

Introductory Remarks  
of

RALPH H. DEMMLER  
Chairman

at Public Hearing

on Proposal to Amend Rule U-50

February 18, 1954

This is a public hearing on a proposal set forth in Holding Company Act Release No. 12217X, dated November 23, 1953, to amend the Commission's Rule U-50.

Comments were originally solicited to be filed on or before December 31, 1953, which time was subsequently extended to February 15, 1954 by Holding Company Act Release No. 12282. On January 21, 1954, Holding Company Act Release No. 12314, this public hearing was called.

The Commission is cognizant of the importance of the action it takes, whether it be to adopt the proposal, to modify it or to withdraw it. Consequently, we desire the help that comes from presentation of divergent points of view. Moreover, because of the legislative character of our rule-making power we would be helped by hearing the answers of the holders of one viewpoint to the arguments of the holders of the other viewpoint.

Comments received by the Commission on any proposal to amend rules historically have not been made available to public examination. The reason given for that policy is that it encourages people to speak freely if they know that their comments will be held confidential. Because a number of opponents of the proposed change in Rule U-50 have requested to see the comments heretofore filed, the Commission has advised those who made comments that in the absence of a request to the contrary, their comments would be available for inspection. So far as I know, no request for confidential treatment has been received and therefore such comments will be made available and an opportunity will be provided to answer them under arrangements which I will describe in a moment.

Our plans for the conduct of the hearing are as follows:

1. Since there are comparatively few persons who have asked to be heard, it will be possible to allow to each firm or organization one hour to present its arguments. If more than one person is to speak for such firm or organization, the time may be divided among all such persons.

2. Those who are in favor of the proposed amendment to Rule U-50 will be heard first in the alphabetical order of the names of the firms or organizations for whom they speak. However, any such firm or organization may yield its place to any other.
3. Those who are opposed to the proposal to amend Rule U-50 will next be heard in similar alphabetical order.
4. If time permits today or tomorrow, there will be given to each such firm or organization a period of 20 minutes to answer arguments theretofore presented by anyone. The order for answering arguments will be the same as the order for principal presentations.
5. A transcript of the oral presentations and copies of comments filed before or at the argument will be available for purchase by any party in interest and an adjourned hearing will be held under similar rules on a day to be announced before the close of this hearing.

These arrangements should give everyone a chance to present everything he has to say on his own behalf or in answer to those who think differently.

The Commission does not desire to take up any substantial portion of the day presenting its own point of view but in the thought that it may be of some service to you in formulating your own arguments I should like to make a few observations.

The Sections of the Public Utility Holding Company Act of 1935 relating to the issuance and sale of securities are 6 and 7. As provided in Section 6(a), securities of registered holding companies and their subsidiaries (other than securities exempted under the terms of Section 6(b)) may not lawfully be issued or sold except in accordance with a declaration filed under Section 7 and with an order from the Commission permitting the declaration to become effective. Section 7(d) provides that (if other requirements are satisfied) the Commission shall permit a declaration to become effective unless the Commission finds that one or more of several conditions exist, including the fact that the terms and conditions of the issue or sale of the securities are detrimental to the public interest or the interest of investors or consumers (Section 7(d)(6)).

Contained in Section 6(b) is a directive to the Commission as follows:

"The Commission by rules and regulations or orders, subject to such terms and conditions as it deems appropriate in the public interest or for the protection of investors or consumers, shall exempt from the provisions of sub-section (a) the issue or sale of any securities by any subsidiary company of a registered holding company, if the issue and sale of such securities are solely for the purpose of financing the business of such subsidiary company and have been expressly authorized by the State commission of the State in which such subsidiary is organized and doing business."

The problem presented by Section 6(b) is a narrow one, namely, in making rules, regulations and orders in carrying out the Congressional directive to exempt the issues described in Section 6(b) what terms and conditions shall the Commission deem "appropriate in the public interest or for the protection of investors or consumers"?

The Act does not indicate the nature of the terms or conditions which may be imposed, but if effect is to be given to the exemption provisions, the extent of what can be required by way of terms or conditions must be something less than what is

required by Section 7, else why the exemption afforded by Section 6(b)? Yet Rule U-50 now applies in the same degree to securities exempt from Section 7 as to securities issued pursuant to that Section. Applications for exemption are granted on condition that the applicant in effect comply with the very provisions from which it seeks exemption.

The legislative history of Section 6(b) indicates that however broad the Commission's power is under that Section to impose terms and conditions, it was not intended that such power be used in a form as to ignore the rights of local regulatory bodies.

The provision of Section 6(b) of the Act which directs the Commission to exempt security issues which have been expressly authorized by a State commission, under the circumstances mentioned in the Section, was not contained in the original Senate bills (S. 1725 - 2796, 74th Congress, 1st Session). The House bill, on the other hand, flatly exempted such issues. The present provision was agreed to in conference. The conference report comments on the provision and indicates that the exemption provision " . . . directs the Commission to exempt the issue of securities by subsidiary companies in cases where holding company abuses are not likely to exist". H. R. Rep. 1903, 74th Congress, 1st Session, 1935 (at p. 67).

Now, is absence of competitive bidding in sales of securities by state regulated utility subsidiaries of holding companies a holding company abuse?

In the original bill introduced in Congress, Section 7(f) included the following phrase: ". . . may condition the issue or sale of a security . . . upon such requirements as to competitive bidding as the Commission may find necessary or appropriate in the public interest or for the protection of investors or consumers". When finally enacted, no mention of competitive bidding was included. Since the Commission's requirement of competitive bidding for state regulated issues of utility companies is based on a general authority to impose terms and conditions and not on categorical Congressional direction, it is appropriate for the Commission at least to reevaluate the requirement. Part VI of Judge Medina's Opinion in the case of United States v. Henry S. Morgan, et al., is enough to stimulate such a reappraisal.

The statute in Section 1(b) does point, among other things, to the evils of (1) an absence of arms-length bargaining, (2) restraint of competition and (3) lack of economies in the raising of capital.

If reliance on state authorization of issues of domestic utility companies would not at this time provide protection from these evils and if these evils in fact exist, then the competitive bidding rule in respect of such issues should not be discarded. If, on the other hand, state authorization is adequate to protect against these evils or if such evils are no longer either a fact or a threat, then we may properly carry out the Congressional mandate to exempt such issues without the imposition of competitive bidding as a term and condition of the exemption.

Assuming the beneficial results from competitive bidding, is it necessary as a matter of national public interest for the Federal Government to require such bidding of operating utility companies in a proceeding duplicating a state regulatory proceeding involving the same factual issues? Is the answer to that question different in the case of equity securities from what it is in the case of debt securities? Should the appeal for competitive bidding be made to management and to the state commissions? These are some of the principal questions to which we are seeking answers. There are other questions such as possible legal doubts as to whether the regulatory commission of a particular state "expressly authorizes" the issue of



securities. You may see other questions. We do not want to confine the discussion. Our minds are open. We shall appreciate enlightenment both as to problems and solutions.

Certain persons opposed to the proposed amendment have requested that this meeting be conducted as an evidentiary hearing with testimony under oath and subject to cross-examination and it has been contended that the Administrative Procedure Act requires that this be done. The proposed amendment of Rule U-50 involves the exercise of the Commission's rule making powers and we are of the opinion that an evidentiary hearing is not appropriate and is not required. Indeed, an informal conference procedure was followed by the Commission at the time Rule U-50 was adopted in 1941. At the conference interested persons were permitted to express their opinions but no sworn testimony was received nor were any of the persons who expressed opinions cross examined in the usual sense of the word. A stenographic transcript of the conference was made and is a part of the record. The written comments received in response to the letter inviting comments on the report of the Public Utilities Division were subsequently included in the record after inquiry was made whether the writers had any objection to such action. In

addition, after the conference was held certain correspondence which had been received following the conference was also included in the record.

Our reason for concluding that this hearing should be conducted in an informal manner will now be briefly stated.

Section 20 of the Holding Company Act includes the following:

"(a) The Commission shall have authority from time to time to make, issue, amend, and rescind such rules and regulations and such orders as it may deem necessary or appropriate to carry out the provisions of this title . . ."

"Rule making" is defined in Section 2(c) of the Administrative Procedure Act which provides in part:

"'Rule' means the whole or any part of any agency statement of general or particular applicability and future effect designed to implement, interpret, or prescribe law or policy \* \*. 'Rule making' means agency process for the formulation, amendment, or repeal of a rule."

In speaking of the Administrative Procedure Act, the Chairman of the House Sub-committee on the Judiciary said:

"In this bill the accepted analytical terminology has been adopted. Accordingly, we speak of rule or rule making whenever agencies are exercising legislative powers. We speak of orders and adjudications when they are doing things which courts otherwise do.

" . . . In rule making an agency is not telling someone what his rights and liabilities are for past conduct or present status under existing law. Instead, in rule making the agency is prescribing what the future law shall be so far as it is authorized to act." 92 Cong. Rec. 5574, 5575.

As previously noted, the Holding Company Act sets forth no procedural requirements for rules and regulations other than their publication as a prerequisite to effectiveness. Section 4 of the Administrative Procedure Act sets forth, generally, procedural requirements for rule making, including instances where rules are not "required by statute to be made on the record after opportunity for an agency hearing". Since the Holding Company Act does not require a hearing for rule making, all that the Administrative Procedure Act does is to impose the requirement of affording "interested persons an opportunity to participate in the rule making through submission

of written data, views, or argument, with or without opportunity to present the same orally in any manner."

In permitting the Commission to exercise its own discretion in determining what, if any, terms or conditions must be imposed in connection with granting exemptions under Section 6(b), the Congress was clearly delegating to the Commission power of a legislative nature. A hearing of the type just described in the words of the Administrative Procedure Act would be more effective than an evidentiary hearing to determine whether the Commission should enlarge the scope of exceptions from Rule U-50.

It has also been contended that inadequate notice of the proposed amendments has been given. The several releases which we have issued collectively comply in full with the notice required by Section 4 of the Administrative Procedure Act. They included (1) a statement of the time, place and nature of the rule making proceedings; (2) reference to the authority under which the amendment is proposed; and (3) the terms of the proposed amendment and a description of the subjects and issues involved. Notice was given of the proposed enlargement of the cases which would be excepted from the requirements of Rule U-50 and, indeed, reference was specifically made to

the Commission's possible consideration of the issuance of additional new rules which would further implement the express purpose of Section 6(b) to place primary regulatory responsibility upon the state regulatory bodies.

In addition, just as was done before Rule U-50 was adopted, the Chairman of this Commission wrote to the various state regulatory agencies inquiring as to the views of those agencies with respect to the proposed amendment to Rule U-50. Similarly, comments were elicited from the companies subject to the Commission's jurisdiction under the Holding Company Act as well as from all other interested persons. The comments received will be part of the record, the Commission believes full and fair disclosure has been made and that there has been more than adequate compliance with the Administrative Procedure Act.

Included among the comments the Commission received, were communications from Baxter, Williams & Company of Cleveland, Ohio, and Halsey, Stuart & Co., Inc. of Chicago, Illinois. The communication from Baxter, Williams & Company included a "motion" and a brief in support thereof. The motion, in substance, requests that the Commission conduct this hearing in accordance with the requirements of Sections 7 and 8 of the

Administrative Procedure Act. A similar suggestion in the nature of an "appeal" was received from Halsey, Stuart & Co. Inc. In view of what has been stated, the Commission has concluded that such a procedure is not required and that the procedure outlined above will comply with the Administrative Procedure Act and the Public Utility Holding Company Act. Accordingly, to the extent such action is necessary, if at all, the Commission has denied the "motion" of Baxter, Williams & Company and the "appeal" of Halsey, Stuart & Co. Inc.

The Commission has also received a communication from the law firm of Wheeler & Wheeler requesting that no further action be taken in connection with the proposed amendment until the Commission has disclosed the nature of the additional new rules it has under consideration for further implementing the specified purpose of Section 6(b) of the Act. The Commission fails to see how such information has any bearing on the question whether this particular proposal should be adopted. Accordingly, the Commission has decided not to accede to the request of Wheeler & Wheeler but rather to proceed with the hearing at this time.

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