

Conclusion

THE story is told that during the height of the customer ownership campaigns in the twenties, when the savings of many small uneducated investors were being channeled into the treasuries of the giant public utility companies, a Czechoslovakian employee of the Electric Bond & Share Company system sold the stock of that company in the Pennsylvania coal fields and assured his customers: “. . . With this stock push the button, and if the light shines, you know your money is safe.” Ironically enough, before, during, and after the depression of the early thirties, people went right on pushing the button and the light never ceased to shine, but a large proportion of these investments vanished into oblivion. Insull’s “fairyland of light and power” prospered and expanded, while the savings of many of the investors in his and other holding company securities were lost beyond recall. The Public Utility Holding Company Act of 1935 was designed to preserve the good in this situation and to eradicate the evil. How well has it succeeded with this purpose?

Numerous Congressmen, Senators, and witnesses testifying before the committee considering the holding company bill predicted that the industry would be wrecked, disintegrated, and annihilated by the provisions of this bill, and that appalling losses would be suffered by investors. The integration provisions of the bill were labeled a death sentence for the whole American philosophy of government and economics and an invitation to communism. And the attacks were continued by holding company executives and others long after the bill became law. The Securities and Exchange Commission began its long and laborious task in a cautious fashion, en-

deavoring to feel its way ahead slowly, rather than to muddy the waters with impetuous action. A few of its early decisions, such as that of American Water Works & Electric Company, were ill-conceived in the light of later rulings, but the mistakes were inconsequential and, in any event, they favored the utilities.

As the captains and the kings of the supermanagement days of the twenties departed, as the tumult, the shouting and the recriminations accompanying the enactment of this legislation faded away in the distance, the realization slowly descended upon the industry that the Act was constitutional, that the Commission was determined to accomplish its assigned mission, and that the divestments and rearrangements required by the Act were not as disastrous as originally advertised. In fact, they have not been disastrous at all. It is no doubt true that the Commission has squeezed a lot of water out of the holding company sponge, but the water was placed there largely in the twenties, and its expulsion should not be deemed a loss chargeable to the Act. The loss was already there in 1935; it had merely not been realized by actual sales. But dispositions of properties have generally been accomplished with no losses to investors. Just before the divestment plan of UGI was filed in 1942, its common stock sold at \$4 per share. This stock rose to \$6 after the plan was filed and to \$9.88 before the securities were distributed. Similar market reactions occurred in the case of The Commonwealth & Southern Corporation, Engineers Public Service Company, and other integration programs.⁵⁰⁷ The record of the past ten years has proved that the apprehension that the Act would cripple the market for utility securities was unfounded. The Commission has not required non-retainable properties to be dumped on the market at sacrifice prices. In fact the Com-

⁵⁰⁷ Statistics in this connection are set forth in the 17th Annual Report of the Securities & Exchange Commission, Fiscal year ended June 30, 1951, page 70.

mission claims that the favorable market reception of the portfolio utility stocks that have been sold was an important factor in strengthening the market for utility securities, particularly common stocks. Compliance with the Act has been achieved by other methods also, such as exchanges of securities or properties, the issuance to shareholders of subscription warrants to purchase portfolio securities, or the distribution of portfolio stocks as dividends.

It is generally true that the electric and gas utility industry, from the standpoint of both operating and holding companies, is in a very healthy condition today. Security values have risen, while rates have decreased. This prosperity may well be attributable to the heavy demand for electric and gas services during World War II and the following years of high business activity. Of course, the "dollar" prosperity of the industry must be appraised in the light of the devaluation of the dollar and the insidious inflation of the Roosevelt and Truman administrations, but the large increases in kwh's for the electric business and in mcf's for natural gas operations are testimonials of the well-being of these branches of the utility business. How much credit for this state of affairs can be given to the Act and to the Commission, and how much should be given to extraneous factors such as those just mentioned? The answer is difficult, if not impossible, to find. There is no way to measure the total effect of each factor. It should be borne in mind that the utility holding company is not an evil, *per se*. It is merely a corporate device with certain features which may be advantageous in some situations and disadvantageous in others, often depending upon whether the viewpoint is that of company officials, investors, consumers, regulatory officials, or the public. Its features which were condemned by Congress were directly attributable to the operators of the device. A utility holding company does not necessarily have to own amusement parks or baseball clubs

or other miscellany in addition to its utility properties; there is no inherent requirement that it extend its operations over many states and foreign countries; and it is not obliged to resist all attempts at regulation by the states in which it does business. The men in charge were responsible for such conditions. It is perhaps unfortunate that persons such as Insull, Foshay, and Hopson were directing the destinies of the large utility empires at the time of the 1929 crash. However, history contains ample proof of the fact that the characteristics of human nature exemplified by these men are continuously being repeated. Consequently, if there had been no Insull, Foshay, or Hopson, there would probably have been others as bad or worse. And their mistakes, if not curbed, would have been repeated and multiplied as their successors grew in power. The revelations of the great depression might have educated some executives to the evils inherent in the type of corporate insanity prevailing during the twenties. Howard C. Hopson is a shining example of the ineffectiveness of such education. The true measure of the beneficial effects of the Act, therefore, is the extent to which it has induced holding company managements to follow sound economic policies in the administration of their businesses. Reasonable minds will differ, of course, upon the proper definition of sound economic policies. Opponents of the Act were firm in their conviction that management policies were sound before the passage of the Act. An unbiased examination of such policies, however, would reveal many practices in the days before the Act which were undesirable, at least from the standpoint of investors, consumers, and the public with whom Congress was concerned. The Act and its administration by the Commission have imposed a number of substantial obstacles to the cupidity of those in control of utility holding companies. Thus it may be said that the remedy has been directed toward the actual seat of the trouble and that it has

no doubt contributed in a substantial measure to the present corporate health of the revamped utility holding companies.

Turning now to a more detailed analysis of the interpretation by the Commission and the courts of the specific provisions of the Act relating to integration, it is evident that the requirements pertaining to the single or principal integrated system have been rather liberally construed. The southwestern system of The Middle West Corporation, now known as the system of Central & South West Corporation, which served an area of 175,500 square miles in four states with transmission lines running 1,200 miles from one end of the system to the other, was held to be an integrated electric utility system. And the officially approved integrated electric service area of American Gas & Electric Company covers seven states and employs gross book assets of over \$750,000,000, thus making it the largest of the continuing holding companies from the point of financial size. Since interconnection or capability thereof is the prime requisite for the integration of an electrical system, the technological advances in this field have made possible far larger integrated systems than those contemplated by the sponsors of the Act. This development has probably been beneficial in view of the great demand for power experienced by the country during the last decade, but it is somewhat destructive of the requirements of the Act as to limited size and localized management. And economical and coordinated operation is usually a concomitant of extensive interconnections so that compliance with the requirement for such operation has not been difficult for the large systems.

The localized nature of manufactured gas operations has prevented the continuance of any large systems in this field. In addition, this business has not been as attractive from a financial standpoint to the holding companies, and the latter have usually divested or agreed to divest their gas proper-

ties rather than their electric systems. Further, the advent of long distance natural gas pipe lines, particularly since the end of World War II, has outmoded the artificial gas business in many large areas. The special provision of the Act with regard to natural gas utilities has been liberally construed in favor of the companies. For example, in the case of American Light & Traction Company, now American Natural Gas Company, it was held that a natural gas system would be integrated even though it derived only 67% of its supply from a common source. The three principal systems of the Columbia Gas & Electric Corporation, now The Columbia Gas System, Inc., were held to be separately integrated, although the Commission could easily have held them to be one system, but all three were held to be retainable since they complied with the tests for principal and additional systems. It can be generally stated that the single system provisions of the Act have been much easier to apply to gas utilities than to electric utilities, and therefore litigation with respect to the former has been considerably less than in the case of the latter.

The Commission has been much stricter in its application of the ABC clauses relating to the retention of additional systems. Particularly in the case of Clause A, the Commission has imposed rigid requirements for compliance. It has interpreted the term "loss of substantial economies" to mean the loss of important economies to the integrated system involved, not to the holding company or to the other businesses concerned. These constitute reasonable requirements. In addition, the Commission requires proof of the loss of substantial economies by "clear and convincing evidence." The possibility of increased expenses arising out of separation has been given little weight, and all company estimates of additional expenses and losses of economies have been discounted substantially upon the ground that intangible benefits would be derived by the various properties after separation. This

theory of intangible benefits upon separation has been applied by the Commission with particular force to proposed combinations of electric and gas utility systems. The Commission is probably justified to a large extent in taking this position, but it imposes a tremendous burden of proof on the holding companies and could well have been modified on occasions where abuse of the gas systems in favor of the electric systems was shown to be absent.

The ambiguity inherent in Clause B of the Act led to a prompt study of the matter by the Commission, which adopted the "one-area" theory as opposed to the "two-area" interpretation urged by the utilities. By virtue of this action, the Commission was able to dispose of many problems merely by reference to a map without the necessity of extended hearings. This ruling was the death knell for the principle of scattation so well exemplified by most of the large systems.

Geographical requirements for the retention of additional integrated systems are also imposed by Clause C, in that the "area or region" affected must be considered. The test here is relative rather than fixed, as in Clause B, and it is concerned with economic as well as geographical size. The advantages of localized management have often been stressed by the Commission, more so than the other provisions of Clause C. However, the more recent decisions involving Clause C evidence a rather liberal interpretation of its provisions and the identical provisions in Section 2(a)(29) of the Act.

Textual ambiguities also plagued the Commission with respect to the other businesses clauses. It adopted as the guiding principle the rather narrow test of the first other businesses clause requiring functional and operational relationship between each miscellaneous business and the utility system which sought to retain the other business. The legislative history was not as clear in this case as it was with reference to Clause B, and the Commission would have been

amply justified in giving independent effect to the second other businesses clause, rather than making it dependent upon and largely subordinate to the operational restriction of the first clause. The economies in operation insisted upon by the Commission under the first other businesses clause are economies in the operation of the integrated utility system and not the other business. Further, the Commission has required that each other business should be minor in importance and size compared to the principal utility business. These tests have been difficult, but not impossible, of attainment and the retention of a large variety of other businesses has been permitted by the Commission.

In spite of the controversial nature of the position taken by the Commission on numerous issues, its decisions relating to Section 11(b)(1) which were litigated in the courts have all been affirmed, with the exception of the other businesses issue in the Engineers Public Service Company case. The commission took the position that the latter case was overruled, in effect, by the Supreme Court in The North American Company case. This was quite possibly an unfounded conclusion on the part of the Commission, but no party has had the temerity to institute another test case, and the matter will undoubtedly remain in the status quo. The judicial approval of the Commission's work with respect to integration constitutes substantial proof of a job well done.

The magnitude of the task being performed by the Commission is indicated by the fact that approximately \$16 billion of utility and nonutility properties have already been divested from various holding company systems in conformance with the requirements of Section 11, and the number of companies subject to regulation under the Act has been reduced from 2,175 to 444, leaving 40 systems with assets of \$13 billion.⁵⁰⁸ The Commission estimates that at the con-

⁵⁰⁸ *Id.* at 63-65.

clusion of the Section 11 program approximately 20 integrated holding company systems with assets aggregating \$7 billion will remain subject to regulation.⁵⁰⁹ It thus appears that the Commission has a substantial assignment remaining ahead of it. However, the guideposts have been established in most instances and the problem is not so much how to integrate but how to dispose of non-integrated properties. The Commission has been patient in this regard, and its patience has been well rewarded.

Future integration problems will be concerned with new acquisitions by existing systems, which must meet the requirements of Section 10(c) of the Act.⁵¹⁰ The comprehensive set of standards which has been examined above should make this task relatively simple. The work of the Commission in this respect will be most effective if it takes advantage of the lesson of the past that its watchful eye should be focused not so much upon the utility systems themselves, but upon the personalities in command of those systems.

And finally, the Commission is now in a position to undertake the studies contemplated by Section 30 of the Act to ascertain the attributes of the most economical and efficient gas and electric utility systems for the nation as a whole.⁵¹¹

⁵⁰⁹ *Id.* at 66.

⁵¹⁰ Section 10 (c) of the Act provides that "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; 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. . . ."

⁵¹¹ Section 30 provides that "The Commission is authorized and directed to make studies and investigations of public-utility companies, the territories served or which can be served by public-utility companies, and the manner in which the same are or can be served, to determine the sizes, types, and locations of public-utility companies which do or can operate most economically and efficiently in the public interest, in the interest of investors and consumers, and in furtherance of a wider and more economical use of gas and electric energy; upon the basis of such investigations and studies the Commission shall make public from time to time its recommendations as to the type and size of geographically and

In view of the absence of articulate and widespread criticism of electric and gas utility operations at this time, it is extremely doubtful that any legislation of consequence in this field will be enacted in the near future or that such legislation is advisable.

economically integrated public-utility systems which, having regard for the nature and character of the locality served, can best promote and harmonize the interests of the public, the investor, and the consumer. . . ." The Commission has recently announced that action pursuant to Section 30 is now in order. Unnumbered release of the Commission dated July 17, 1952.