 10(c). Generally speaking, more difficulty will arise in the future over the disposition of large and expansive units in the various systems than will occur where smaller and more compact units must be eliminated. As we have seen in the foregoing paragraph, however, this statement must be qualified by pointing out that certain properties may be too small to sell. Even so, the loss resulting from having to give away or abandon a small unit may not compare with the greater loss of having to sell a large unit at a sacrifice under an 11(b)(1) order. Doubtful

of Central States Edison, 7 S. E. C. 268 (1940); In the Matter of Lexington Utilities Co., 2 S. E. C. 968 (1937). In the California Public Service Company case a nonintegrated subsidiary of a nonintegrated holding company system proposed to acquire the water and electric properties of a nearby but not interconnected company. The parent company had been pursuing a program of integration and stated that it wanted to dispose of the subsidiary involved here, but had been unable to do so on account of its small size. It was contended that the acquisition of the new properties would make this subsidiary large enough to be attractive to a purchaser, due to the fact that these assets would increase the subsidiary's account approximately 25% and would move it into the "charmed circle" of a million dollar company. These transactions were approved by the commission for this reason.


114 See also, In the Matter of States Electric & Gas Corp., 2 S. E. C. 392 (1937).
acquisitions which have been permitted because they were considered "small" include items all the way from six-tenths of a mile of power line\textsuperscript{116} to several complete utility properties.\textsuperscript{116} It should be added that "smallness" of the properties to be acquired is determined on a comparative basis, the relation of the size of those properties to the size of the acquiring system being the important consideration.

A number of special situations have arisen where public utility systems have desired to acquire nonutility properties. These fall into the category of "other businesses" in section 11(b)(1), and are retainable only when they meet the strict requirements laid down in that section. Nonutility businesses to be retained must be "reasonably incidental, or economically necessary or appropriate to the operations" of the principal system, or the commission may permit the retention of such businesses if they are found to be "necessary or appropriate in the public interest or for the protection of investors or consumers and not detrimental to the proper functioning" of the main system or the additional system or systems retainable under the ABC clauses. It is plain that the framers of the act intended to restrict the ownership of nonutility properties to a minimum, the principle being that in so far as possible a utility company should engage in utility operations, and no others.\textsuperscript{117} The greatest stumbling block encountered was the fact that the existing utility systems had not been built up on that basis, and the rights of investors and consumers now have to be considered in reducing these nonutility activities to the desired minimum. The

\textsuperscript{116} In the Matter of Fall River Electric Light Co., 1 S. E. C. 465 (1936).
\textsuperscript{117} In the Matter of Great Lakes Utilities Co., S. E. C. Release No. 3207 (Dec. 22, 1941); In the Matter of National Gas & Electric Corp., 8 S. E. C. 197 (1940). See also, In the Matter of Trustees of Associated Gas & Electric Corp., S. E. C. Release No. 3353 (Mar. 3, 1942) (electric utility properties); In the Matter of West Coast Power Co., 7 S. E. C. 350 (1940) (electric utility assets); In the Matter of Consumers Power Co., 4 S. E. C. 228 (1938) (electric utility assets); In the Matter of Central States Edison, 7 S. E. C. 268 (1940) (natural gas utility assets); In the Matter of Arkansas Western Gas Co., 8 S. E. C. 286 (1940) (utility assets of a gas and water company).
\textsuperscript{117} "... In general, the pattern of the statute and the context of the relevant statutory provisions seem to indicate that the 'other business' tests [of $11(b)(1)$] are not to be applied to operations grossly out of proportion to the utility business with respect to which they are claimed to be 'reasonably incidental, or economically necessary or appropriate.' In the ordinary case, therefore, we believe that the statute contemplates that after compliance with Section 11(b)(1) the integrated utility systems retainable by a registered holding company will constitute its, primary business and that retainable non-utility interests will occupy a clearly subordinate position." In the Matter of North American Co., S. E. C. Release No. 3405, p. 44 (April 14, 1942).
commission has been extremely liberal in permitting acquisitions of nonutility properties to date, as an examination of a few cases will indicate. Nonutility businesses which are reasonably incidental, or economically necessary or appropriate to the operations of the electric system to which they belong include coal mining and the sale of steam, previously used to produce power, for heating purposes. And a wholesale natural gas production and transmission system may be considered reasonably incidental to a natural gas system. However, acquisitions of many wholly unrelated properties have been permitted. These have been justified for many of the special reasons that have been discussed in the preceding few pages, e.g., because of the smallness of the properties in relation to the rest of the system.


119 In the Matter of Engineers Public Service Co., 3 S. E. C. 580 (1938).


121 Water properties: In the Matter of Northern Indiana Public Service Co., S. E. C. Release No. 3145 (Nov. 25, 1941); In the Matter of California Public Service Co., 8 S. E. C. 302 (1940) (the system involved in this case was already engaged in gas, electricity, water, ice, farming, and sewage businesses); In the Matter of Arkansas Western Gas Co., 8 S. E. C. 286 (1940); In the Matter of Northeastern Water & Electric Corp., 8 S. E. C. 64 (1940); In the Matter of Central U. S. Utilities Co., 7 S. E. C. 445 (1940); In the Matter of International Utilities Corp., 5 S. E. C. 765 (1939); In the Matter of Commonwealth & Southern Corp., 5 S. E. C. 665 (1939); In the Matter of Republic Electric Power Corp., 3 S. E. C. 992 (1938); In the Matter of Northeastern Water & Electric Corp., 3 S. E. C. 823 (1938); In the Matter of Engineers Public Service Co., 3 S. E. C. 580 (1938).

122 Telephone companies or assets: In the Matter of Commonwealth & Southern Corp., 5 S. E. C. 665 (1939); In the Matter of Engineers Public Service Co., 3 S. E. C. 580 (1938); In the Matter of Lexington Utilities Co., 2 S. E. C. 968 (1937); In the Matter of Public Service Co. of New Hampshire, 2 S. E. C. 890 (1937).


124 Tenement houses, machinery, and equipment: In the Matter of Public Service Co. of New Hampshire, 1 S. E. C. 762 (1936).


or because the proposed transactions would render such properties more marketable. From this rough survey it is evident that the commission has not restricted the acquisition of nonutility properties to the absolute minimum contemplated by the act. It is well that it has not done so in the formative stages, although, as the commission recognizes, a day of reckoning under section 11(b)(1) will come.

Conclusion

Principal attention in this article has been paid to the requirements of 10(c)(2), the more difficult of the two clauses of section 10(c), and these standards have been studied in the light of section 2(a)(29), which defines an integrated public utility system. Both electric and gas utility systems were analyzed. In regard to electric utility systems it was demonstrated that physical interconnection of properties is the most important integrational factor, while the requirement of economical operation, although of considerable consequence, takes a secondary position. The other elements, those requiring operation in a single area or region, localized management, efficient operation, and effective regulation, are definitely subordinate to the standards of interconnection and economical operation. With respect to gas utility systems, a similar situation was shown to prevail. The requirement that the properties be operated in a single area or region, which corresponds to the requirement of interconnection for electric utilities, is considered of paramount importance, and the other standards calling for substantial economies, localized management, efficient operation, and effective regulation are subordinate to the geographical factor. If geographical integration alone will cure all the evils existing in the utility business, as the government economists believed in 1935, then this emphasis on interconnection of electric properties or limitation of gas properties to a single area or region is justified. The truth of the major premise has not been established beyond question, however, and it would seem advisable to make a more balanced application of the act. The tendency at the present time is in this direction.

A number of special situations arising under section 10(c) in which the commission has enunciated grounds for approval not found within the four corners of the act have been discussed at length. The bene-

ficial effect of these cases in more freely permitting necessary activities of the utility businesses cannot be denied. The situations which arise daily in these industries are too varied and complicated to be treated in a mechanical way under a strict interpretation of 10(c). It must be noted, however, that the “evolutionary process” theory in regard to integration originally adopted by the commission is being speeded up to some extent, and will be increasingly accelerated as time progresses.

The provisions of section 11(b)(1) did not become effective until January 1, 1938, and in fact no attempt was made to enforce them until early in 1940. The commission recognized that bringing about ultimate integration was a vast and complicated problem, and that its work would have to be done slowly and carefully. Ever since 1935, however, the dealings of public utility holding companies have raised integrational questions that could not be postponed as could the larger problems under 11(b)(1). Many intrasystem, intersystem, and other transactions have been proposed that alter the geographical arrangement of the companies involved. The solution to these problems is found in section 10(c), as we have seen. Prior to the accomplishment of overall integration, partial integration of many systems has been achieved under this section of the act. As a result of the frequent application of 10(c), it has become an important factor in the formulation of basic integrational policies. It is true that the S. E. C. has not strictly enforced the requirements of this section in all cases, but the adoption in 1940 of the “articulated interpretation” indicates an increasing tendency in the direction of rigid adherence to the standards of 10(c). The developments under section 10(c) consistently and logically foreshadow the steps taken under 11(b)(1). As the time for the consummation of the objectives of section 11(b)(1) approaches, the commission becomes more and more careful in approving new acquisitions and rearrangements of properties within the various systems. Recent hearings in 11(b)(1) proceedings, as evidenced by the order in the North American case, indicate that the outline of geographical integration laid down by Congress is now about to be extensively filled in by the S. E. C. The geographical tangle which confronted the commission in 1935 has been straightened out in small sections by the 10(c) cases, and the insight which the commission has gained through these cases into the underlying difficulties of the situation will undoubtedly be of great benefit to that body with respect to the larger problems which it must face at this time.