SEVENTEENTH ANNUAL REPORT
OF THE
SECURITIES AND EXCHANGE COMMISSION

FISCAL YEAR ENDED JUNE 30, 1951

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SECURITIES AND EXCHANGE COMMISSION

Headquarters Office
425 Second Street NW.
Washington 25, D. C.

COMMISSIONERS

HARRY A. McDONALD, Chairman
DONALD C. COOK, Vice Chairman
RICHARD B. McENTIRE
PAUL R. ROWEN
ROBERT I. MILLONZI

ORVAL L. DuBOIS, Secretary

LETTER OF TRANSMITTAL

SECURITIES AND EXCHANGE COMMISSION,
Washington, D. c., January 11, 1952.

SIR: I have the honor to transmit to you the Seventeenth Annual Report of the Securities and Exchange Commission, in accordance with the provisions of section 23 (b) of the Securities Exchange Act of 1934, approved June 6, 1934; section 23 of the Public Utility Holding Company Act of 1935, approved August 26, 1935; section 46 (a) of the Investment Company Act of 1940, approved August 22, 1940, section 216 of the Investment Advisers Act of 1940, approved August 22, 1940, and section 3 of the act of April 25, 1949, amending the Bretton Woods Agreement Act. Respectfully,

HARRY A. MCDONALD,
Chairman.

THE PRESIDENT OF THE SENATE,
THE SPEAKER OF THE HOUSE OF REPRESENTATIVES,
Washington, D. C.

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FOREWORD

This is the seventeenth annual report to the Congress of the Securities and Exchange Commission, summarizing the work of the Commission during the fiscal year July 1, 1950, to June 30, 1951.

The year has been an extremely active one for the Commission. The raising of new capital by industry, particularly for use in connection with the defense effort, has continued at a high rate. In all, approximately $6,400,000,000 of securities were registered during the year. The processing of registration statements and other documents filed by various companies in connection with their financing programs constitutes a major work load of the Commission. This large amount of work, the volume and timing of which is entirely beyond the control of the Commission, requires thorough and prompt attention for the protection of investors and the accommodation of the issuing companies in their efforts toward successful financing.

In addition, the Commission, under the statutes which it administers, is charged with many other important duties, such as the surveillance of the securities markets, the regulation of the activities of brokers and dealers, and the direction and supervision of the integration and simplification of public utility holding company systems. The report discusses these and the other activities of the Commission. In connection with the discussion of the Commission's activities under the Public Utility Holding Company Act of 1935, the report contains a cumulative tabulation of all companies and properties divested by registered public utility holding company systems since December 1, 1935, the effective date of that Act.

The Commission has endeavored to maintain a high standard of accomplishment in connection with its major work notwithstanding successive drastic reductions in its staff in recent years made necessary by budget limitations. The number of employees of the

Commission, today is about one-half of the number employed in 1941. Since the end of the fiscal year the over-all staff was reduced by 12 percent, from 1027 to 904, up to December 31, 1951, and because of the unavailability of funds a further decrease to about 875 is likely by July 1, 1952. Despite the streamlining of procedures and the deferment and elimination of various routine activities, the reduction in staff has reached a point of being a serious threat to the Commission's ability to carry out its essential duties under the statutes which it has the responsibility of administering and to cooperate promptly and fully in the financing of the defense effort.

COMMISSIONERS AND STAFF OFFICERS
(as of December 31, 1951)

Commissioners

HARRY A. MCDONALD, of Michigan, Chairman -- Term expires June 5, 1956

DONALD C. COOK, of Michigan, Vice Chairman -- Term expires June 5, 1954

RICHARD B. McENTIRE, of Kansas -- Term expires June 5, 1953

PAUL R. ROWEN, of Massachusetts -- Term expires June 5, 1955

ROBERT I. MILLONZI, of New York -- Term expires June 5, 1952 [Footnote: Appointed June 21, 1951, to fill the vacancy created by the resignation of Edward T. McCormick, effective March 31, 1951.]

Secretary: ORVAL L. DuBOIS

Staff Officers

BALDWIN B. BANE, Director, Division of Corporation Finance. ANDREW JACKSON, Associate Director.

MORTON E. YOHALEM, Director, Division of Public Utilities. JEROME S. KATZIN, Associate Director.

ANTHON H. LUND, Director, Division of Trading and Exchanges. SHERRY T. MCADAM, Jr., Associate Director.

ROGER S. FOSTER, General Counsel. LOUIS LOSS, Associate General Counsel.

EARLE C. KING, Chief Accountant.

LEONARD HELFENSTEIN, Director, Division of Opinion Writing.

ALFRED HILL, Executive Assistant to the Chairman.

WALTER C. LOUCHHEIM, Jr., Foreign Economic Adviser to the Commission.

HASTINGS P. AVERY, Director, Division of Administrative Services.

WILLIAM E. BECKER, Director, Division of Personnel. J

AMES J. RIORDAN, Director, Division of Budget and Finance.

REGIONAL AND BRANCH OFFICES

Regional Administrators

Zone 1 -- Peter T. Byrne, Equitable Building (Room 2006), 120 Broadway, New York 4, N. Y. [Footnote: Scheduled for move to 42 Broadway, New York 4, N. Y., in February 1952.]

Zone 2 -- Philip E. Kendrick, Post Office Square Building (Room 501) 79 Milk Street, Boston 9, Mass.

Zone 3 -- William Green, Peachtree Seventh Building (Room 350), Atlanta 5, Georgia.

Zone 4 -- Charles J. Odenweller, Jr., Standard Building (Room 1608), 1370 Ontario Street, Cleveland 13, Ohio.

Zone 5 -- Thomas B. Hart, Bankers Building (Room 630), 105 West Adams Street, Chicago 3, Ill.

Zone 6 -- Oran H. Allred, United States Courthouse (Room 103), Tenth and Lamar Streets, Fort Worth 2, Tex.

Zone 7 -- William L. Cohn, 2 Midland Savings Building (Room 822), 444 Seventeenth Street, Denver 2, Colo. [Footnote: Appointed December 18, 1951, to fill the vacancy created by the death of John L. Geraghty on November 27, 1951.]

Zone 8 -- Howard A. Judy, Appraisers Building (Room 308), 630 Sansome Street, San Francisco 11, Calif.

Zone 9 -- James E. Newton, 1411 Fourth Avenue Building (Room 810), Seattle 1, Wash.

Zone 10 -- E. Russel Kelly, 425 Second Street NW., Washington 25, D. C.

Branch Offices

Federal Building (Room 1074), Detroit 26, Mich.

United States Post Office and Courthouse (Room 1737), 312 North Spring Street, Los Angeles 12, Calif.

Pioneer Building (Room 400), Fourth and Roberts Streets, St. Paul, Minn.

COMMISSIONERS APPOINTED DURING FISCAL YEAR

Robert I. Millonzi

Mr. Millonzi was born in Buffalo, N. Y., on July 12, 1910. He received an A. B. degree in 1932 and an LL. B. degree in 1935 from the University of Buffalo. He was admitted to practice before the New York State Supreme Court in 1935, and subsequently admitted to practice before the Federal Courts and the Tax Court of the United States. Until his appointment as a member of the Securities and Exchange Commission in 1951, he was engaged in private practice in New York, associated with the firm of Diebold and Millonzi. From 1940 to 1943 he was Counsel to the New York State Department of Agriculture and Markets. On June 21, 1951, he was appointed a member of the Securities and Exchange Commission for a term of office ending June 5, 1952.

PART I
ADMINISTRATION OF THE SECURITIES ACT OF 1933

The Securities Act of 1933 is designed to provide investors with the protection of full and fair disclosure, by means of registration statements and prospectuses, of pertinent information regarding securities publicly offered for sale through the mails or other instrumentalities of interstate commerce, and to prevent misrepresentation, deceit, and other fraudulent practices in the sale of securities. The Act requires in general that every security which is to be offered for sale by the use of the mails or other instrumentalities of interstate commerce must first be registered with this Commission unless it is entitled to one of the exemptions from registration provided in the statute. Securities so exempted consist, in general, of United States government and municipal securities and issues of banks, railroads, cooperatives and other organizations and associations specified in section 3 (a) of the Act or covered by exemptions in rules and regulations adopted by the Commission, as discussed elsewhere in this report, pursuant to section 3 (b) thereof. The

registration provisions also do not apply to certain transactions specifically exempted by section 4 of the Act. However the anti-fraud provisions of both Acts apply to exempted securities and transactions. The fact that a registration statement has been filed under the Act, or that it has been examined by the Commission's staff, or that it is in effect, does not imply any approval or disapproval by the Commission of the merits of the security as an investment, and the statute makes any representation to the contrary a criminal offense. While registration, therefore, does not insulate investors against risk, the requirement that registrants must furnish investors at or before a sale with a full disclosure of material facts essential to the formation of an intelligent investment judgment makes available to them information with which to gage the risk.

THE REGISTRATION PROCESS

The Registration Statement and Prospectus

Any security may be registered with the Commission by filing a registration statement under the terms and conditions specified in the Act, and it is one of the Commission's most important functions to examine these statements for their compliance with the statutory requirements. An integral part of each statement is the prospectus, consisting of pertinent information from the registration statement proper. Unless a registration statement is in effect as to a security, the Act makes it unlawful to sell or offer to buy the security through the mails or in interstate commerce, and it is also made unlawful to sell or deliver any security unless accompanied or preceded by a prospectus meeting the requirements of the Act.

While as a practical matter it is the prospectus that brings all the pertinent information contained in the registration statement directly to the attention of the investor, it should be pointed out that the event of filing any registration statement, which is immediately made public by the Commission pursuant to the statute, gives rise to widespread publicity released by financial news services, financial writers, and newspapers generally, covering various items of information selected by them from the registration statement.

Effective Date of Registration Statement

In order to permit the information contained in a registration statement to become known to the investing public, the Act provides a 20-day waiting period after the filing of the registration statement before the registration statement becomes effective and the security may be offered for sale. If the registration statement is amended after it is filed but before it has become effective, the 20-day waiting period starts anew from the time of the amendment, unless the amendment is filed with the consent of or by order of the Commission. The Commission is empowered at its discretion to accelerate the effective date of a registration statement, in cases where the facts justify such acceleration, so that a full 20-day period need not expire before the securities may be offered for sale. The Act

directs that, in the exercise of this power, the Commission must give due regard to the adequacy of the information about the security already available to the public, to the complexity of the particular financing, and to the public interest and the protection of investors.

Examination Procedure

The Commission's work of examining registration statements and prospectuses filed in connection with public offerings of securities under the Securities Act of 1933 is conducted by the examining sections of the Division of Corporation Finance. If a registration statement presents problems of an oil and gas, mining, or engineering nature, appropriate technical experts on the staff cooperate with the examiner, accountant and attorney of the examining section in processing that document. Not infrequently the staff may have occasion to consult with other departments or agencies of the Government in completing the examination of a particular filing.

In order to simplify the preparation of registration statements calculated to meet the requirements of the statute and the rules, the Commission has continued to make available to the registrant the assistance of a profiling conference with its staff of expert analysts, accountants and lawyers. The prefiling conference is employed most usually to advise the prospective registrant concerning appropriate methods of simplifying any material required to be filed in a registration statement or other document, or to help solve any other problem -- whether legal, statistical, or accounting -- anticipated in connection therewith. A large number of these prefiling conferences deal mainly with methods of simplifying the presentation of required financial data. Failure to take advantage of the latitude permitted by the Commission's rules to omit duplicate material or to substitute comparable material in more compact form may result in a confusing mass of financial statements particularly when dealing with complicated cases such as those involving mergers, reorganizations and the acquisition of other companies and businesses. In such situations the pre-filing conference may result in avoiding the delay, inconvenience and expense that would otherwise be caused by the need of furnishing substantial revisions or amendments of material after the original filing. Thus in one recent case the number of pages of financial statements proposed to be included in a prospectus of a company operating a chain of hotels was reduced by half mainly by adopting a suggestion of eliminating unnecessary financial statements and repetitious financial footnotes. In another case, involving a new company formed to take over the businesses of several other companies, the number of pages of financial statements included in the prospectus was reduced to less than half the number originally proposed by adopting a suggestion to arrange several similar financial statements on the same page in columnar form and eliminate certain duplicate financial footnotes.

Where examination discloses any omission or incomplete statement of material fact or inaccuracy in the registration statement, the staff relies for enforcement mainly upon another informal procedure, that of sending the registrant a "letter of comment," which

points out the inadequacies found upon examination. Such letter is sent as soon as possible after the statement is filed and affords an opportunity for the filing of a correcting amendment before the indicated effective date of registration. This device avoids the necessity for the Commission to exercise its little-used authority under section 8 of the Act to institute formal proceedings against the registration statement. While the statute does not specifically authorize such a procedure, perhaps no other device adopted in connection with the registration process has equal capacity to accomplish a common-sense administration of the Act in a manner calculated to afford fair treatment to registrants and cause a minimum of interference with financing plans.

Time Required for Registration

While the Commission makes every effort to complete the registration process within the statutory 20-day waiting period, accomplishment of this objective is often impeded by a number of variable factors largely beyond its control. For example, experience has shown that the time required by the staff to complete examination of the registration statement and send out the letter of comment regarding indicated deficiencies to the registrant cannot generally be reduced in the average case below a recently achieved low of 10 calendar days. In the 1949 fiscal year the actual time required for this step averaged such 10 days in each month of the year. However, in the 1950 fiscal year, while for two of the early months of the period this average was bettered with a showing of 9 days each, in two of the later months the average rose to 11 days and in the closing month reached 12 days. During the 1951 fiscal year, as may be seen from the table below, this average rose to 11 days in four separate months of the year. Another important variable factor in the time required to complete the registration process is the time elapsing between the date of the letter of comment and the date the registrant's correcting amendment is filed, which of course is wholly beyond the control of the Commission. Then follows the necessarily variable factor of time required by the staff to examine such amendment in the same manner as the original filing. The average time required in each month of the 1951 fiscal year for each of these principal stages as well as for all steps combined in the registration process is shown in the accompanying table. The total elapsed time, which was as high for the average case as 30 1/2 days for the whole of the year 1947, and which had dropped to an all-time low of 21 1/12 days for 1950, showed the same low figure of 21 1/12 days for 1951.

(chart omitted)

VOLUME OF SECURITIES REGISTERED

The amount of securities effectively registered during the 1951 fiscal year was $6,459,333,000, making the sixth consecutive period of registrations in excess of $5,000,000,000 each and averaging over $6,200,000,000 per fiscal year. This average is more than three times the approximate annual average of $2,000,000,000 for the previous

six fiscal years. More than three-quarters of the effective registrations are for cash sale for account of issuers, and the comparatively high current registration rate is equally apparent in this principal item and its components.

(chart omitted)

Number of Statements

The amount registered in the 1951 fiscal year was distributed over 487 statements covering 702 issues, compared with the same number (487) of statements covering 647 issues during the previous fiscal year. The number differs slightly from that shown under "Registration Statements Filed" on a subsequent page, as explained in footnote 2 of appendix table 1.

Type of Registration

About 80 percent of the amount registered in the 1951 fiscal year was for cash sale for account of issuers, 2.3 percent was for cash sale for account of others than issuers, and 17.7 percent was for other than cash sale as itemized in part 3 of appendix table 1. Comparative figures are as follows:

(charts omitted)

From similar tables in recent annual reports, it can be ascertained that of approximately $29.1 billion effective registrations for cash sale for account of issuers during the past six fiscal years, $10.0 billion were electric, gas, and water, $5.85 billion were transportation and communication, $5.75 billion were manufacturing, $5.47 billion were financial and investment, $1.13 billion were foreign government, and all others were less than $1.0 billion. "Transportation" does not include issues subject to Interstate Commerce Commission filings and therefore exempt from registration.

Recent trends have been for electric, gas and water issues to head the list, for financial and investment issues to rise into second place, and for manufacturing issues to drop from first place in 1946 and 1947 to third place in 1951 fiscal year. Foreign government registrations for 1951 are unusually large by reason of inclusion of the $500,000,000 State of Israel bonds.

Type of Security

Bonds amounted to 54.9 percent of the total registered in the 1951 fiscal year for cash sale for account of issuers, preferred stocks to 8.3 percent, and all other equity securities to 36.8 percent, as shown by the following figures:

(chart omitted)

Type of Offering

Over 49 percent of the securities registered for cash sale for account of issuers in the 1951 fiscal year were to be sold through investment bankers pursuant to agreements to purchase for resale. About 34 percent (including $0.84 billion open-end investment company issues) were to be sold on a "best-efforts" basis. The term "best-efforts" as used here means all offerings through investment bankers other than those pursuant to agreements to purchase for resale. The remaining 17 percent were to be sold direct by issuers to investors. Comparative figures follow:

(chart omitted)

Purpose of Issue

Nearly 51 percent of the net proceeds of the securities registered for cash sale for account of issuers in the 1951 fiscal year were for new money purposes including plant, equipment, working capital, etc. About 12 percent were for the retirement of debt and preferred stock. About 25 percent were for the purchase of securities, principally by investment companies. The remaining 12 percent were for use of foreign governments. The figures are shown in detail in part 3 of appendix table 1.

Cost of Flotation

Commissions and discounts to investment bankers, in the case of new issues effectively registered for cash sale through them to the general public, have amounted to approximately the following per-cents of gross proceeds:

(chart omitted)

The above showing is exclusive of investment company securities, offerings through rights to existing stockholders, securities sold to special groups such as officers and employees, and securities registered for other than cash sale. The commissions and discounts shown on bonds in the above table are broken down by quality and size of issue in appendix table 2 of this report and its predecessors.

Early in 1951, the Commission published a report entitled "Cost of Flotation, 1945-49" covering all securities effectively registered under the Securities Act of 1933 during those five calendar years. The total was nearly $30 billion and represented nearly 3,500 issues. The primary purpose was to present basic factual data on a matter of public interest which had been regarded as a trade secret prior to 1933, and to provide more complete coverage and detail on cost of flotation than can as yet be found elsewhere. The cost of flotation of the approximately $30 billion securities aggregated a figure equal to $2.64 for

every $100 of gross proceeds, including $2.12 commissions and discounts to investment bankers and $0.52 other expenses. New issues of securities for cash sale through investment bankers to the general public, not including issues of investment companies, came to about half of the $30 billion, and produced the following aggregate costs in percent of gross proceeds:

(chart omitted)

New issues of securities for cash sale through subscription rights to stockholders constituted the second largest group, about 13 percent of the total, and produced the following aggregate costs in percent of subscription prices and without taking into consideration as an element of cost the discount from market prices at which the subscriptions were invited:

(chart omitted)

Securities of investment companies amounted to about 11 percent of the total dollar amount of securities effectively registered for cash sale during the five-year period 1945-49. About 70 percent of this amount was of open-end companies, 4 percent of closed-end companies, and 26 percent of fixed trusts, face-amount certificates and investment plans. The cost of marketing securities of open-end companies is called the "sales load" and averaged 7.88 percent of the gross proceeds of 246 flotations over the five years.

The publication referred to shows comparable figures for the remaining groups: new issues for cash sale directly to the general public, to special groups such as officers and directors, and in exchange for outstanding securities, secondary distributions registered for account of selling security holders, and securities for future issuance in conversions and other purposes. It is implemented by another quarterly publication of the Commission styled "Cost of Flotation" which, commencing with the first quarter of 1950, presents data on the cash cost of marketing individual issues of securities registered during each period, including details of offering, underwriting compensation, other expenses of notation divided into (1) cost of professional services, (2) taxes and fees, and (3) printing and other expenses, and supplementary data reported by registrants on the outcome of issues involving subscription rights or offers of exchange. Current copies of the quarterly "Cost of Flotation" may be obtained from the Superintendent of Documents, Government Printing Office, Washington 25, D. C.

ALL NEW SECURITIES OFFERED FOR CASH SALE

Registered Securities

Securities effectively registered under the Securities Act of 1933 which were offered for cash sale for account of issuers during the 1951 fiscal year amounted to $3,135,000,000,

approximately the same amount as for the preceding fiscal year. Three-fourths of these offerings of registered securities during the fiscal year took place in the first six months of 1951. The amounts of such offerings in the last two years, valued at actual offering prices, were as follows:

Corporate
1951: $2,957,000,000
1950: $2,987,000,000

Foreign government
1951: $178,000,000
1950: $176,000,000

Total
1951: $3,135,000,000
1950: $3,163,000,000

These totals exclude securities sold through continuous offering, such as issues of open-end investment companies, employee purchase plans, and the $500,000,000 State of Israel bonds in process of sale at the close of the fiscal year.

Unregistered Securities

Corporate

During the 1951 fiscal year, $3,953,000,000 of unregistered corporate securities are known to have been offered for cash sale for account of issuers, including a record volume of securities placed privately. The basis for exemption of these securities from registration is as follows:

(chart omitted)

Noncorporate

Unregistered government and eleemosynary securities offered for cash sale in the United States for account of issuers during the 1951 fiscal year amounted to $13,318,000,000 as compared with $15,678,000,000 in the 1950 fiscal year. These totals consisted of the following:

(chart omitted)

Use of Net Proceeds of Corporate Securities

Proceeds from corporate securities flotations for cash sale for account of issuers, both registered and unregistered, were mainly to be used for expansion of fixed and working capital, approximately $5,263,000,000 being raised for these purposes. This amount was considerably higher than the $3,843,000,000 for new money purposes during the 1950 fiscal year, but was approximately $500,000,000 less than in the 1949 and 1948 fiscal years. Electric and gas companies accounted for 34 percent of the new money financing, manufacturing for 32 percent, communication for 10 percent, real estate and financial for 9 percent, railroad and other transportation for 8 percent, and commercial and miscellaneous companies for 7 percent. Corporate securities offered for cash sale for retirement of outstanding securities and bank debt totaled only $1,204,000,000 as compared with $1,651,000,000 in the 1950 fiscal year.

REGISTRATION STATEMENTS FILED

A considerable increase occurred last year in the number and dollar amount of new financing involved in registration statements. Thus, as set forth in the table below, there were filed and examined in the 1951 fiscal year 544 registration statements covering proposed offerings in the aggregate of $6,371,827,423, compared with figures of 496 registration statements and proposed offerings in the aggregate of $5,220,654,010 in the 1950 fiscal year.

(chart omitted)

Additional documents filed in the 1951 fiscal year under the Act

Material amendments to registration statements filed before the effective date of registration: 777

Formal amendments filed before the effective date of registration for the purpose of delaying the effective date: 476

Material amendments filed after the effective date of registration: 642

Total amendments to registration statements: 1,895

Supplemental prospectus material, not classified as to amendments to registration statements: 1,074

Reports filed under section 15 (d) of the Securities Exchange Act of 1934 pursuant to undertakings contained in registration statements under the Securities Act of 1933:

Annual reports: 735

Current reports: 2,996

EXEMPTION FROM REGISTRATION UNDER THE ACT

The Commission is authorized by section 3 (b) of the Act to adopt rules and regulations granting exemptions from the registration requirements for security offerings not exceeding $300,000 in aggregate offering price to the public. The most important of the regulations adopted under this section are Regulation A, which provides a general exemption for small issues up to the statutory maximum permissible amount of $300,000, and Regulation B, which affords an exemption for fractional undivided interests in oil or gas rights and is limited to a maximum aggregate offering price of $100,000. [Footnote: Under another such exemption, that provided by Regulation A-M for assessable shares of stock of mining companies, the Commission received and examined 8 prospectuses covering securities having an aggregate offering price of $475,688 during the 1951 fiscal year.]

These regulations granting exemption from registration pursuant to section 3 (b) carry no exemption from the civil liabilities for misstatements or omissions imposed by section 12 or from the criminal liabilities for fraud imposed by section 17. They simply permit the making of a small offering on the basis of less complete disclosure than in the case of a registered security and require the filing of certain minimum information with the nearest regional office of the Commission a certain number of days before the offering may be made. [Footnote: An offering may be made under Regulation A five business days after the letter of notification is filed with the Commission. An offering sheet complying with the requirements of Regulation B becomes effective on the eighth calendar day after it is filed with the Commission.] If any sales literature is to be used, it must be filed in advance of its use.

Exempt Offerings Under Regulation A

After three successive years had shown a slight decrease in the amount of small financing undertaken pursuant to Regulation A, the 1951 fiscal year shows a slight increase therein and reflects at least a halt to any such previous trend.

Fiscal year 1947
Number of letters of notification filed: 1,513
Aggregate offering price: $210,791,114

Fiscal year 1948
Number of letters of notification filed: 1,610
Aggregate offering price: $209,485,794

Fiscal year 1949

Number of letters of notification filed: 1,392
Aggregate offering price: $186,782,661

Fiscal year 1950
Number of letters of notification filed: 1,357
Aggregate offering price: $171,743,472

Fiscal year 1951
Number of letters of notification filed: 1,358
Aggregate offering price: $174,277,762

Included in the 1951 fiscal year totals are 141 letters of notification covering stock offerings filed by companies engaged in some phase of the oil and gas business.

In addition to the total of 1,358 letters of notification, there were received and examined during the past fiscal year 1,212 amendments to these letters of notification and also 1,741 filings of sales literature to be used in connection with such offerings.

Information available as to 1,351 of these offerings in the 1951 fiscal year shows that 751 covered proposed offerings of $100,000 or less; 251 more than $100,000 and less than $200,000; and 349 more than $200,000 but not more than $300,000. Issuing companies made 1,122 of these offerings; stockholders 215; and issuers and stockholders jointly, the remaining 14. Less than half, or 588 of them, were underwritten, 452 by commercial underwriters and 136 by officers and directors and other persons not regularly engaged in the underwriting business.

Regulation A provides a means whereby small businessmen may seek from public investors the relatively small amounts of venture capital which they ordinarily require; and it may be of interest to note, from the filings made in the 1951 fiscal year as distributed by regional offices, how this regulation is used by issuers located in every part of the nation.

(chart omitted)

Exempt Offerings Under Regulation B

The exemption from registration provided by Regulation B for fractional undivided interests in oil or gas rights is limited, as previously indicated, to a maximum offering price of $100,000. A person intending to sell securities under this regulation must file with the nearest regional office of the Commission an offering sheet which calls for a brief summary of pertinent information regarding the security being offered.

During the 1951 fiscal year, the Commission received and examined 96 offering sheets together with 76 amendments to such offering sheets. These filings are in addition to the

141 offerings under Regulation A which covered oil and gas securities. The following actions were taken on these Regulation B filings:

Action taken on filings under Regulation B

Temporary suspension orders (rule 340 (a)): 18

Orders terminating proceedings after amendment: 12

Orders consenting to withdrawal of offering sheet and terminating proceeding: 5

Orders terminating effectiveness of offering sheet: 3

Orders consenting to withdrawal of offering sheet (no proceeding pending): 3

Orders accepting amendment of offering sheet (no proceeding pending): 44

Total orders: 85

Of the 76 amendments received during the year, approximately 44 were filed as a result of informal letters of comment sent by the staff rather than of formal suspension orders. The Commission maintains a specialized oil and gas unit in the Division of Corporation Finance at its headquarters to administer Regulation B and to advise and assist with technical phases of all offerings of oil and gas securities arising under various provisions of the Securities Act and other statutes administered by the Commission. For example, during the year this unit participated in the examination of 78 registration statements, and 57 amendments thereto, filed under the Securities Act, and reviewed 47 broker-dealer inspection reports made pursuant to the Securities Exchange Act, which involved securities of oil producing, natural gas, or refining companies. Petroleum geologists conduct field investigations of tracts and wells and furnish advisory reports thereon in connection with investigations made by the Commission and its regional offices. Development activity in the Rocky Mountains which was noted in the 1950 fiscal year has been extremely marked during the 1951 fiscal year.

Confidential written reports of sales under Regulation B. -- The Commission received and examined under rules 320 (a) and 320 (c) and (d) during the 1951 fiscal year 1,922 confidential written reports on Forms 1-G and 2-G relating to actual sales made pursuant to Regulation B in the aggregate amount of $1,127,226. This total may be compared with $829,875 during the preceding year. These reports are of assistance to the Commission in determining whether violations of law occur in sales of oil and gas securities exempted from registration.

Oil and gas investigations. -- The Commission conducts a considerable number of oil and gas investigations, arising largely out of complaints received from the public, to

determine whether there has been any violation of any other provision of law in the sale of securities exempted under Regulation B, with particular attention to the registration requirements of section 5 and the fraud prohibitions contained in section 17 of the Securities Act. Not infrequently in such an investigation it may be necessary to conduct extensive field trips in the ascertainment of certain material facts. Depending upon the circumstances of the particular case, a field trip may involve an inspection of well locations, a study of the productive history or oil possibilities of the areas under consideration, interviewing and taking depositions of persons who worked on the wells, getting affidavits from the purchasers of oil where there has been actual production, obtaining authenticated statements by State officials of well logs, plugging records, tax records and production records that have been filed pursuant to the statutes of the States in which the operations took place, the preparation of maps and similar activities.

Often investigation is directed to highly objectionable sales literature which greatly overemphasizes the possibilities of success from the proposed security purchase. So it was in the case of Oil Prospectors, Inc. and Ralph Malone, which offerors had made a number of filings under Regulation A, and in virtually all instances used such literature. In this situation the Commission made a field examination of a lease and well in Texas and filed a complaint in the United States District Court, Northern District of Texas, against the offerors, charging violation of the anti-fraud provisions of section 17 (a) in the sale of capital stock of Oil Prospectors, Inc. A temporary restraining order was issued immediately after the close of the fiscal year, on July 2, 195f, and a hearing was expected on the Commission's motion for a permanent injunction shortly thereafter.

As suggested above, a substantial number of these oil and gas investigations grow out of violations of the registration requirements of section 5. In one such case, J. Stacey Henderson, and others, sold fractional working interests in test wells located in Caddo Parish, Louisiana, without making any attempt to comply with the registration provisions of section 5. A Commission engineer visited the immediate location of the test wells and Shreveport where he gathered necessary geological and production data. At the separate trial of Henderson which ensued, where the Commission engineer gave expert testimony as to the geological conditions and productive possibilities of the area, Henderson was found guilty on one count of an indictment charging violation of the Mail Fraud Statute in connection with the sale of fractional undivided interests in oil and gas rights and was sentenced to serve five years in prison and to pay a fine of $1,000 and costs.

An additional case illustrates the fact that often an oil and gas investigation is of important assistance to other regulatory work of the Commission. As discussed elsewhere in this annual report, the Commission issued during the 1951 fiscal year a stop order under section 8 (d) against the grossly inaccurate, misleading and incomplete registration statement of Ralph A. Blanchard and George P. Simons doing business as Northwest Petroleum. Eight days after the filing of that registration statement the Commission obtained an injunction from the United States District Court for the District of Oregon against these registrants from selling the shares or interests they proposed offering the

public until such time as a registration statement with respect thereto became effective. Contributing largely to the facts upon which this injunction was granted was a technical report resulting from an investigation made by the oil and gas staff, especially regarding the productive capacity and other technical characteristics of the oil wells involved in the offering.

FORMAL ACTION UNDER SECTION 8

In almost all instances the Commission's informal examination procedures, such as the profiling conference and the letter of comment, are sufficient to insure that the registration statement meets the standards of fair disclosure prescribed by the statute. However, there are infrequent instances when it becomes necessary to exercise its powers under section 8 in order to prevent a registration statement from becoming effective in deficient, misleading or inaccurate form or to suspend the effectiveness of one which has already become effective. Under section 8 (b) the Commission may institute proceedings to determine whether it should issue an order to prevent a registration statement from becoming effective. Such proceedings are authorized if the registration statement as filed is on its face inaccurate or incomplete in any material respect. Under section 8 (d) proceedings may be instituted at any time to determine whether the Commission should issue a stop order to suspend the effectiveness of a registration statement if it appears to the Commission that the registration, statement includes any untrue statement of a material fact or omits to state any material fact required to be stated or otherwise necessary to make the statements included not misleading. Under section 8 (e) the Commission may make an examination to determine whether to issue a stop order under section 8 (d).

Stop-order Proceedings Under Section 8 (d)

One stop order was issued during the year and another stop-order proceeding was instituted just before the close of the year (where the hearing was scheduled after such close) pursuant to section 8 (d). The former case is described below.

Ralph A. Blanchard and George P. Simons -- doing business as Northwest Petroleum -- File No. 2-8243. -- This case was completed during the 1951 fiscal year although instituted previously.

Prior to the filing of the registration statement about $300,000 had been raised by sales of shares to public investors, of which about $30,000 was retained by the promoters and about $270,000 was turned over to Mon-O-Co Oil Corporation for drilling operations. With the exception of one well, which had a rated capacity of 20 barrels per day, the wells which were drilled were completely unproductive.

In the registration statement as originally filed it was represented that 350 shares were being offered; as amended during the course of the proceedings, the registration statement recited that 447 shares, of which 330 were "company shares" and 117 shares were "personal shares," were being offered at $500 a share, or an aggregate of $223,500. However, the amendment did not specify the order in which company shares or personal shares would be sold. The Commission, in its disposition of this case, found that the failure of the registrants to include a definite undertaking with respect to the order in which the company and personal shares were to be sold, in order adequately to inform prospective purchasers of the order in which proceeds of a sale of less than all of the shares were to be applied, rendered the registration statement as amended materially misleading.

The Commission also found that, in view of the extensive experience of Mon-O-Co and the promoters in attempting to exploit the tracts in question, the registrants knew that in all probability further drilling operations would not result in a return sufficient to warrant the investment of funds by the public on the basis contemplated by registrants, and that the failure of the registrants to make the disclosures necessary to a full understanding by prospective shareholders of the actual prospects of return rendered the registration statement misleading.

The Commission concluded that the registration statement was grossly inaccurate, misleading and incomplete, and issued a stop order suspending its effectiveness. At the close of the 1951 fiscal year the registrants had not attempted to correct the deficiencies found in the registration statement and the stop order was still in effect.

DISCLOSURES RESULTING FROM EXAMINATION OF REGISTRATION STATEMENTS

The result of the Commission's work in the examination of registration statements may be illustrated by the cases described below.

Misleading security description revised -- Dividend rights and earnings prospects clarified -- Position of promoters and new investors contrasted. -- A company operating a life, health and accident insurance business filed its first registration statement under the Securities Act of 1933 purporting to cover an issue of "Special Stock Debentures" to be offered in units of $500 each. It appeared to the staff upon examination of the statement that these securities were not debentures at all, as the term is commonly understood, but were essentially contracts for the purchase of capital stock. Thus, the purchaser of the "debenture" agreed to pay $500 (all at one time or in installments) and the company agreed in consideration thereof to deliver at the end of five years 25 shares of common capital stock. In each of these five years the purchaser was entitled to receive the equivalent of such dividends as would be paid on 25 shares of stock were such shares already issued; and he was entitled to an additional distribution based upon a percentage

of the amount of life insurance renewal premiums paid to the company by its policy holders in each such year. The company referred to this latter distribution as a "bonus." Apart from making use of such misleading nomenclature as "debentures" and "bonus," the prospectus as originally filed was so prepared as to make it virtually impossible for even a skilled analyst to form a reasonable judgment of the investment merits of the securities.

In the ensuing examination process the prospectus and the security instrument itself were amended to substitute the term "Special Investment Contract" for "Special Stock Debenture"; and the term "bonus," which ordinarily means something given beyond-what is strictly due, and which did not appear to be applicable to any feature of these securities, was dropped.

To provide investors with some indication of what the purchaser's right to dividend equivalents might be worth, the amended prospectus also pointed out that earnings per share during the past four years had amounted to 30 cents, 62 cents, 12 cents, and 13 cents, respectively, and, to provide them with an indication of what the right to distributions based on the life insurance renewal premium business done by the company might be worth, it was furthermore pointed out in the amended prospectus that, if the amount of such business done in 1950 were applied, total distributions over the five-year period would amount to some $28.14. It thus becomes apparent that, notwithstanding the specification in the investment contract that $25 of the $500 purchase price was to be attributed to the 25 shares of stock which the contract called for, and the remaining $475 was to be attributed to the rights to dividend equivalents and distributions based on life insurance renewal business, the cost of the stock should properly be regarded as very much greater than $25 ($1 per share). In this connection the amended prospectus states: "It should be noted, therefore, that very substantial increases in earnings will be necessary if purchasers of the investment contracts are to enjoy a satisfactory return on the stock they will receive at the price they are paying."

The amended prospectus also introduces an explanation that, assuming eventual issuance of all of the stock called for by the investment contracts in accordance with the terms of the contracts, the original incorporators will hold some 72 percent of the outstanding stock for which they paid approximately $37,500, in contrast to the position of incoming investors who will receive only an 18 percent interest in the company in exchange for a total contribution of $1,200,000.

In addition, the amended prospectus discloses that one of the company's two largest stockholders has repeatedly borrowed substantial sums from the company and that a presently outstanding loan (originally $600,000 but at the date of the prospectus reduced to $378,000) admittedly was under-collateralized by about 50 percent. This stockholder, the amended prospectus further discloses, profited to the extent of some $59,000, on a $500 investment, in the sale of property to the company, and to the extent of some

$15,000 in connection with the purchase by the company of the business of another insurance company.

Besides, this registrant was called upon to file very substantial amendments to the financial statements included in the registration statement proper which were deemed by the staff to be necessary in order to meet the standards of disclosure imposed by the Act. The more significant of the deficiencies in these financial statements as originally filed involved the inclusion in income of (1) proceeds from the sale of the securities, (2) amounts received as contributed surplus, (3) borrowed money received and repaid, and (4) payments and adjustments for retirement of outstanding bonds. Following discussions with the staff, the company filed financial statements which were appropriately amended to reflect generally accepted accounting principles, resulting in a reduction of 1950 reported net income from $124,000 to $33,000 (approximately), and a reduction of earned surplus as of December 31, 1950, from $231,000 to $102,000 (approximately).

Events after date of financial statements recognized. -- When a utility company filed its registration statement for an offer of common stock in March 1951, the 1949 and 1950 income statements included approximately $125,000 and $415,000 ($75,000 and $228,000 after taxes), respectively, and the balance sheet included a deferred credit for contingent revenues of approximately $412,000 (equivalent to $227,000 after taxes) for revenues billed by the registrant pursuant to a rate increase granted by the local regulatory commission. At the time of filing the statement the United States Court of Appeals had affirmed the action of the United States District Court in vacating the regulatory commission's order and had ordered amounts collected after a certain date impounded. The court had ordered that the registrant refund to its customers all monies collected under the increased rates but had granted a stay of its judgment pending appeal to the Supreme Court.

The above situation was fully disclosed in the financial statements and matters requiring amendment had been corrected to put the statement in final form. However, at about the time the registration statement was to become effective the Supreme Court of the United States refused to review the appellate court's findings that the order of the local regulatory commission be vacated. The registrant and its accountants then proposed to expand the footnote describing the litigation to explain the effect of the Supreme Court's action but without eliminating from the income statements the revenues then to be refunded or correcting the balance sheet to show the liability for the ordered refund. However, the registrant was requested by the staff to adjust the income statements and balance sheet in respect of the refundable amounts, since, under the circumstances, no accounting justification then existed for including in the income statements amounts which clearly were not proper revenue items and for failing to show the proper current liabilities.

The statements were amended to remove the amounts in question from the income statements and to show them in the balance sheet, together with the $412,000 originally

shown as a deferred credit, as a current liability ($614,000) after deducting impounded funds of $336,000. The effect of the change on earnings and earned surplus was as follows:

1949 net income
As originally filed: $1,471,000
As amended: $1,398,000

1950 net income
As originally filed: $2,489,000
As amended: $2,261,000

Earned surplus
As originally filed: $7,434,000
As amended: $7,133,000

Earnings restated to reflect taxes and loss carry-over. -- A registrant's prospectus as originally filed included a summary of earnings showing a net loss of $142,000 for the first fiscal year of its operations (certified by independent public accountants) and net profits of $110,000 and $216,000 for the succeeding two months (unaudited). No franchise, income and excess profits taxes had been deducted and the registrant was therefore asked to make appropriate provision for such taxes. The summary, as then amended, showed the net loss of $142,000 for the company's first full year, and set forth net profit for the succeeding three months combined of $168,000, after deducting a provision of $218,000 for franchise, income and excess profits taxes. However, the staff discovered that, in computing the income and excess profits taxes for the three-month period, the company had deducted the full amount, rather than one-quarter of the amount, of allowable net operating loss carry-over from the first fiscal year. Pursuant to the request of the staff, the summary was again revised, on the presumption of continuing profitable operations which the registrant did not disclaim, to show the taxes for the first quarter of the second year computed on the basis of deducting only one-quarter of the first year's allowable net operating loss carry-over. As finally revised, the summary showed net profit (after taxes) of $116,000 for the quarter -- compared with the profit figure of $168,000 for the same period as shown in the first revision and that of $326,000 for two months only of such period as set forth in the original filing.

Restatement of balance sheet to eliminate unearned rents and royalties as assets. -- In the course of an examination of an amendment to an effective registration statement of a machine manufacturer it was noted that the proportion of rental income to sales of products had increased materially and that the items of "Trade Receivables with Extended Maturities" and "Deferred Rental Income" had become major elements in the balance sheet. In response to a request that the method of accounting be explained, a representative of the company disclosed to the Commission that the former account represented payments not due within the ensuing year on notes and contracts receivable

covering rentals of leased machines and that the leases normally called for payment of rentals over a period of forty-eight months. Further explanation revealed that it was the practice of the company to record the full amount of rent receivable upon execution of the leases and to credit an equal amount to deferred income from which transfers were made to profit and loss on a straight-line basis over the useful life of the machines, then estimated at five years. Since this method of accounting appeared to be unique among companies doing business on a similar basis, the staff requested that the financial statements be amended to eliminate from the accounts the rents and royalties not earned at the balance sheet date except to the extent that collections had been made in advance of the due dates. Further discussions with representatives of the registrant and its independent accountants brought concurrence with the staff's views and resulted in an amendment the significance of which may be seen from the following figures. "Rentals and Royalties Receivable under Machinery Lease Agreements" listed under current assets were reduced from $3,500,000 to $800,000 and "Trade Receivables with Extended Maturities" were reduced from $4,730,000 to $24,000, accounting for a total of $7,400,000 applied as a contra reduction of "Deferred Rental Income" from $9,100,000 to $1,700,000. The above adjustments reduced total current assets from $17,300,000 to $14,600,000, with a resulting reduction in the current ratio from 1.61-to-l to 1.34-to-l, and reduced the balance sheet totals from $40,900,000 to $33,500,000. Since the statements on the former basis had been published, the change in presentation was referred to in the "Accountants' Report" and explained in the following "Supplemental Note" added to the financial statements by way of amendment to the registration statement:

Since the closing of the accounts for the fiscal year ended November 30, 1950, and the issuance of the annual report to stockholders, the company has revised its procedure with respect to accounting for rentals on leased machines. Heretofore, the full amount of such rentals was recorded as receivable at the time of execution of the leases, with a corresponding credit to deferred income which was transferred to profit and loss over a period of five years, the estimated life of the machines. Under the revised procedure, rentals are recorded only as they become due for payment and are credited initially to deferred income, thereafter being transferred to profit and loss as earned over the life of the machines. This change in policy has been given effect in the accompanying balance sheet with the result that $7,385,000 has been eliminated from asset classifications and from deferred income; the balance of deferred income as stated under the revised procedure represents that portion of rentals received or now due, not yet transferred to profit and loss. Of the aggregate amount of unrecorded rentals yet to be received under the terms of existing machine lease agreements $7,385,000, approximately §2,600,000 is scheduled for payment within the ensuing year.

Failure to disclose history of the enterprise, its principal promoter, and the denial of a patent application under which an allegedly valuable license was granted registrant. -- An Ohio company organized in the latter part of 1949 filed a registration statement in June 1950 covering a proposed public offering of 30,000 shares of its Class A stock at

$100 per share. The registrant indicated that it was formed for the purpose of manufacturing, selling, leasing, and operating apparatus to be used particularly in connection with steel refining and in production of steel ingots for mills in the district in which its plant might be established. An exhibit in the registration statement set forth that for each Class A share sold to the public, a share of Class B stock would be given to another Ohio corporation in consideration of the latter's grant to the former of an exclusive license to manufacture, sell, lease and operate equipment developed by it, but such information was omitted from the prospectus. Both classes of stock had equal voting rights. Investigation by the staff developed that the Ohio corporation which granted the license to the registrant had only one patent and that it related to an emulsion process of no apparent commercial value which would expire in about three years. It was also ascertained that the principal promoter had filed a patent application covering a combustion chamber or "unit" employing a special fuel which was to be used in various furnace applications such as the steel open hearth. Apparently this patent was to be transferred to the corporate holder of the Class B stock which was to grant registrant a license thereon. The registration statement failed to disclose either the facts regarding its emulsion process or that the claims in the patent application relating to the "combustion chamber" it proposed to manufacture had been disallowed in full by the United States Patent Office. In addition the prospectus failed to disclose that the Ohio corporation which purported to grant licenses was under the control of the registrant's principal promoter. Furthermore the prospectus omitted to state that it appeared from an examination of the latter's books by the Ohio authorities that $60,000 of its funds had been transferred to the principal promoter of the registrant and was unaccounted for. The registration statement also failed to state that the principal promoter had been indicted in 1948 for violating the Ohio Securities Act in the sale of promissory notes, that he had been a fugitive from justice during 1949 and that he was awaiting trial after having been released on bail. After the registrant had become aware that the investigation had been instituted it withdrew its registration statement in July 1950.

Failure to make material disclosures including the possible effect on enterprise of the Defense Production Act of 1950 and the mobilization of the national economy. -- A company in the electronics field recently discharged in bankruptcy proceedings pursuant to Chapter XI of the National Bankruptcy Act filed a registration statement covering 4.00,000 shares of convertible Class A stock to be offered to the public at $2.50 per share. The prospectus failed to disclose adequately that one of the principal purposes of the offering was to repay a substantial loan made to the registrant by a principal and possibly controlling stockholder. In addition, the prospectus failed to set forth adequately the use which would be made of the proceeds in the event that a smaller amount than 400,000 shares was sold and to indicate the position in which purchasers of the shares might find themselves in such event. The prospectus also failed to disclose clearly that the cost of financing would represent at least thirty-one percent of the gross proceeds if all the shares were sold. Moreover, the registrant ailed to indicate its relatively poor competitive position and failed to point out the effect of the mobilization of the national economy and the impact of the Defense Production Act of 1950 upon its ability to obtain

materials and components needed for the manufacture of its proposed product. Finally, the registrant omitted to set forth a substantial contingent liability to the United States Government and to make adequate provision therefor in the balance sheet. After these failures in disclosure were directed to the registrant's attention, it withdrew its registration statement.

CHANGES IN RULES, REGULATIONS AND FORMS

Rules 171, X-6, and U-105 -- Disclosure detrimental to the national security. -- The Commission adopted during the past year rules providing for the omission or confidential treatment of information, if publication of the information would, in the opinion of the Commission, acting in consultation with other executive departments or agencies of the United States, be detrimental to the national security. [Footnote: Securities Act release no. 3409] Such rules are applicable to all filings under the Securities Act of 1933, the Securities Exchange Act of 1934, and the Public Utility Holding Company Act of 1935.

Procedure has been established whereby the Commission, upon request, will render advance, informal opinions in cases where issuers, underwriters, or other persons are in doubt as to the extent to which, or the manner in which, particular information may be disclosed in a registration statement, prospectus, application for registration, report, proxy statement, notification, or other document filed with the Commission or an exchange pursuant to any of those Acts.

The general types of information which will be treated confidentially under the new rules are as follows:

(1) The number, size, character, and location of ships in construction, or advance information as to the date of launchings or commissionings; or the physical set-up or technical details of shipyards.

(2) Specific information about war contracts, such as the exact type of production, production schedules, dates of delivery, or progress of production; estimated supplies of strategic and critical material available; or nationwide "round-ups" of locally published procurement data except when such composite information is officially approved for publication.

(3) Specific information about the location of, or other information about, sites and factories already in existence, which would aid saboteurs in gaining access to them; information other than that readily gained through observation by the general public disclosing the location of sites and factories yet to be established, or the nature of their production.

(4) Any information about new or secret military designs, or new factory designs for war production.

(5) Any information of a classified nature dealing with any atomic project, construction or product.

Amendment of Rules 220 and 222 of Regulation A. -- On September 8, 1950, the Commission invited comments on proposed amendments to rules 220 and 222, which are a part of Regulation A under the Securities Act of 1933. After considering the comments received the Commission amended those rules, effective January 8, 1951, to provide a new method for determining public offering price in connection with certain offerings through rights and warrants under Regulation A. [Footnote: Securities Act release no. 3399.]

In the past there has been some difficulty in determining in advance how the price limitations of Regulation A apply to certain rights offerings by issuers, which may be accompanied by sales of the rights and of the offered securities made at varied prices by underwriters and controlling persons. In order to minimize these difficulties, the Commission added a new paragraph (i) to rule 220. This paragraph provides generally that, for the purposes of Regulation A, the offering price of securities offered through rights or warrants shall be either (1) their market value as determined prior to the filing of the letter of notification or (2) the price to be received by the offeror, whichever is higher, and that no separate consideration shall be given to any sale of the rights or warrants by any person. In addition, rule 222 is amended to provide that the letter of notification filed in such cases shall state the market value, as well as the take-down price, of the securities.

Where additional shares of an outstanding class are to be offered through rights, it will normally be appropriate for the person preparing the letter of notification simply to set forth the current market value of the outstanding shares of the class to be offered. However, if it can be demonstrated that the offering will result in a dilution of the value of the outstanding shares, it will be permissible for the person filing the letter of notification to compute the dilution and to base the computation of market value of the offered securities on the diluted value.

Where the market value of securities to be offered through rights or warrants cannot be determined prior to the offering, the new provisions that have been added to the rule will not be applicable. In such cases, the application of the price limitations of paragraphs (a), (b), and (d) will turn on the take-down price, the amount received by controlling persons who sell their rights, and, if there are any underwriters, any amounts received from the public by such underwriters.

Amendment to Rule 240 of Regulation A-M. -- During the year the Commission also adopted certain amendments to rule 240 under Regulation A-M. [Footnote: Securities Act

release no. 3384.] That regulation exempts certain offerings of assessable mining securities from registration under the Act. The amendments, by deletion of paragraph (c) of the rule, removed the restriction which prevented issuers from commencing more than one offering under the regulation each year; and, by revision of paragraph (f), require the reporting to the Commission of assessments received by an issuer. However, the regulation as amended continues to limit the aggregate of unregistered offerings and assessments received to not more than $100,000 in each yearly period.

Proposed revision of Form S-l designed to shorten and improve prospectus. -- The Commission had under consideration at the end of the year a proposed revision of Form S-l, which is one of the forms for registration of securities under the Securities Act of 1933. The purpose of this revision is mainly to shorten and improve the prospectus and thereby facilitate its distribution and make it more useful to investors. Notice of the proposal was published in detail and the Commission also invited comments and suggestions from all interested persons. [Footnote: Securities Act release no. 3406.] Some of the items of information currently required to be shown in the prospectus would be omitted from the prospectus under this proposal but would be otherwise filed with the registration statement. For example, the prospectus would include very limited information as to the nature of the underwriting commitment. Details of the underwriting arrangements would be omitted from the prospectus but would be otherwise filed as a part of the registration statement. Certain other items of information would be similarly treated. The Commission's experience has been that, to a considerable extent, detailed items and instructions result in unnecessarily detailed answers in the prospectus. Accordingly, the revised items and instructions of the proposed form have been somewhat streamlined for the purpose of producing more concise statements in the prospectus without sacrificing essential information. A revised form was adopted after the end of the fiscal year.

LITIGATION UNDER THE SECURITIES ACT

It is sometimes necessary to obtain compliance with the Securities Act by resort to the courts. Where continued violation of the Act and consequent damage to the public is threatened, the Commission acts promptly to safeguard the public interest by instituting injunctions.

Several of the actions in which the Commission has obtained injunctions during the last fiscal year involved the sale of mining securities. In *SEC v. Francis D. Graves and Earl E. Brown* [Civil Action No. 548, E. D. Wash.], the defendants were enjoined from further violations of the registration and fraud provisions of the Act in the sale of undivided participating interests in two mining leases, one of which they did not own. The Commission's complaint alleged that they had told investors, among other things, that samples taken from the properties contained monazite, thorium, gold and other minerals in commercial quantities when no sampling had been conducted, that monazite would be

produced in the near future when they had made no arrangements to exploit the properties, and that they had invested $30,000 in the enterprise when their total investment was approximately $1,500. *SEC v. Carl I. Addison and Joe W. Black* [Civil Action No. 1251, E. D. Tex.] is another action in which the Commission obtained an injunction against further violations of the registration and fraud provisions of the Act in the sale of mining securities. This case involved the sale of stock in a Canadian company organized for the purpose of producing uranium ore. *SEC v. Marvin C. Meddock* [Civil Action No. 913, E. D. Wash.], *SEC v. Yankee Mines Inc. et al.* [Civil Action No. 2755, D. Idaho.], and *SEC v. Alhambra Gold Mines Corporation* [Civil Action No. 11820, S. D. Calif.] are other cases in which sales of securities of mining companies in violation of the Act were enjoined. The Meddock case involved violation of the fraud provisions; the last two cases charged violation of the registration provisions.

A number of the cases in which the Commission successfully sought injunctions against violations of the Act involved the sale of securities in oil and gas companies. In *SEC v. Penner Oil and Gas, Inc., et al.* [Civil Action No. 2841, N. D. Okla.], a permanent injunction was entered against all defendants. Criminal proceedings were also brought in connection with this promotion, which involved a widespread solicitation by mail campaign. A description of the fraud involved is contained elsewhere in this report. [Footnote: See discussion of U. S. v. S. E. J. Cox et al., infra.] In *SEC v. Gold Creek Mining Company* [Civil Action No. 1888. D. Utah.] the company and two individual defendants consented to the entry of an injunction against further violations by them of the fraud and registration provisions of the Act in the sale of various types of securities in oil properties located in Oklahoma. Among the misrepresentations alleged to have been made in the sale of the securities were statements that the proceeds of the sales of stock would accrue to the company when in fact the shares being offered were personally-owned shares of one of the individual defendants and the proceeds from the sales were largely used by him, and that the company's leases were surrounded by producing oil wells when in fact most of the surrounding wells had been abandoned.

Injunctions were also obtained during the last fiscal year in the following cases which involved the sale of securities in oil and gas companies or interests in oil and gas leases: *SEC v. Western Osage Oil Company* [Civil Action No. 12986, S. D. Calif.], *SEC v. Avonwold Oil Corporation* [Civil Action No. 67-191, S. D. N. Y.], *SEC v. William R. Justice and Adrian J. Belisle* [Civil Action No. 71-50, D. Neb.], and *SEC v. Western Oil Fields, Inc., et al.* [Civil Action No. 3463, D. Colorado.] The first three cases charged violation of the registration provisions; the last violation of the fraud provisions. Violations of the registration provisions were also charged in *SEC v. Sierra Nevada Oil Company* [Civil Action No. 13056, S. D. Calif.]. In that case, after the court had orally announced that it was prepared to issue a preliminary injunction, a voluntary petition under Chapter X of the Bankruptcy Act was filed by the defendant corporation in another jurisdiction and defendants argued that the stay of proceedings in the order approving the petition prohibited entry of an injunction order. After the close of the fiscal year, the Chapter X court, on motion of the Commission, clarified its order, and a preliminary

injunction was thereafter entered. A complaint filed against *Spearow Company Inc., et al.* [Civil Action No. 6070, D. Oregon.] charging noncompliance with the Act's registration provisions is still pending.

During the year, the Commission obtained injunctions against further violations of the Act in many cases involving sales of securities of other types of businesses. One such case was *SEC v. Co-op Insurance Company et al.* [Civil Action No. 1496, D. Ariz.], where the Commission charged, inter alia, that the defendants had obtained an option to purchase certain of the stock of the insurance company at $1.00 per share and had then proceeded to make a public offering of these securities at successively higher prices of $2.50, $3.50, and $5.00 per share without disclosing to purchasers the fact of the option agreement or that the price at which the stock was being sold had been arbitrarily established by the defendants.

In *SEC v. Patrick F. Cusick, First Guardian Securities Corporation and Leonard S. Baum* [Civil Action No. 59-354, S. D. N. Y.] it was alleged that First Guardian, a registered broker-dealer, acting through Vice President Baum, bought for resale a substantial amount of Mr. Cusick's personally owned shares of Standard Brewing stock and thereafter offered the stock to the public. No registration statement with respect to the Standard Brewing shares was in effect with the Commission. After obtaining a temporary restraining order, the Commission discovered evidence which indicated additional violations of its Acts by First Guardian and instituted action to revoke its registration as a broker-dealer. Inasmuch as First Guardian consented to the revocation of its license and proceeded to liquidate, the Commission subsequently agreed to-a dismissal of the injunction action.

The defendant in *SEC v. Robert J. Cottle* [Civil Action No. 913, E. D. Wash.] consented to the entry of a permanent injunction against further violations of the fraud provisions of the Act. The Commission alleged that Cottle sold securities by falsely representing, among other things, that he was a member of the New York and Boston Stock Exchanges, that he was operating a successful trading account with a large brokerage firm in Boston, that he was earning and paying large profits to investors, and that a prominent Boston banker was associated with him in connection with such account. Actually Cottle was using the money received from investors to bet on horse and dog races and for other personal purposes. Later he was convicted and sentenced to a term of three years for violations of the Act and the Mail Fraud Statute.

In *SEC v. Mercer Hicks Corporation* [Civil Action No. 5896, S. D. N. Y.] the defendants consented to the entry of a permanent injunction against further violations by them of the fraud provisions of the Act on the basis of a complaint filed against them during the previous fiscal year. While this action was pending, proceedings were instituted which concluded in the revocation of the broker-dealer registration of the corporation.

An injunction against violation of the registration and fraud provisions of the Act was obtained in SEC v. Northwest Acceptance Corporation and .Robert M. Hawley [Civil Action No. 2774, W. D. Wash.]. The alleged representations included a statement that the company had substantial earnings when, in fact, severe losses had been suffered and the company showed a net loss for the year ending September 30, 1950. It was also alleged that defendants stressed the company's past dividend record without disclosing that a dividend paid during the promotion was, in fact, a return of capital and that they assured investors that the company would repurchase the stock at any time without loss to them when, in fact, such repurchase would impair the corporation's capital in violation of the law of the State of Washington where it was incorporated.

In *SEC v. Atlas Tack Corporation* [Civil Action No. 50-143, D. Mass.] an injunction was entered directing the defendant, its officers and directors to file reports as required by the statute and to correct the deficiencies contained in the reports which had been filed.

In *SEC v. Evergreen Memorial Park Association et al.* [Civil Action No. 1821, E. D.], the Commission's original complaint charged defendants with selling unregistered securities in the nature of "investment contracts" in violation of Section 5 of the Securities Act of 1933. After the close of the fiscal year, the Commission sought leave to amend the complaint in order to charge, in addition, violations of the antifraud provisions of Section 17 (a). The "investment contracts" allegedly involved sales of cemetery lots in wholesale quantities coupled with representations and agreements that investors would obtain large profits within stated periods from the resale of these lots at retail, that the defendant vendors would improve the cemetery as a whole and also lots of particular investors to facilitate their resalability, and that said defendants would resell the lots for investors within stated periods at specified profits.

The Commission participated as *amicus curiae* during the past fiscal year in only one case involving the proper interpretation of the Securities Act of 1933. In *Crummer v. Crumley* [D. Nev., Civil Action No. 900.] the plaintiff instituted an action under sections 12 (1), 12 (2) and 17 (a), charging that defendants sold him unregistered stock in violation of the Act, and that he had been induced to buy this stock by fraudulent misrepresentations and statements of half-truths. In January 1951, the court denied a motion of defendants to dismiss the complaint with respect to the section 12 (1) cause of action and reserved judgment on the motion with respect to the remaining causes of action. Subsequently, the Commission filed a brief as *amicus curiae* expressing the following views: (1) that jurisdiction of the section 12 (2) cause of action was not dependent upon a showing, as defendants contended, that the alleged misrepresentations and half-truths were communicated by use of the mails or instruments of interstate commerce, but that it would suffice if either the mails or interstate facilities were used in the sale of the stock; and (2) that the federal jurisdictional requirements of sections 12 (2) and 17 (a) would be satisfied if it were shown, as plaintiffs alleged, that the mails were used to effect collection of plaintiff's check in partial payment for the stock, to demand completion of the purchase agreement, and to deliver the stock. The Commission

expressed the opinion that it was unnecessary for the court to decide whether plaintiff could also base his private action on the alleged violation of section 17 (a), since it believed that any wrong which plaintiff suffered could be redressed under section 12. The case was pending at the close of the fiscal year.

PART II
ADMINISTRATION OF THE SECURITIES EXCHANGE ACT OF 1934

The Securities Exchange Act of 1934 is designed to insure the maintenance of fair and honest markets in securities transactions both on the organized exchanges and in the over-the-counter markets, which together constitute the Nation's facilities for trading in securities.

Accordingly the Act provides in general for the regulation and control of transactions in such markets and of practices and matters related thereto, including solicitations of proxies of stockholders and transactions by officers, directors, and principal stockholders. It requires specifically that information as to the condition of corporations whose securities are listed on any national securities exchange shall be made available to the public; and provides for the registration of such securities, such exchanges, brokers and dealers in securities, and associations of brokers and dealers. It also regulates the use of the Nation's credit in securities trading. While the authority to issue rules on such credit use is lodged in the Board of Governors of the Federal Reserve System, the administration of these rules and of the other provisions of the Act is vested in the Commission.

REGULATION OF EXCHANGES AND EXCHANGE TRADING

Registration and Exemption of Exchanges

Section 5 of the Act requires each securities exchange within the United States or subject to its jurisdiction to register with the Commission as a national securities exchange or to apply for exemption from such registration. Exemption from registration may be granted to an exchange which has such a limited volume of transactions effected thereon that, in the opinion of the Commission, it is not practicable and not necessary or appropriate in the public interest or for the protection of investors to require its registration. During the fiscal year no change occurred in the number of exchanges registered as national securities exchanges or in the number granted exemption from such registration.

At the close of the 1951 fiscal year the following 16 exchanges were registered as national securities exchanges:

Boston Stock Exchange

Chicago Board of Trade

Cincinnati Stock Exchange

Detroit Stock Exchange

Los Angeles Stock Exchange

Midwest Stock Exchange

New Orleans Stock Exchange

New York Curb Exchange

New York Stock Exchange

Philadelphia-Baltimore Stock Exchange

Pittsburgh Stock Exchange

Salt Lake Stock Exchange

San Francisco Mining Exchange

San Francisco Stock Exchange

Spokane Stock Exchange

Washington Stock Exchange

Four exchanges were exempted from registration at the close of the 1951 fiscal year. These were:

Colorado Springs Stock Exchange

Honolulu Stock Exchange

Richmond Stock Exchange

Wheeling Stock Exchange

Information pertinent to the organization, rules of procedure, trading practices, membership requirements and related matters of each exchange is contained in its registration or exemption statement, and any changes which are effected in such information are required to be reported promptly by the exchanges. During the year numerous changes in their rules and trading practices were reported by the various exchanges, each of which was reviewed to ascertain whether the change effected was in the public interest and complied with the provisions of the Act. The nature of these changes varied considerably; some of the more significant which occurred are briefly outlined below:

Boston Stock Exchange amended its rules relating to commissions for the purpose of making it clear that the rates of commission prescribed by the Constitution of the exchange are minimum rates and that, so far as the Constitution and rules of the exchange are concerned, members are free to charge greater commissions if the conditions and circumstances warrant, provided that if the commission being charged exceeds the minimum rate, that fact must be disclosed in writing to the customer.

Cincinnati Stock Exchange amended its rules to prohibit the selling of a lot of stock (all or none) at a lower price than the best bid on the Exchange, which may be for a smaller lot. Likewise the amendment also prohibits the purchase of a larger lot of stock at a higher price without taking small lots offered at lower prices. The revised rule does not, however, prevent a buyer or seller from going around smaller lots at the same price but having precedence as to the time the order was received.

San Francisco Mining Exchange increased its schedule of commission rates on stocks selling up to 29 cents per share.

San Francisco Stock Exchange adopted a rule which provides that when a member firm holds securities for customers which have been fully paid for, or holds securities for customers the market value of which is in excess of the amount required under the Exchange's margin maintenance rules, such securities are to be segregated and marked in such a manner as to clearly identify the owners of such securities.

Disciplinary Actions by Exchanges against Members

Each national securities exchange, pursuant to a request of the Commission, reports to the Commission any action of a disciplinary nature taken by it against any of its members, or against any partner or employee of a member, for violation of the Securities Exchange Act of 1934, of any rule or regulation thereunder, or of any exchange rule. During the year four exchanges reported taking disciplinary action against 16 members, member firms, and partners and employees of member firms.

The nature of the actions reported included fines ranging from $100 to $5,000 in 8 cases with total fines aggregating $8,850; suspension of an individual member from exchange

membership for a period of three months; censure of individuals or firms for infractions of the rules, and warnings against further violations. The disciplinary actions resulted from violations of exchange rules, principally those pertaining to handling of customers' accounts, capital requirements, floor trading, commission rates, and conduct inconsistent with just and equitable principles of trade.

REGISTRATION OF SECURITIES ON EXCHANGES

Nature and Purpose of Registration

An issuer may register a security on a national securities exchange by filing with the Commission and the exchange an application for registration which sets forth on a prescribed form reliable and comprehensive information about the affairs of the issuer and its securities which is available for public inspection. The law also requires the registrant to file annual, quarterly, and other periodic reports in order to keep this information up to date. The statute makes it unlawful to trade in a security on the exchange unless it is so registered (except where it has been admitted to unlisted trading privileges, or is exempt).

Examination of Applications and Reports

The work of examining applications and reports filed under the Securities Exchange Act is integrated with the examination work arising under the Securities Act and certain other statutes administered by the Commission. All applications and reports are examined to determine whether accurate and adequate disclosure has been made of the specific types of information required by the Act and the rules and regulations promulgated thereunder. Where such disclosure has not been made, necessary correcting amendments are obtained from the registrant. The result of this examination work may be illustrated by a description of a few actual cases arising during the 1951 fiscal year.

Loss from currency devaluation charged to profit and loss instead of surplus. -- The annual report required of a company with wide foreign operations must include financial statements not only with respect to the registrant separately and the registrant and its domestic subsidiaries combined but also with respect to the foreign subsidiaries of such company. During the 1951 fiscal year the staff noted from the annual report filed by one such registrant -- a large manufacturer of specialized machinery -- that a charge had been made to surplus of $4,911,325.31 in the combined statements of its foreign subsidiaries as a result of devaluation of foreign currencies and of the translation of working capital and reserves of foreign subsidiaries into United States dollars at current exchange rates.

The Division of Corporation Finance took the position that this amount represented the loss from the devaluation of foreign currencies during the year and should be reflected in the profit and loss statement. The Division also called the attention of this company to the

reports to stockholders which had been published by other large corporations with substantial foreign activities and which had applied the method of accounting for such loss suggested by the staff in this instance. The combined profit and loss statement of foreign subsidiaries was thereupon amended, changing the final credit figure of $3,126,335.98 net income to a final debit figure of $1,784,989.33 which was, pursuant to the Commission's recently amended Regulation S-X, captioned "Net income less Special charge (net charge)."

Losses of subsidiaries and adjustments of depreciation transferred from surplus to income statement. -- At the beginning of its 1949 fiscal year a registrant, engaged in the manufacture of aircraft parts, owned 71 percent of the voting stock of one subsidiary, and 100 percent of the common stock along with approximately 61.5 percent of the preferred stock (which had voting rights) of another subsidiary. Through the year 1948 its consolidated financial statements had included these companies. A merger agreement between the two subsidiaries subsequently became effective in the latter part of 1949 and under its terms the registrant early in 1950 received 75,000 shares of new second preferred stock of the surviving company for its investment in the two companies. The surviving company ceased to be a subsidiary as a result of the exchange of stock.

The investment in the new preferred stock was thereafter in the registrant's annual report shown in the balance sheet at the cost of the investments surrendered in exchange therefor, and the sum of $1,400,000 was provided from earned surplus as a reserve for the revaluation of the new stock to approximately its par value. The financial statements also reflected adjustments of accumulated depreciation for prior years (less applicable additional income taxes) as a credit to earned surplus in the amount of $62,346.78. For 1949 the merged subsidiaries sustained losses of $741,164.61 and of $230,394.88, respectively, or a combined loss of the two companies (consolidated with the parent in the previous year) of $971,559.49, no portion of which was reflected in the statement of income of the parent. However, the above-mentioned reserve against the combined investment created by a charge to earned surplus appeared to reflect the management's opinion as to the loss in the investment.

It was the opinion of the staff that in this situation the losses sustained by the subsidiary companies, to the extent of the registrant's equity therein, were an incident of the year 1949, and that the losses as well as the adjustment relating to depreciation should be reflected in the statement of income. The statement of income as it was subsequently amended to reflect these views showed a loss of $589,560.76 for 1949 as compared to the statement as originally filed which showed a net income of $428,199.91.

Change made in method of computing depletion. -- For many years, including the year 1949, a large copper mining company had followed the practice of computing unit depletion of metal mines at separate rates per pound of copper from individual properties, charging such depletion direct to surplus. The following note was appended to the statement of surplus: ". . . The unit rates used are based on the mine values included in

the balance sheets . . . and the ore reserves of the respective mines as estimated as of March 1, 1913, or at the date of acquisition, or in the case of a subsidiary company at a subsequent date . . . Part of the depletion charge is based on United States Treasury Department valuations as of March 1, 1913, determined for depletion purposes in connection with Federal income taxes." The reason given in a note and in the certificate of the independent certified public accountants for using this method of treatment of depletion read: "While it is recognized that charges made for the amortization of cost of fixed assets are generally shown as deductions in profit and loss statements, the difficulty of determining the extent of ore reserves and of allocating the depletion charges between cost and appreciation, the variance in the amount of the charge during the different periods depending upon the particular properties operated, and other uncertainties and variables, have caused the registrant to follow consistently the practice above mentioned. . . ."

Inasmuch as some years had passed and distinct progress had been made in the method of preparing financial statements since this matter was first discussed with the registrant, a suggestion was made by the staff during the 1951 fiscal year that the problem be reexamined. Accordingly in February 1951 representatives of the registrant and its independent certified public accountants met with members of the staff and reviewed the question of accounting for depletion and other matters in order to secure an over-all improvement in the presentation of the company's financial statements for the benefit of investors. As a result of these co-operative prefiling discussions, in its annual report for the year 1950, filed on April 27, 1951, the registrant changed its practice with respect to depletion so that the deduction was computed on the basis of an over-all unit rate applied to the pounds of copper sold from the registrant's own production except that depletion of a consolidated subsidiary was computed separately as heretofore. The over-all rate is deemed by the company to be sufficient in amount to provide for the amortization of the net book value of mines on or before the exhaustion of the mines. The charge for depletion of mines as thus calculated was shown as a deduction in the profit and loss statement for the year 1950. The company added this note to its 1950 financial statements: "The registrant makes no representation that the deduction represents the depletion actually sustained or the decline, if any, in mine values attributable to the year's operations (which amounts are not susceptible of determination), or that it represents anything other than a general provision for the amortization of the remaining book value of mines. Depletion used in estimating United States taxes on income has been computed on a statutory basis and differs from the amount shown in these accounts." The accountants made appropriate reference in their certificate to the change in procedure and hereafter will be able to omit a cumbersome explanation from the company's financial accounts.

Statistics of Securities Registered on Exchanges

At the close of the 1951 fiscal year, 2,188 issuers had 3,523 security issues listed and registered on national securities exchanges. These securities consisted of 2,581 stock

issues aggregating 3,477,564,645 shares, and 942 bond issues aggregating $20,896,324,569 in principal amount. This represents an increase of 329,880,327 shares and a decrease of $2,394,222 principal amount of bonds, respectively, over the aggregate amounts listed and registered at the close of the 1950 fiscal year.

The following table shows the number of applications and reports filed during the fiscal year in connection with the registration of securities on national securities exchanges:

Applications for registration of securities on national securities exchanges: 559

Applications for registration of unissued securities for "when issued" trading on national securities exchanges: 83

Exemption statements for trading subscription rights on national securities exchanges: 88

Annual reports: 2,148

Current reports: 8, 792

Amendments to applications, annual and current reports: 1,139

During the fiscal year ended June 30, 1951, 58 new issuers registered securities on national securities exchanges, and the registration of all securities of 52 issuers was terminated, principally by reason of retirement and redemption and through mergers and consolidations.

The annual and current reports listed above are in addition to the corresponding reports filed under section 15 (d) of the Securities Exchange Act pursuant to undertakings contained in registration statements, reported in the preceding chapter. The total of both classes of such reports is 2,883 annual reports and 11,788 current reports.

Temporary Exemption of Substituted or Additional Securities

Rule X-12A-5 provides a temporary exemption from the registration requirements of section 12 (a) of the Act for securities issued in substitution for, or in addition to, securities previously listed or admitted to unlisted trading privileges on a national securities exchange. The purpose of this exemption is to enable transactions to be lawfully effected on an exchange in such substituted or additional securities pending their registration or admission to unlisted trading privileges on an exchange.

The exchanges filed notifications of admission to trading under this rule with respect to 165 issues during the year. In some instances, the same issue was admitted to trading on more than one exchange, so that the total admissions to such trading, including duplications, numbered 317.

Formal Action Under Section 19 (a) (2)

In case any issuer of a security listed and registered on an exchange fails to comply with any provision of the Act or the rules and regulations, the Commission is empowered under section 19 (a) (2) to institute formal proceedings looking to the termination of such registration. Specifically, the Commission may, after giving appropriate notice and opportunity for hearing, deny, suspend the effective date of, suspend for a period of not exceeding 12 months, or withdraw, the registration of such security.

Pursuant to this authority during the 1951 fiscal year the Commission after a public hearing ordered withdrawn from registration on the San Francisco Mining Exchange the common stock of New Sutherland Divide Mining Company. This company had failed to file its annual report for 1949, the exchange had consequently suspended trading in the stock of the company, and officers of the company had stated to representatives of the Commission that the company had no assets or funds with which to file such report or with which to file a petition in bankruptcy or effect dissolution of the company.

MARKET VALUE OF SECURITIES TRADED ON EXCHANGES

The unduplicated total market value on December 31, 1950, of all securities admitted to trading on one or more of the twenty stock exchanges in the United States was $228,087,813,000 :

Stocks:

New York Stock Exchange: $93,807,269,000

New York Curb Exchange: $13,874,294,000

All other exchanges: $3,314,772,000

Total: $110, 996,335,000

Bonds:

New York Stock Exchange: $115,951,939,000

New York Curb Exchange: $957,839,000

All other exchanges: $181,700,000

Total: $117,091, 478,000

Total stocks and bonds: $228,087,813,000

New York Stock Exchange and Curb figures are as set forth by those exchanges. There is no duplication of issues between those two exchanges, but many of the issues traded on them are also admitted to trading on one or more of the eighteen other exchanges and are not included in the amounts shown above for such other exchanges only. The market value of bonds on New York Stock Exchange includes $96,899,382,000 of United States Government and subdivision issues.

SPECIAL OFFERINGS ON EXCHANGES

Rule X-10B-2 under the Securities Exchange Act permits special offerings of large blocks of securities to be made on a national securities exchange provided such offerings are effected pursuant to a plan which has been filed with and approved by the Commission. A security may be the subject of a special offering when it has been determined that the auction market on the floor of the exchange cannot absorb a particular block within a reasonable period of time without unduly disturbing the current price of the security. A special offering of a security is made at a fixed price consistent with the existing auction market price of the security, and members acting as brokers for public buyers are paid a special commission by the seller which ordinarily exceeds the regular brokerage commission. Buyers of the security are not charged any commission on their purchases and obtain the security at the net price of the offering.

Since February 6, 1942, the date on which rule X-10B-2 was amended to permit special offerings, the Commission has declared effective special offering plans of the following nine exchanges on the date shown opposite each:

New York Stock Exchange -- Feb. 14, 1942

San Francisco Stock Exchange -- Apr. 17, 1942

New York Curb Exchange -- May 15, 1942

Philadelphia-Baltimore Stock Exchange -- Sept. 23, 1943

Detroit Stock Exchange -- Nov. 18, 1943

Midwest Stock Exchange -- Mar. 27, 1944

Cincinnati Stock Exchange -- June 26, 1944

Los Angeles Stock Exchange -- May 28, 1948

Boston Stock Exchange -- Sept. 15, 1948

On June 30, 1951, the Commission declared effective for an indefinite period of time the amended special offering plans of the Midwest Stock Exchange, New York Curb Exchange, New-York Stock Exchange, and San Francisco Stock Exchange. These are the same special offering plans which the Commission previously declared effective for an experimental period expiring on June 30, 1951. These amended special offering plans were discussed in last year's annual report. [Footnote: See 16th SEC Annual Report 29-30. The amended special offering plans of the New York Stock Exchange, New York Curb Exchange and San Francisco Stock Exchange were initially declared effective for an experimental period on August 24, August 25 and November 7, 1949, respectively; similar action was taken on November 1, 1950, with respect to the amended plan filed by the Midwest Stock Exchange. The experimental period for all four exchanges was subsequently extended. See Securities Exchange Act releases nos. 4299, 4309, 4343, 4410, 443T, 4457, 4510, 4535, and 4622.]

Each exchange with a special offering plan in effect has been requested to report certain information to the Commission on each offering effected on the exchange under the plan. Such reports showed a total of 19 offerings effected on the Midwest Stock Exchange, New York Stock Exchange and San Francisco Stock Exchange during the fiscal year ended June 30, 1951. These offerings involved the sale of 160,384 shares of stock with an aggregate market value of $5,073,000 and ranging in market value from $41,200 to $1,601,200. Special commissions paid to brokers participating in these 19 offerings totaled $99,000. By comparison, in the preceding fiscal year a total of 29 offerings involving 430,955 shares of stock having a market value of $11,129,000 were effected on two exchanges with special commissions paid to brokers totaling $266,000.

During the period February 19, 1942, through June 30, 1951, a total of 454 offerings have been effected. These offerings totaled 5,507,239 shares with a market value of $160,537,000 and brokers have been paid special commissions totaling $3,180,800.

SECONDARY DISTRIBUTIONS APPROVED BY EXCHANGES

A "secondary distribution," as the term is used in this section, is a distribution over the counter by a dealer or group of dealers of a comparatively large block of a previously issued and outstanding security listed or admitted to trading on an exchange. Such distributions take place when it has been determined that it would not be in the best interest of the various parties involved to sell the shares on the exchange in the regular way or by special offering. The distributions generally take place after the close of exchange trading. As in the case of special offerings, buyers obtain the security from the dealer at the net price of the offering, which usually is at or below the most recent price registered on the exchange. It is generally the practice of exchanges to require members

to obtain the approval of the exchange before participating in such secondary distributions.

During the fiscal year ended June 30, 1951, 5 exchanges reported having approved a total of 80 secondary distributions under which 4,664,187 shares of stock with a market value of $128,017,000 were sold.

UNLISTED TRADING PRIVILEGES ON EXCHANGES

(chart omitted)

Clause 1 of section 12 (f) of the Securities Exchange Act of 1934 provides for continuance of unlisted trading privileges to which a security had been admitted on an exchange prior to March 1, 1934. Historically, admission of securities to trading on stock exchanges upon application of members -- the so-called "unlisted trading" on exchanges -- came first. Any member could have any security added to the roster. As the stock exchanges grew in importance and public interest in them increased, it became necessary to require reports and disclosures from the issuers along with various other actions for protection of the security holders, and it also became possible to charge issuers a fee for listing. Consequently, listing by agreement between the issuers and the exchanges, stipulating what data and actions were required of the issuers, gradually succeeded the process of adding issues to the trading roster upon members' requests. Thus, New York Stock Exchange abolished unlisted trading in 1910. Other leading exchanges such as Boston and Philadelphia continued to allow unlisted trading on their floors in issues listed on some other principal exchange, on the ground that listing on such other exchange afforded the necessary background of reports and actions by issuers. A few exchanges continued to extend unlisted trading privileges to issues not covered by listing agreements between issuers and any domestic stock exchange. New York Curb Exchange is the principal surviving representative of this group and continues to have most of the "clause 1" issues which have no domestic listed status. As anticipated by Congress, when it amended section 12 (f) on May 27, 1936, to provide for limited continuance of unlisted trading on exchanges, there has been a considerable shrinkage in number of "clause 1" issues over the years, as they became listed or were retired, refunded, exchanged for other issues, or otherwise disappeared from exchange trading.

Clause 2 of section 12 (f) provides for the extension of unlisted trading privileges to securities already listed on some other national securities exchange. Most of the trading privileges pursuant to this clause have been applied for and obtained with respect to stock issues by 8 leading regional stock exchanges. Most of the stocks involved are listed on New York Stock Exchange. The total reported volume in "clause 2" stocks during 1950 was about 13,000,000 shares, an important figure to the regional exchanges but equivalent to less than 2% of the share volume on New York Stock Exchange during that

year. Admissions of bond issues pursuant to clause 2 have been 8, of which only 2 are extant.

Clause 3 of section 12 (f) provides for the further extension of unlisted trading privileges to unlisted securities. In these cases, information substantially equivalent to that filed in respect of an issue listed on a national securities exchange must be available. Applications covering stocks have been approved by the Commission in 11 instances and with respect to 9 issues, 2 of which were admitted to trading on several exchanges. Only 4 stock issues continue their status under clause 3, and 2 of these have become listed on another exchange leaving only 2 with dependence for status on clause 3. Bond admissions have been 45, but all the issues except 13 have been retired or listed.

The unduplicated number of stock issues admitted to unlisted trading on the exchanges, and which are not listed on some national securities exchange as well, was 354 as of June 30, 1951, aggregating 342,084,643 shares or less than 9 percent of all shares on the 20 exchanges. Reported exchange volumes therein for the calendar year 1950 came to 34,310,513 shares or less than 4 percent of the total reported exchange volumes for that year. New York Curb Exchange alone accounted for 32,054,348 or 93.4 percent of the 34,310,513 share volume. In considering these figures, it should be recalled that reported ticker volume of New York Curb Exchange is less than 90 percent of the true total, and that volume of trading in stocks removed during the year is not included.

Bond issues admitted to unlisted trading on the exchanges have become reduced over the years to a very small number. As of June 30, 1951, there were 59 pursuant to clause 1, 2 pursuant to clause 2, and 13 pursuant to clause 3. All but 3 of the issues were on New York Curb Exchange. Of the total 74 issues, 6 were listed on another national securities exchange and 68 were not so listed.

Applications for Unlisted Trading Privileges

As a result of applications filed pursuant to clause 2 of section 12 (f) and approved by the Commission during the 1951 fiscal year, unlisted trading privileges were extended as follows:

Stock exchange applying:

Boston -- 18 stocks

Cincinnati -- 1 stock

Detroit -- 3 stocks

Los Angeles -- 23 stocks

Midwest -- 2 stocks

New Orleans -- 2 stocks

New York Curb -- 1 stock

Philadelphia-Baltimore -- 8 stocks

Pittsburgh -- 1 stock

San Francisco -- 8 stocks

Total -- 67

The actual number of issues involved is less than 67 since applications by different exchanges are often with respect to the same issue, resulting in duplication.

No applications were made or approved during the fiscal year for unlisted trading privileges in bond issues pursuant to clause 2, nor for unlisted trading privileges in either stock or bond issues pursuant to clause 3 of section 12 (f).

Changes in Securities Admitted to Unlisted Trading Privileges

The usual considerable number of notifications of minor changes in securities admitted to unlisted trading was received during the year from the stock exchanges pursuant to paragraph (a) of rule X-12F-2.

Applications for continuance of trading in unlisted issues after more important changes than those contemplated under paragraph (a) of rule X-12F-2 are made under paragraph (b) of that rule, and were limited during the last fiscal year to one by New York Curb Exchange in the case of Nippon Electric Power Company, Ltd., 6% percent bonds due 1953 which was withdrawn when the Curb obtained a listing of the bonds, and one by Boston Stock 'Exchange in the case of Chicago, Milwaukee, St. Paul & Pacific Railroad Company common stock which was withdrawn upon approval of unlisted trading in that issue pursuant to clause 2 of section 12 (f). Accordingly, no denials and no grants of applications pursuant to paragraph (b) of rule X-12F-2 were made during the last fiscal year. The Commission prefers that application for trading be made pursuant to clause 2 of section 12 (f) rather than paragraph (b) of rule X-12F-2 whenever this course is possible.

DELISTING OF SECURITIES FROM EXCHANGES

Securities Delisted by Application

The granting of applications filed by New York Stock Exchange pursuant to rule X-12D2-1 (b) resulted in the delisting of 3 bond and 2 stock issues from that exchange during the fiscal year. The applications covering the bonds and 1 of the stocks declared the amounts in public hands were no longer sufficient to warrant exchange trading [Footnote: Illinois Central R. R. Co., 4 percent Leased Line Stock, Securities Exchange Act release no. 4507 (1950). Adriatic Electric Co., 7 percent bonds due 1952, Securities Exchange Act release no. 4511 (1950). Illinois Central R. R. Co., sterling 3 percent bonds due 1951, Securities Exchange Act release no. 4554 (1951). Ernesto Breda Co., 7 percent bonds due 1954. Securities Exchange Act release no. 4554 (1951).], and the application covering the remaining stock was based on bankruptcy and termination of transfer facilities. [Footnote: Norwalk Tire & Rubber Co., common stock, Securities Exchange Act release no. 4496 (1950).]

The granting of applications filed by issuers pursuant to rule X-12D2-1 (b) resulted in the delisting of 9 stock issues of 6 issuers during the fiscal year. Inactivity on the exchange was given as a reason for delisting 4 stock issues of 3 issuers on the Chicago Board of Trade [Footnote: Knickerbocker Fund for the Diversification, Supervision and Safekeeping of Investments, shares of beneficial interest, Securities Exchange Act release no. 4496 (1950). Corn Products Refining Co., preferred and common, Securities Exchange Act release no. 4587 (1951). Allied Mills, Inc., common stock, Securities Exchange Act release no. 4595 (1951). Corn Products Refining Co. preferred and common and Allied Mills, Inc. common stock remain listed on New York Stock Exchange.] and 3 stock issues of an issuer on Cincinnati Stock Exchange. [Footnote: Carthage Mills Incorporated, Preferred "A", Preferred "B" and common stock, Securities Exchange Act release no. 4558 (1951).] Concentrated ownership was the basis of application with respect to an issue on Midwest Stock Exchange [Footnote: W. H. Barber Co., common stock, Securities Exchange Act release no. 4486 (1950).], and acceptance of an offer to exchange into stock of another company except for a small residue was the basis with respect to an issue on San Francisco Stock Exchange. [Footnote: Hale Bros. Stores, Inc., common stock, Securities Exchange Act release no. 4566 (1951).]

Securities Delisted by Certification

Securities which have been paid at maturity, redeemed, or retired in full, or which have become exchangeable for other securities in substitution therefor, may be removed from listing and registration on a national securities exchange if the exchange files a certification with the Commission to the effect that such retirement has occurred. The removal of the security becomes effective automatically after the interval of time prescribed by rule X-12D2-2 (a). The exchanges filed certifications under this rule effecting the removal of 183 separate issues. In some instances the same issue was removed from more than one exchange, so that the total number of removals, including duplications, was 226. Successor issues to those removed became listed and registered on exchanges in many cases.

In accordance with the provisions of rule X-12D2-1 (d), New York Curb Exchange removed 3 issues from listing and registration when they became listed and registered on New York Stock Exchange. This rule permits a national securities exchange to remove a security from listing and registration in the event trading therein has been terminated pursuant to a rule of the exchange which requires such termination if the security becomes listed and registered and admitted to trading on another exchange. Removal under this rule is automatic, the exchange being required merely to notify the Commission of the removal.

Securities Removed from Listing on Exempted Exchanges

A security may be removed from listing on an exempted exchange merely upon notification by such an exchange to the Commission setting forth the reasons for such removal. Honolulu Stock Exchange removed five issues from listing thereon during the year due in one case to the call of the security for redemption and in two cases due to the liquidation of the issuers. In the remaining two cases the securities became exchangeable for other securities which subsequently became listed on the same exchange.

MANIPULATION AND STABILIZATION

One of the evils which the Securities Exchange Act of 1934 was primarily designed to prevent is the manipulation of security markets by practices which are deceptive or otherwise improper. Sections 9, 10, and 15 of the Act prohibit certain specifically described forms of manipulative activity such as wash sales, if effected for the purpose of creating a false or misleading appearance of the market and matched orders, if entered for a like purpose; effecting a series of transactions in which the price of a security is raised or depressed, or in which, the appearance of active trading is created, for the purpose of inducing purchases and sales by others; circulation by a broker, dealer, seller or buyer, or by a person who receives a consideration from a broker, dealer, seller or buyer, of information concerning market operations conducted for a rise or a decline; and the making of material false and misleading statements by brokers, dealers, sellers and buyers, or the omission of material information regarding such securities, for the purpose of inducing purchases or sales.

Pursuant to its statutory authority, the Commission has adopted rules and regulations to aid it in carrying out the expressed will of Congress. Sections 9, 10, and 15 as augmented by the Commission's rules and regulations are aimed at freeing our securities markets from artificial influence and maintaining fair and honest markets, where prices are established by supply and demand and are uninfluenced by manipulative activity.

Manipulation

The manipulation of security prices in years prior to the enactment of the Securities Exchange Act took millions of dollars annually from the public and was one of the principal reasons for the adoption of the Act. In the early days of the Commission's existence, some market operators attempted to continue their manipulative activities. The Commission uncovered these activities and caused the imposition of various penalties upon certain operators, including expulsions from exchanges, revocation of broker-dealer registrations, fines and jail sentences.

As a result of the administration of the Act, manipulation has been reduced to a point where it is no longer an appreciable factor in our markets. However, sporadic attempts artificially to raise or depress the prices of securities are still encountered, and it is evident that any relaxation of market surveillance on the part of the Commission would create a danger of establishment of many of the manipulative practices the Act was designed to prevent.

The staff regularly scrutinizes price movements in approximately 8,200 securities, including about 3,600 issues traded on exchanges and about 4,600 of the most active over-the-counter issues. The volume of transactions of listed securities and the number of dealers making a market in over-the-counter issues are also closely observed. An observation is made on a daily basis of all listed securities as they appear in such publications as the Wall Street Journal and of over-the-counter issues as they appear in The National Daily Quotation Service. Complete records are kept on a weekly basis (with the exception of about 600 inactive issues which are kept on a monthly basis) of all of the above-mentioned securities. In addition unusual activity in stock transactions on the New York Stock Exchange and the New York Curb Exchange is observed from the ticker as soon as it occurs.

Information maintained concerning all these securities includes not only data reflecting the market action but also includes the latest news items, earnings figures, dividends, options and other facts which might explain price and volume changes. Trained analysts daily scan the Wall Street Journal, Standard and Poor's, Moody's and other financial publications and record any items that might be reflected in the market price of these securities. Reports required by the Securities Acts from corporations or their officers, directors and 10 percent stockholders and from registered broker-dealers are studied. Important information contained in these reports is recorded on the securities' weekly price and volume record. All possible known information regarding a security is maintained on a current basis. Dates of public releases of any news regarding a company are carefully recorded. At the inception of any unusual volume of trading or price fluctuations in a security, all this information is reexamined. The market action of the security is compared with the action of other securities in the same industry group and with the action of the general market and a conclusion drawn as to the necessity for an investigation.

The markets for securities about to be sold to the public are watched very closely. In this connection the markets for 1,370 issues in the amount of $173,209,739 offered under Regulation A, were carefully checked for improper pricing or market grooming. Over 500 other securities were kept under special daily observation during the 1951 fiscal year for periods from 10 to 90 days, largely because a public offering under a registration statement was proposed with the right to stabilize reserved by the underwriter or issuer. Issues actually offered during the fiscal year had a public offering price in excess of $3,380,000,000.

In administering the anti-manipulative provisions of the Act there is a premium on prompt action to prevent harm before it occurs, and at the same time to avoid interference with the legitimate functioning of the markets. To accomplish this the Commission has continuously modified and sought to improve its procedures for the systematic surveillance of trading in securities. Methods used to detect manipulation have necessarily been flexible, since techniques employed by manipulators change constantly, increasing in subtlety and complexity.

The Commission operates on the premise that manipulation should be, and in most cases can be, suppressed at its inception. Losses suffered by the public are seldom recoverable, even though the perpetrator of a fraud is brought to justice. Therefore, it is believed that it is more important to prevent a possible manipulation than to allow unlawful market operations to continue until it appears that sufficient evidence for a successful prosecution is available.

It has been found that many would-be violators of the regulations prohibiting manipulation have been halted by prompt inquiries by the Commission. The fact that trading in a given security is under investigation is kept confidential by the Commission, as public knowledge of the existence of such investigations may unduly affect the market or reflect unfairly upon individuals whose activities are being investigated. As a result, the Commission occasionally receives criticism for failure to investigate certain cases' when in fact it is actually engaged in an investigation. However, while the general public is unaware that an inquiry is being made, any person or group of persons conducting unusual market activity in a security will be made aware by questions asked either their brokers or themselves after the brokers have supplied the names of their principals. In this connection the Commission receives excellent cooperation from the stock exchanges and from brokers and dealers.

The Commission's surveillance of unusual market activity may take the form of a simple inquiry, addressed to an exchange or broker by our nearest Regional Office, asking for an explanation or the names of the buyers and sellers. This type of inquiry is used when the market activity is limited to a brief period during a day's trading or at most a single day's transactions. If the explanation is logical and devoid of manipulative features, no further investigation is made. If the explanation is considered unsatisfactory, an investigation is

initiated and conducted by our Regional Office located nearest the exchange or market on which the transactions were made.

Investigations take two forms. The "quiz" or preliminary investigation is designed to detect and discourage incipient manipulation by a prompt determination of the reasons for the unusual market behavior. Often the quiz discloses no violations of the anti-manipulative provisions of the Securities Acts. The quiz is then closed. If possible violations of other sections of the Securities Acts or violations of other statutes are revealed, the information obtained in the "quiz" is made available to the proper division of the Commission or to the appropriate agency for any action that they might consider necessary. When facts are uncovered which require more intensive investigation, formal orders are issued by the Commission. In a formal investigation, members of the Commission staff are empowered to subpoena pertinent material and to take testimony under oath. In the course of such investigations, data on purchases and sales over substantial periods of time are compiled and trading operations involving considerable quantities of securities are often scrutinized.

Stabilization

In administering those provisions of the Securities Exchange Act prohibiting manipulation of securities prices certain stabilizing transactions are permitted. Stabilizing is a word which is frequently misunderstood. The law prohibits injection of artificial activity into the market. One exception is stabilization. But stabilizing is permissible only when it is used to prevent or retard a price change, usually a decline. No moving around of the market under the label of stabilizing is permitted. Stabilization means maintenance of a price independently reached in the market.

Prudent regulation by this Commission has permitted the investment industry to change its methods with changing conditions and to achieve its primary function -- which is to supply industry with the capital it needs. For this purpose formal Commission rules dealing with stabilization relate only to offerings "at the market" or at prices related to a changing market price. The practice applicable to fixed price offerings is embodied in a wealth of interpretative material. It is the Commission's experience that issuers and underwriters place great value on the immediate service which the Commission is able to render them by being at all times available to give them responsible advice as to the proper stabilizing techniques in the offerings of securities. Also the same policy of the Commission extends to both manipulation and stabilization in that it seeks to prevent violations of the law rather than to allow them to develop to the point where monetary losses occur. The investor naturally wants to see a violator of the law brought to justice, but this does not insure the return of any financial loss that he may have suffered.

The law requires that all issuers or underwriters must file with the Commission a notice of intent to stabilize if an issue is to be stabilized. Thus the staff is able to observe and assist the registrant before and during an offering.

Of 554 registration statements filed during the fiscal year, 231 contained a statement of intention to stabilize to facilitate the offerings covered by such registration statements. Each of these latter filings was examined critically as to the propriety of the proposed method of distribution, market support and the full disclosure thereof.

Stabilizing operations were conducted in offerings of stock issues aggregating 19,461,164 shares with an aggregate public offering price of $402,878,038. Bonds stabilized had a total face amount of $64,500,000. In connection with these stabilizing operations over 350 conferences were held with representatives of issuers and underwriters. Many more written and telephone requests were answered to assist them to avoid violations of the rules. 9,210 reports from these representatives were received, listed, examined and filed.

SECURITY TRANSACTIONS OF CORPORATION INSIDERS

Purpose of Regulation

In the Congressional hearings which led to the passage of the Securities Exchange Act of 1934, a common practice among some officers, directors, and large stockholders of engaging in short-term speculation in the listed stocks of their companies was revealed. For example, four of the officers and directors of a company were participants in a pool which made a profit of some $200,000 in less than 3 months in 1933 through trading in the company's common stock. In another instance the president of a company together with his brothers controlled the company through ownership of a little more than 10 percent of its stock. They sold their holdings for upward of $16,000,000 shortly before the company passed a dividend and later repurchased the stock for about $7,000,000, making a profit of approximately $9,000,000 on the transaction. In these instances not only were the insiders profiting by transactions based on information available to them solely because of their privileged position and not available to the public, but the stockholders and the investing public were unaware and had no way of knowing that they were trading in their companies' stocks. Such abuses as these and others led to the inclusion of the provisions of section 16 in the Securities Exchange Act. The basic Congressional objectives sought in the provisions of section 16 are twofold: (1) to provide public stockholders with information as to the prospects of their company which may be implicit in the security transactions of the insiders; and (2) to prevent corporation insiders from using inside information to unfair advantage in security trading.

Reports of Transactions and Holdings

For the purpose of affording to the public information as to the transactions and holdings of insiders, section 16 (a) provides that every person who is directly or indirectly the beneficial owner of more than 10 percent of any class of any equity security which is listed and registered on a national securities exchange, or who is an officer or director of

the issuer of such a security, shall file with the exchange and the Commission, at the time of the registration of such security or within 10 days after the time he becomes such beneficial owner, officer or director, a statement of the amount of all equity securities of such issuer of which he is directly or indirectly the beneficial owner, and within 10 days after the close of each month thereafter in which there has been any change in his beneficial ownership a statement indicating such changes and his holdings at the close of the month. Similar provisions are contained in section 17 (a) of the Public Utility Holding Company Act of 1935 covering officers and directors of registered public utility holding companies and in section 30 (f) of the Investment Company Act of 1940 covering officers, directors, principal security holders, members of advisory boards, investment advisers, and affiliated persons of investment advisers of registered closed-end investment companies.

Publication of Data Reported

The originals of these reports are available for public inspection from the moment they are filed. Recognizing, however, that a relatively limited number of investors have the opportunity to inspect the reports at the Commission's central office or at exchanges where additional copies of section 16 (a) reports must also be filed, the Commission condenses and publishes the information contained in the reports in a monthly Official Summary of Security Transactions and Holdings for distribution to investors, newspaper correspondents, press services and other interested members of the public. The elimination of certain items of nonessential data and slight changes in the format of the Summary have made it possible during the 1951 fiscal year to reduce the size of the Summary more than a third, with a corresponding reduction in printing and related costs.

Volume of Reports Filed and Examined

The number of reports filed during the 1951 fiscal year, as shown in the following table, represents an increase of more than 11 percent over the number filed during the preceding year. In fact, it is the largest number of such reports filed in any fiscal year since 1938.

(chart omitted)

Preventing Unfair Use of Inside Information

For the purpose of preventing the unfair use of information which may have been obtained by an insider by reason of his relationship to his company, section 16- (b) of the Securities Exchange Act of 1934 provides for the recoverability by or in behalf of the issuer of any profit he may realize from any purchase and sale, or any sale and purchase, of any equity security of the company within any period of less than six months. Corresponding provisions are contained in section 17 (b) of the Public Utility Holding Company Act of 1935 and section 30 (f) of the Investment Company Act of 1940. While the Commission is not charged with the enforcement of the civil remedies created by

these provisions, which are matters for determination by the courts in actions brought by the proper parties, it is interested in seeing that information with respect to possible profits by insiders is made available to issuers and public stockholders.

SOLICITATION OF PROXIES, CONSENTS, AND AUTHORIZATIONS

Pursuant to sections 14 (a) of the Securities Exchange Act of 1934, 12 (e) of the Public Utility Holding Company Act of 1935 and 20 (a) of the Investment Company Act of 1940 the Commission has adopted Regulation X-14 which is designed to regulate the solicitation of proxies, consents and authorizations in connection with securities of companies subject to those statutes in order to protect investors by requiring the disclosure of certain information to them at the time^ their proxies are solicited. The information prescribed for such disclosure is calculated to enable the investor to act intelligently upon each separate matter with respect to which his vote or consent is sought. The regulation also contains provisions enabling security holders who are not allied with the company's management to communicate with other security holders when management is soliciting proxies, either by arranging for the distribution of their own proxy statements or through the inclusion of their proposals in the proxy statements of management.

Statistics Relating to Proxy Statements

A slight increase occurred in the number of proxy solicitations made pursuant to Regulation X-14 during the 1950 calendar year when the staff of the Division of Corporation Finance received and examined material relating to 1/737 proxy solicitations including "follow-up" material in 185 instances, compared with 1,653 solicitations made in the preceding calendar year. [Footnote: On a fiscal year basis 1,788 solicitations were made in 1951 as compared with 1,668 in 1950. Follow-up material was used in 192 instances during the 1951 fiscal year.]

The number of solicitations made by management during the 1950 calendar year accounted for 1,713 or nearly 99 percent of all proxy statements filed that year; nevertheless, there were 24 solicitations made during the same period by non-management groups. Besides, 57 of the 1,713 proxy statements filed by management contained 97 proposals of 24 different stockholders. Certain of these stockholders arranged for the inclusion of their proposals in the proxy statements of more than one company. The number of management proxy statements including such stockholder proposals has increased from 19 in 1946 to 57 in 1950, while such stockholder proposals have grown from 34 to 97 and the number of different stockholders making these proposals has correspondingly risen from 9 to 24.

The election of directors overshadows in its frequency all other items of business combined for which proxies are sought. Thus in 1950 there were proxy statements

covering 1,523 stockholders' meetings at which the election of directors was one of the items of business, and 191 meetings not involving the election of directors, along with 23 remaining solicitations seeking assents and authorizations which did not involve any meeting or any voting upon directors.

The items of business other than that of election of directors for which stockholders' action was sought in the 1950 calendar year covered many specific proposals, the wide range and frequency of which may be noted in the following tabulation.

(chart omitted)

A remarkable increase is reflected above in the number of proxies submitting employees pension plans to the vote of stockholders. Thus, the 152 such proxies filed in the 1950 calendar year may be compared with 49 in 1949; 59 in 1948; 66 in 1947; and 75 in 1946. This increase is due largely to the negotiation of a number of plans recently on an industry-wide basis.

Examination of Proxy Material

Copies of proposed proxy material must be filed in preliminary form with the Commission, for its information and processing only, at least 10 days prior to the date the definitive copies are first sent or given to security holders; and copies of the statement in definitive form must be filed at the time proxy material is furnished to security holders. The Commission's proxy examination work must be completed during this comparatively brief interval between the filing of the material in its preliminary and definitive forms. Where a preliminary proxy statement fails to set forth information meeting the disclosure standards of the statute and the regulation, the parties concerned are notified immediately to that effect and given an opportunity to correct any such discrepancy before the definitive proxy statement is prepared. Illustrations of changes made in proxy material as a result of the Commission's examination procedure arising in actual cases during the 1951 fiscal year are given below.

Consolidated financial statements required. -- Under the regulation a proxy statement may incorporate by reference any financial statements contained in an annual report sent to security holders in connection with the same meeting as that to which the proxy statement relates, provided such financial statements substantially meet the requirements of the Commission's regulations governing the form and content of financial statements. A large grocery chain-store corporation, as a part of the preliminary proxy material relating to a proposal to increase its authorized preferred stock, included the financial statements that had been used in its annual report to stockholders for the preceding year. However, the accounts of three major subsidiaries, one financing fixture and equipment purchases, the second purchasing merchandise for the registrant, and the third operating a chain in Canada, were not included in the consolidated financial statements in that annual report, the accounts of the parent and certain other subsidiaries having been consolidated

in those statements. The effect was that neither a substantial amount of property and other assets used in the registrant's business nor senior securities of the unconsolidated subsidiaries were shown in the consolidated balance sheet proposed to be submitted to stockholders with the proxy solicitation.

The staff took the position that in view of the importance of the three unconsolidated subsidiaries to the integrated operations of the registrant the financial statements to be made part of the proxy material to be furnished stockholders should be on a complete consolidated basis. As a result the definitive proxy material as sent to stockholders contained financial statements on that basis.

Certain problems solved in accounting for acquisition of business and assets. -- Proxy statements prepared in connection with plans for acquisition, merger or recapitalization of corporations frequently raise special problems as to what financial statements will adequately reveal the proposed action. For example, a steel manufacturing company in its offer to acquire the business and assets of another company in a related business proposed to pay for the net assets to be acquired with additional issues of its senior and junior capital shares in an aggregate amount which the acquiring company considered represented fair value for the acquisition. These securities were to be distributed to the holders of the senior and junior securities of the company being acquired according to a fixed pro rata basis, thereby effecting the dissolution of the company. The purchase price of the assets being acquired, paid by the issuance of capital stock, was substantially in excess of the book value of the assets. This excess was allocated to fixed assets since the amount was approximately equivalent to the difference between independent currently appraised values and book values.

In the preliminary proxy material proposed to be submitted to the stockholders of the respective companies, statements of earnings and of assets, liabilities and capital of the respective companies were furnished in conventional form. However, the proposed data did not readily demonstrate the impact of the acquisition upon the acquiring company as affected (1) by the new capital structure and (2) by the new valuation placed upon the fixed assets to be acquired. Specifically, the stockholders would be unable to determine readily (1) the coverages of liquidating values and of dividend requirements of the preferred shares as increased, and (2) the earnings per share of the common stock as increased and as affected by the increased amount of the preferred stock. Accordingly, the respective companies were requested by the staff to furnish in the proxy statements a pro forma consolidating balance sheet giving effect to the recapitalization and acquisition, together with a pro forma statement of profit and loss for the year 1950 of both companies combined, calculating the income and excess profits taxes under the Revenue Act of 1950 for the entire year, and calculating depreciation charges upon the basis of the increase in valuation of the fixed assets. Also upon such request the pro forma net income, applicable to common stock in the aggregate and in per share amounts after provision for preferred stock dividends, was stated and accompanied by an

explanation that this information was not necessarily indicative of the results of future operations or the availability of net income for dividend purposes.

Complete financial statements required in order to show results of significant corporate proposals. -- A registrant engaged in real estate operations submitted preliminary draft copies of proxy solicitation material, without complete financial statements, seeking among other matters authorization of stockholders to amend the company's certificate of incorporation so as to reduce the par value of capital stock by a split-up from $10 per share to $1 per share; to reduce correspondingly the capital of the company from $4,255,690 to $425,569; to execute eighteen separate mortgages, together covering all of the company's real properties and aggregating $5,000,000 in principal amount to mature in 10 years, with interest at the rate of 4 percent per annum; to distribute forthwith to stockholders the $5,000,000 of mortgage proceeds and other funds of the company aggregating $5,250,252. The company stated that financial statements had not been included for the reason that they were not deemed material for the exercise of prudent judgment in regard to the matters to be acted upon at the meeting. The company had included a summary of the balance sheet at the close of its last fiscal year and a table showing for ten years the "net income after operating expenses, adjusted to exclude interest on indebtedness, depreciation, and income taxes."

The first letter of comment issued by the Division of Corporation Finance indicated the need to furnish to stockholders in this connection certified financial statements for three fiscal years, unaudited statements of a more recent date, and a pro forma balance sheet as of such recent date showing the effect of the proposed transactions covered by the proxy statement. The company was also requested to furnish to stockholders a complete summary of earnings for the last ten fiscal years.

The most recent balance sheet indicated a stockholders' equity of $6,236,210.30; and the pro forma balance sheet, as of the same date, after giving effect to mortgaging of properties, reduction of capital and distribution to stockholders, indicated a stockholders' equity of $835,951.10. The table of "adjusted income" originally submitted averaged $729,000 per year (with a minimum of $688,000 and maximum of $787,000) compared with interest and amortization on the proposed mortgages of $385,000, which latter figure was changed to $350,000 in the revised material. The revised summary of earnings for ten years and six months afforded adequate material for analysis of the effect of the change in capital structure of the company by showing in separate columns "Rental and Other Income"; "Operative, Administrative, and General Expense"; "Depreciation" (revealed as being in excess of $200,000 per year); "Interest on Indebtedness" (none in the last six months shown); "Income Taxes"; and "Net Income."

Failure to disclose certain essential information including the names of persons acquiring a controlling block of common stock from the issuer. -- The registrant filed preliminary proxy soliciting material to be used in connection with a forthcoming annual meeting at which it was proposed (1) to vote upon a proposal to lease the registrant's

plants and equipment for a term of years to a corporation controlled by an outside group and (2) to elect nine directors for the coming year. Five directors were to be elected by holders of the registrant's preferred stock because of defaults in the payment of dividends, and four by holders of registrant's common stock. The management and control of the registrant had been changed some months previously. The financial position of the registrant was very weak due to continued losses in its peacetime operations and large indebtedness which was past due. The material indicated it was anticipated that within six months there would be submitted to stockholders for their approval a plan of recapitalization, including the issuance of a large block of common stock, in exchange for the outstanding stock of the lessee corporation. Such stock would have represented control of the registrant.

No disclosure was made of the names of the persons financially interested in the lessee corporation who might succeed to control of the registrant. This and other deficiencies were brought to the attention of the registrant, after which revisions of the preliminary soliciting material were filed. The proposal to lease the plants was ultimately abandoned, among other reasons because the registrant was unable to obtain the required consents of its mortgage creditors. The revised material proposed a plan of recapitalization which involved the issue of common stock for cash to the same outside group. The obligation to purchase such additional stock was subject to various material conditions which had to be met by the company. These proposals would have substantially reduced the interests of the old common and preferred stockholders, and would have given control of the company to the outside group, who for the first time were named.

A few years earlier, the Commission had obtained an order enjoining the central figure in this group from the purchase of certain securities in violation of the Securities Exchange Act of 1934. Certain other questionable activities of this individual had been brought to the Commission's attention in the course of its earlier investigation of investment companies. Because of continued material deficiencies in the revised proxy soliciting material, the Commission ordered a private investigation under section 21 (a) of the Securities Exchange Act of 1934. During the course of the investigation the registrant made numerous revisions to reflect facts disclosed by the investigation. The registrant apparently was reluctant, however, to disclose the existence of the injunction against the principal promoter as well as other adverse facts regarding him developed during the course of the investigation.

Subsequently, the registrant abandoned the proposed plan of recapitalization, including the sale of common stock, and confined its deferred annual meeting to the election of directors, for which a committee acting on behalf of holders of preferred stock had solicited sufficient proxies to elect a majority of the board.

Problem arising in use of inventory reserves to equalize reported income. -- The Commission's 14th Annual Report referred to the adoption by the American Institute of Accountants of research bulletins recommending that inventory reserves created in

anticipation of losses not yet incurred should not enter into the determination of income. These bulletins assisted in correcting a troublesome practice that had arisen during and immediately after World War II. While this problem was largely corrected in recent years, it arose in the 1951 fiscal year in connection with the examination of a proposed proxy statement soliciting authority to dispose of all of the assets of that part of the company's business to which the inventories in question applied. The independent public accountants of this particular company, a leading processor of certain raw materials, had noted in their certificate accompanying the registrant's first annual report following the publication of the Institute's bulletins that the net income for the fiscal year had benefited through return to income of previously created reserves and that under recently accepted accounting principles the amount should have been restored directly to surplus. That annual report and the subsequent year's annual report submitted on the same basis were amended at the request of the staff to eliminate the Qualification in the certificate of the accountants and to return the reserve directly to surplus.

Despite the fact that the Commission had required such amendment of those annual reports, the company included in a preliminary proxy filed in the 1951 fiscal year a summary of earnings for ten years prepared on the original basis. In this summary the first seven years reflected deductions for additions to the inventory reserve and the years 1948 and 1949 reflected partial return of the reserves to income. Results for 1950 were not furnished in this preliminary proxy material. When complete financial statements including a new summary were then furnished at the instance of the Commission, it was discovered that while data for two of the years summarized, 1948 and 1949, were restated to conform to the amended annual reports, a footnote was appended to the net profit item for the year 1947 which read: ". . . after appropriation of $1,500,085 -- see Consolidated Statement of Profit and Loss." In the opinion of the Commission's staff, which corresponds with the Institute's recommendation noted above, the amount of $1,500,085 was an appropriation of surplus and not a proper charge in the profit and loss statement. Accordingly, the issuer was advised that the net profit for the year in question should be reported before making the $1,500,085 deduction, and that the footnote should be deleted. The issuer was further advised that, to the extent that other deductions in prior years represented appropriations of income similar to that made in 1947, the earnings summary should be recast to show results for all years on a uniform basis.

As a result of the amendments secured in this case, the net profit for each of the seven years 1941 through 1947 was reflected in the summary as revised at a substantially higher figure, the effect of which was to increase the net profit shown for the seven-year period from approximately $7,000,000 to $12,000,000. That no losses in the amount of this difference had been sustained over the period seems clear by a statement in the definitive proxy material that the market value of inventory early in 1951 was approximately $5,000,000 in excess of (or about double) the book value, which value represented cost under the last-in-first-out method of pricing.

REGULATION OF BROKERS AND DEALERS IN OVER-THE-COUNTER MARKETS

Registration

Section 15 (a) requires the registration of brokers and dealers using the mails or instrumentalities of interstate commerce to effect transactions in securities on over-the-counter markets, except those brokers and dealers whose business is exclusively intrastate or exclusively in exempt securities.

Statistics relating to registrations of brokers and dealers fiscal year ending June 30, 1951

Effective registrations at close of preceding fiscal year -- 3,930

Effective registrations carried as inactive [Registrations on inactive status because of inability to locate registrant despite careful inquiry] -- 70

Registrations placed tinder suspension during preceding fiscal year -- 0

Applications pending at close of preceding fiscal year -- 23

Applications filed during fiscal year -- 464

Total -- 4,487

Applications withdrawn during year -- 16

Applications cancelled during year -- 0

Registrations withdrawn during year -- 363

Registrations cancelled during year -- 43

Registrations denied during year -- 0

Registrations suspended during year -- 0

Registrations revoked during year -- 85

Registrations expired by Rule X-15B-3 -- 0

Registrations effective at end of year -- 3,945

Registrations effective at end of year carried as inactive [Registrations on inactive status because of inability to locate registrant despite careful inquiry] -- 9

Applications pending at end of year -- 26

Total -- 4,487

Administrative proceedings

Registration may be denied or revoked by authority of section 15 (b) of the Act, and brokers and dealers may be suspended or expelled from national securities associations and exchanges for specific types of misconduct on the part of the firm, its partners, officers, directors or employees. To carry out these provisions of the Act, applications for registration must be examined in the light of the information contained therein and information obtained from numerous other sources available to the Commission in order to determine whether the firm is entitled to registration for which it has applied. When it appears that an applicant may be disqualified under such standards, proceedings are ordered by the Commission to determine whether on the evidence adduced it is consistent with public interest to permit registration. The applicant is, of course, given notice of the issues to be considered and afforded full opportunity to be heard thereon. Similar procedures are followed in proceedings brought against registered brokers and dealers to determine whether registration should be revoked or the firm suspended or expelled from membership in a national securities exchange or association. The following tabulation reflects the number of such proceedings pending during the fiscal year:

(chart omitted)

As shown in the above table, there were pending at the beginning of the fiscal year two proceedings to determine whether applications for registration should be denied or granted, and five such proceedings were instituted during the year. Of these seven, four registrations were granted and the proceedings dismissed; two applicants withdrew their applications; one proceeding remained pending at the end of the year.

At the beginning of the fiscal year, there were 23 pending proceedings to revoke registration, 12 of which also involved consideration of suspension or expulsion from the NASD. During the year, 92 revocation proceedings were instituted, three of which involved also the question of suspension or expulsion from the NASD, and one suspension or expulsion from an exchange. A total of 84 of the proceedings instituted concerned the failure to file financial reports as required by rule X-17A-5, and eight concerned alleged fraudulent conduct. A total of 93 revocation proceedings were decided during the year, leaving 22 pending at the end of the year.

In se\en proceedings the Commission revoked registration on findings of fraudulent conduct prohibited by the Securities Act and the Securities Exchange Act, including such

frauds as misappropriation of customers' funds and securities, misrepresentations in the sale of securities, manipulation of the market price of securities on national securities exchanges, the sale of unregistered securities in violation of section 5 of the Securities Act, false and fictitious entries on books and records and filing of false financial reports with the Commission.

Proceedings against W. F. Coley & Company, Inc., and Wade F. Coley, its president and controlling stockholder, resulted in an order revoking the registration of the firm, expelling the firm from the NASD, and the finding that Wade F. Coley, personally, was the cause of such order. [Footnote: *In the matter of W. F. Coley & Company, Inc.*, Securities Exchange Act release No. 4470, July 18, 1950. On Oct. SO, 1950, Wade F. Coley was convicted in the United States District Court at Greenville, S. C., on a plea of guilty, to an indictment charging violations of the anti-fraud provisions of the Securities Act of 1933, the Mail Fraud Statute, section 17 (a) of the Securities Exchange Act and Rule X-17A-3 thereunder requiring registered brokers and dealers to keep public books and records, the Perjury Statute, and the False Statement Section (Section 1001) of the Criminal Code in connection with his operation of W. F. Coley & Company, Inc., and the effecting of securities transactions on behalf of customers of that firm.] The Commission found that the firm, aided and abetted by Coley, had misappropriated customers' securities and funds, had concealed such misappropriations by false or deficient records, and had filed false financial reports with the Commission.

In proceedings against Mercer Hicks Corporation and Mercer Hicks, its president and controlling stockholder, the Commission revoked the registration of the firm, expelled it from the NASD, and found Mercer Hicks, personally, a cause of such revocation and expulsion, the respondents consenting thereto. [Footnote: *In the matter of Mercer Hicks Corp. and Mercer Hicks,* Securities Exchange Act release No. 4557, Jan. 31, 1951.] On the respondents' admission of the facts alleged, the Commission found that Mercer Hicks Corporation and Mercer Hicks, individually, had made false and misleading representations in the sale of the corporation's stock, that purchasers were told that the corporation was being operated at profit but were furnished with no financial data, and that purchasers were not informed of the corporation's operating deficits or the fact that dividends were paid out of capital surplus obtained from the sale of the stock. The Commission also found that the corporation and Hicks appropriated funds and securities held for customers and substituted therefor the stock of the corporation, without the knowledge of these customers.

It is customary, when adequate evidence of violations can be obtained in time, to institute court action promptly to enjoin further violations, deferring until later consideration of other remedial or punitive action. Thus in the instance of Mercer Hicks Corporation, the Commission's action to revoke its broker-dealer registration was instituted after the district court, Southern District of New York, had enjoined the fraudulent acts and practices later alleged in the revocation proceedings. [Footnote: *SEC v. Mercer Hicks Corp. and Mercer Hicks*, S. D. N. Y. No. 5896. Litigation release 632, Dec. 26, 1950.] In

two other instances during the current year, registration was revoked on findings of fraudulent conduct by the registrants after a court had enjoined them from further violations. [Footnote: In May 1949, S. H. Junger, George T. Anderson and Robert S. Junger, individually, and as co-partners in Junger, Anderson and Company, were enjoined on complaint of the Commission from engaging in certain fraudulent practices discovered during an investigation. *SEC. v. Caplan, Junger, Anderson and Company*, Civil No. 49-138 S. D. N. Y. Litigation release 514, May 14, 1949. On July 27, 1950, the Commission revoked the registration of Junger, Anderson and Company on findings of fraudulent conduct, but specifically finding that as to Robert S. Junger, there was no evidence that he knowingly participated in the scheme. S. H. Junger and Company, a partnership, consisting of Samuel H. Junger and his wife, Frances Junger, was later permitted to register as broker and dealer, Securities Exchange Act release No. 4563, Feb. 8, 1951. In *SEC v. Howard F. Hansell, Jr.*, Civil 62-240 S. D. N. Y., the court on complaint filed by the Commission enjoined Hansell from further violations of section 9 (a) (2) of the Securities Exchange Act. Litigation release 627, November 22, 1950. Later, the Commission revoked Hansell's registration on findings of fraudulent conduct. Securities Exchange Act release No. 4536, Dec. 18, 1950.]

In proceedings resulting in the revocation of the broker-dealer registration of Lawrence R. Leeby [In the matter of Lawrence R. Leeby, doing business as Lawrence R. Leeby & Company. Securities Exchange Act release No. 4601], the Commission rejected the contention that a broker-dealer, conducting a securities business as a sole proprietor, may engage in "personal transactions" as distinguished from "company transactions" without recording them on his business books. This proceeding is also significant because it is the only instance in which the Commission has twice revoked the registration of a broker-dealer. Leeby first became registered in 1936. In 1943, the Commission revoked his registration on findings of fraudulent practices in the sale of oil royalties. In 1946, he again applied for registration, and after hearings the Commission granted him the limited registration he requested. He was permitted to do business as a broker, but his dealer activities were limited to the sale of investment companies' shares.

On October 21, 1948, he petitioned the Commission to remove the restriction with respect to his dealer activities so that he might do a general securities business. At a hearing on his petition he testified that he had fully complied with the conditions of 1946 registration and had not effected any transactions as a dealer except in investment companies' shares. Since an examination of his books and records made by the Commission's staff reflected nothing to the contrary, the Commission removed the restriction. When it was later discovered that Leeby had purchased and sold Ribbonwriter shares during the period when his registration as a dealer was limited to investment companies' shares and that these transactions were not recorded on his books, proceedings to revoke his registration were instituted. During the hearings, he sought to defend the exclusion of the transactions in Ribbonwriter stock from his broker-dealer books on the ground that these were "personal transactions" unrelated to his securities "business."

In its findings, however, the Commission held as artificial any attempted distinction between "personal transactions" and "company transactions" where the "company" is a sole-proprietorship, and held that all securities transactions of the proprietor are required to be recorded on his broker-dealer books whether they are for so-called personal investment for what is termed "firm trading account" for which business capital is employed. The Commission made the finding that Leeby's failure to enter his "personal" transactions in an account on his broker-dealer books was in willful violation of the bookkeeping rules prescribed for brokers and dealers under section 17 (a) of the Securities Exchange Act, and the further finding that the representation in his application and testimony, in connection with his 1948 petition for unconditional registration as a dealer, that he had fully complied with the conditions of his limited registration was false and misleading.

Broker-Dealer Inspections

Section 17 (a) of the Securities Exchange Act empowers the Commission to make periodic, special, and other examinations of the books and records of brokers and dealers. Such inspections have become the principal means by which the Commission detects and prevents violations of law by brokers and dealers. Inspections are frequently limited to a particular phase of the-firm's business, but generally they encompass examination of all characteristic activities.

During the fiscal year the Commission's regional offices, the staff of which conducts these inspections, reported on 922 such examinations, 696 of which were inspections of NASD members. As in previous years, a substantial number of violations of the rules and regulations were discovered, including non-compliance with the capital rule, the hypothecation rule, and Regulation T prescribed by the Board of Governors of the Federal Reserve System. There were a few instances of secret profits, a good many transactions in which the reasonableness of the price to the customer in relation to current market was questionable, and a fairly large number of infractions too scattered to classify separately.

Consistent with accepted standards of administrative procedure, those violations which appear to be inadvertent or the result of misinformation or innocent misinterpretation, and not "willful," are called to the attention of the firm involved to afford it an opportunity to "put its house in order." Other remedies which may be invoked against violations are discussed in detail under the preceding caption "Administrative Proceedings."

Investigations

Investigations of brokers and dealers stem from various sources. When an inspection discloses conduct or practices the full facts with reference to which must be obtained and analyzed to determine whether any remedial or punitive action is necessary investigation

is promptly undertaken. Investigations are also made when complaints from customers are received. Other investigations may be commenced as a result of information supplied by cooperating agencies such as state securities commissions, securities exchanges and associations, or "better business bureaus." When investigations are completed and the evidence has been analyzed, the staff makes recommendations to the Commission for such further action as appears appropriate. In some instances the recommendation may be for injunctive relief, in some for administrative action such as discussed above and in some for notice, as contemplated by the Administrative Procedure Act to achieve compliance with the Act.

The following schedule reflects the number of such investigations during the fiscal year.

(chart omitted)

Financial Reports

One of the Commission's rules, X-17A-5, requires brokers and dealers to file financial reports each calendar year. During the 1951 fiscal year, 3,705 such reports were filed. Examination of the financial report filed by a broker-dealer affords the staff an opportunity to determine whether, as of the date of the report, the firm is in compliance with the capital requirements prescribed by rule X-15C3-1, and if it is not, the firm is given an opportunity to bring its financial condition up to the required standards. Failure to do so may, of course, require more drastic measures to enforce the rule.

SUPERVISION OF NASD ACTIVITIES

Membership

At June 30, 1951, there were 2,846 members of the National Association of Securities Dealers, Inc. (NASD), the only national securities association registered as such with the Commission. This represented an increase of 62 members in the year as a result of 212 admissions to, and 150 terminations of, membership. At the same date there were registered with NASD as registered representatives 30,922 individuals, including generally all partners, officers, traders, salesmen and other persons employed by member firms in capacities which involved their doing business directly with the public. This represented an increase of 2,128 registrations during the year as a result of 5,128 initial registrations or re-registrations and 3,000 terminations of registrations.

Disciplinary Actions

During the 1951 fiscal year the Commission received from the NASD reports of final action in 22 disciplinary cases in which formal complaints had been filed against members. One of these complaints was dismissed on the finding by the NASD District

Business Conduct Committee of initial jurisdiction that there had been no violation of the Rules of Fair Practice as alleged in the complaint. In the remaining 21 cases the appropriate Business Conduct Committee found that the members or registered representatives of the members cited in the complaints, had acted in violation of the Rules of Fair Practice and imposed. various penalties as a consequence of those infractions.

Of the 21 disciplinary decisions which included findings of violations against those named in the complaints, eight cases were directed solely against member firms who were subjected to the following penalties: Two member firms were expelled; two member firms were each fined $500 and censured; one member firm was fined $300; one member firm was fined $100 and censured; and two member firms were censured.

In nine other cases findings of violations of the Rules of Fair Practice, and the consequent penalties, were directed not only against member firms but also against registered representatives of such members who had been named, together with their employers, in the complaints. One such case resulted in expulsion of the member firm involved and revocation of the registration with the NASD as registered representative of one individual and suspension of such registration of two other individuals. This decision, which had been affirmed by the Board of Governors on appeal, was appealed to the Commission by R. H. Johnson and Co., the member firm, and at the year-end was in process before the Commission. [Footnote: Securities Exchange Act release No. 4571 (1951). This appeal, pursuant to the provisions of section 15A (g) of the Securities Exchange Act of 1934, operates as a stay of the effectiveness of the NASD's action pending the Commission's decision. There was also Pending at the year-end, its status not substantially changed during the year, another such appeal to the Commission from an NASD decision which imposed on Otis & Co., the appellant, a two-year suspension from membership in NASD. This action arose from a stock offering of Kaiser-Fraser Corporation in 1948 as described in considerable detail in the Commission's 15th Annual Report, pages 73-77, and 16th Annual Report, pages 58-59.] In two unrelated cases the member involved was expelled from the Association and the registration with the NASD of two registered representatives of each of the two firms were revoked. [Footnote: After the close of the fiscal year one of these decisions was appealed to the Commission by George J. Martin Co., the member, and Alfred and Irving Shayne, the representatives.]

In another case both a member and a representative of that member were each fined $500; in another, fines of $200 were imposed both on the member and on the member's representatives. The only other such case involving a fine resulted in a fine of $5,000 on the member firm, six months' suspension of registration of one representative, three months' suspension and a fine of $1,000 with respect to another and three months' suspension and a fine of $100 with respect to a third representative. In three other cases against both member firms and representatives of the firms, the firms were censured and in addition the representatives were respectively suspended for 30 days, fined $100 and fined $25.

A third category of cases consisted of those in which a finding of violations, and the imposition of penalties, was directed solely against a representative of a member with a concurrent finding that the member had not acted in violation of the Rules of Fair Practice and dismissal of that portion of the complaint directed against the member. In this type of action revocation of the representative's registration resulted in three cases and, in a fourth, the penalty was a five-year suspension of registration.

The Commission continued its practice of referring to the NASD for appropriate action facts disclosed in the course of its broker-dealer inspection program which tend to indicate possible violations of the Association's Rules of Fair Practice. At the end of the last fiscal year there were four such references in process before the Association and, in this year, ten additional references were made. At the end of the year nine of these references were in process, reports of disposition having been received by the Commission from the Association on five of the cases. Four of these five cases were disposed of by informal means without invoking formal complaint procedure; the formal complaint case resulted in a fine of $100 and censure of the member involved, as mentioned above.

Commission Review of Action on Membership

Under section 15A (b) (4) of the Securities Exchange Act of 1934, and NASD by-laws, except in cases where the Commission approves or directs admission to or continuance in membership as appropriate in the public interest, no broker or dealer may hold NASD membership if he controls a person who has been, among other things, expelled from a registered securities association for violation of an association rule prohibiting conduct inconsistent with just and equitable principles of trade, or is subject to an order of the Commission revoking his registration or expelling him from NASD membership.

Pursuant to this authority, and with consideration to the affirmative recommendation of the Board of Governors of the NASD, the Commission approved the admission to membership of O. H. Hecht, who was under a disqualification arising from expulsion by and from the NASD of Mutual Investments, Ltd., a broker-dealer firm of which Hecht had been a partner, on findings that the firm had been guilty of conduct inconsistent with just and equitable principles of trade. [Footnote: Securities Exchange Act release No. 4619 (1951)] The Commission also approved a similar petition by the NASD for the continuance in NASD membership of Oscar F. Kraft & Co. while controlling Carter Harrison Corbrey, who was under disqualification as a consequence of expulsion from NASD membership and revocation of broker-dealer registration by the Commission. [Footnote: Securities Exchange Act release No. 4562 (1951)]

During the year two other petitions were filed with the Commission under this same section of the statute by or on behalf of firms seeking to retain NASD membership while

controlling a disqualified person. Each of these petitions was withdrawn prior to a decision on the merits by the Commission.

CHANGES IN RULES, REGULATIONS, AND FORMS

As stated elsewhere in this report, section 16 (b) of the Act provides in general that where any director or officer of the issuer of a listed and registered equity security or the beneficial owner of more than 10 percent of any class of such security has realized any profit from any purchase or sale, or sale and purchase, of any equity security of the issuer, such profit inures to and may be recovered by the issuer, or by any security holder acting in its behalf. The section authorizes the Commission to adopt rules exempting therefrom any transactions not comprehended within its purpose. Various rules adopted during the 1951 fiscal year under this authority, after consideration of all comments and suggestions invited and received in the premises, are briefly described below.

Rule X-16B-1. Exemption from section 16 (&) of certain transactions by registered investment companies. -- This new rule, in the form of a revision of rule X-16B-1 which in its previous form had' become obsolete, exempts transactions which the Commission has, by order entered pursuant to section 17 (b) of the Investment Company Act, exempted from 17 (a) of that Act.

Rule X-16B-3. Exemption from section 16 (b} of certain acquisitions of securities under stock bonus or similar plans. -- Rule X-16B-3 was amended so as to exempt from section 16 (b) acquisitions by directors or officers of securities received under certain types of bonus, profit-sharing, retirement or similar plans not previously exempted by this rule. It should be noted that the rule exempts only certain acquisitions of securities under plans of the types specified. Sales of securities so acquired are not exempted by the rule and are, therefore, within the purview of section 16 (b) of the Act if within six months before or after such sales the director or officer effects other acquisitions which can be matched against them.

Rule X-16B-5. Exemption from section 16 (5) of certain transactions in which securities are received by redeeming other securities. -- This new rule was adopted to exempt from the operation of section 16 (b) those transactions in which one security is surrendered for another, where both the old and the new securities are substantially and in practical effect equivalents and where the transaction does not require the payment of any consideration.

Rule X-16B-6. Exemption of long-term profits incident to sales within six months of the exercise of an option. -- This new rule grants partial exemption with respect to profit which might otherwise be deemed to have been realized and recoverable, where there is a purchase by an "insider" of an equity security pursuant to the exercise of an option or a similar right and a sale of that equity security within six months thereof. A statement of

the considerations which led to the adoption of this rule accompanied its promulgation in Securities Exchange Act release No. 4509.

As set forth more fully in that statement, the Commission had been aware for some time of a controversy concerning the proper method of computing profits under section 16 (b) where there is a sale of an equity security acquired pursuant to an option. The Act makes such profits recoverable in private litigation, thus placing upon the courts the ultimate responsibility for the interpretation of section 16 (b), but gives the Commission, as pointed out above, responsibility for exempting by rule transactions which it may determine to be "not comprehended within the purposes of section 16 (b)."

Uncertainty as to just what profits would, as a matter of legal interpretation, be recoverable in the absence of a rule, as well as uncertainty whether the Commission should attempt by rule making to affect pending litigation, had previously induced the Commission to refrain from adopting such a rule. The Commission determined to express its understanding of the relationship between such transactions and the underlying purpose of section 16 (b), as set forth in the published statement; and to exercise its rule-making power in the light of that understanding, as reflected in this new rule.

Rule X-16C-3. Exemption of sales of securities to be acquired. -- The Commission adopted a new rule, designated rule X-16C-3, exempting certain sales from the provisions of section 16 (c) of the Securities Exchange Act of 1934.

Section 16 (c) provides that it shall be unlawful for any beneficial owner of more than 10 percent of any class of equity security registered on a national securities exchange, or a director or officer of the issuer of such a security, to sell any equity security of the issuer (other than an exempted security), (1) if he does not own the security sold, or (2) if, owning the security, he does not either deliver it within 20 days or deposit it in the mails or other usual channels of transportation within five days, unless he was unable to do so notwithstanding the exercise of good faith or it would cause undue inconvenience or expense.

The purpose of the rule is to permit persons who are entitled to receive a security "when issued" or "when distributed" as an incident of ownership of another security to sell the new security subject to the same restrictions as would apply if the "when issued" or "when distributed" security were already in their possession. This rule assumes, of course, that the "when issued" or "when distributed" sale is otherwise lawful under the Securities Act of 1933 and the Securities Exchange Act of 1934.

Revised Form U5S. -- During the fiscal year the Commission adopted substantial revisions in the annual reporting requirements applicable to public utility holding companies registered under the Public Utility Holding Company Act of 1935. [Footnote: Public Utility Holding Company Act release No. 10432]

The. object of these changes was to reduce the over-all reporting requirements for registered holding companies under both the 1935 Act and the Securities Exchange Act of 1934. A new Form U5S was promulgated as the annual report form for registered holding companies. The Commission has abolished Form U-14-3, heretofore required to be filed annually under the 1935 Act by registered holding companies, and Forms U5-K and U5-MD which registered holding companies formerly had the option of filing in lieu of Form 10-K under section 13 or 15 (d) of the 1934 Act. Whereas each registered holding company in a system has heretofore been required to file separate annual reports on Form U5S, the revised requirements provide that only one annual report shall be filed by the top registered holding company for all registered holding companies in the system. Registered holding companies required to file annual reports under Section 13 or 15 (d) of the 1934 Act (formerly on Form 10-K) may now satisfy these requirements in full by filing copies of their annual reports prepared on the new Form U5S.

LITIGATION UNDER THE SECURITIES EXCHANGE ACT

Brokers and Dealers

Although the Commission's sanctions against brokers and dealers violating the Securities Acts include administrative proceedings and references to the Attorney General for criminal prosecution, it is often necessary to seek court injunctions to afford immediate protection to investors.

In *S. E. C. v. Lloyd Beversdorf* [E. D. Mich. Civil Action No. 10290], the Commission obtained a final judgment by consent enjoining the defendant from further violations of the broker-dealer registration provisions. The Commission charged that he was engaging in a broker-dealer business without having registered with the Commission in accordance with section 15 (b) of the Securities Exchange Act.

In *S. E. C. v. Adams & Company* [N. D. Ill. Civil Action No. 49 C 1145] during the fiscal year the individual defendants consented to the entry of a judgment restraining them from further violations of the fraud provisions of the Securities Act and of the Securities Exchange Act. A similar judgment was entered against Adams & Company by default. In that case a temporary receiver had been appointed for the protection of customers during the previous fiscal year when the Commission had filed its complaint. The complaint had charged that the defendant Adams & Company, a registered broker-dealer, and three of its officers violated the fraud provisions of both the Securities Act and the Securities Exchange Act in soliciting and accepting customers' orders for the purchase and sale of securities while its liabilities exceeded its assets; in inducing customers to purchase securities by representing that such securities would be held in safekeeping when, in fact, the securities were being hypothecated to secure loans made to the firm; and in soliciting customers to purchase securities and accepting payment therefor upon the representation

that the securities would be delivered when, in fact, the defendants used the customers' money for their own benefit.

In *S. E. C. v. Frank S. Kelly* [N. D. Ill. Civil Action No. 50 C 1798], the Commission's complaint sought to enjoin the defendant, a registered broker-dealer, from further violations of certain of the fraud provisions of the Securities Exchange Act of 1934. The complaint charged that the defendant effected transactions in securities for the accounts of customers and, as a part of such business, solicited and accepted orders from customers for the purchase of when-issued securities, using money received from customers to purchase securities for his own account and for other purposes without disclosing that fact to his customers. The court granted a temporary restraining order and appointed a receiver for the defendant. Subsequently, the defendant consented to a final injunction.

In *S. E. C. v. Howard V. Hansell* [S. D. N. Y. Civil Action No. 62-240] the defendant consented to the entry of a final judgment enjoining him from further violations of the anti-manipulative provisions of the Securities Exchange Act. The Commission's complaint charged that the defendant, in trading in securities on the New York Stock Exchange and the New York Curb Exchange, induced other persons to purchase said stock by raising the market price of such stocks by means of purchasing the stock through other persons, recommending the stock to brokerage firms and friends on the representation that the stocks would increase in price, asking brokerage firms and friends to purchase the stock as a favor to him and, in connection with one of the stocks, engaged a public relations man to induce brokerage firms and others to purchase such securities. Subsequently, Hansell's broker-dealer registration was revoked.

Injunctive action was also brought against Mercer Hicks and Mercer Hicks Corporation, a broker-dealer, for alleged violations of the Securities Act of 1933. This case is discussed above at pages 51 and 52.

Amicus Curiae Cases

In addition to the cases in which it is a party, the Commission frequently participates as *amicus curiae* upon important questions of law, but not on factual issues, arising in suits between private parties involving construction of the Acts administered.

An important issue involved in all of the private actions in which the Commission participated as *amicus curiae* under section 10 (b) of the Securities Exchange Act of 1934 and rule X-10B-5 thereunder during the past year is whether that section and rule are applicable to transactions in securities not traded by professionals on the exchanges or in the over-the-counter markets of brokers and dealers. The Commission has repeatedly expressed the view that the section and rule are applicable to such transactions. The Commission's view was upheld in July 1950 by the United States District Court for the Eastern District of Pennsylvania in *Robinson v. Difford* [92 F. Supp. 145]. The question,

among others, is also involved in *Speed v. Transamerica Corp.* [D. Del., Civil Action No. 480. See 13th Annual Report of S. E. C., p. 63, 15th Annual Report of S. E. C., p. 72, and 16th Annual Report of S. E. C., p. 58], *Fratt v. Robinson* [W. D. Wash., Civil Action No. 2765] and *Northern Trust Co. v. Essaness Theatres Corp.* [N. D. Ill., Civil Action Nos. 50 C 1750 and 50 C 1762], all of which were pending at the close of the fiscal year.

In the Fratt and Northern Trust Co. cases, the Commission also expressed the view that the applicable statute of limitations in an action for damages for the violation of rule X-10B-5 is that of the state of the forum. Moreover, in the Northern Trust Co. case the Commission presented argument to the following effect: (1) that section 10 (b) and rule X-10B-5 apply to intrastate transactions in securities involving the use of the mails, irrespective of whether the securities are registered for trading on an exchange or whether the issuer conducts an interstate business, (2) that under rule X-10B-5 it is sufficient that the mails or facilities of interstate commerce are used in connection with a particular sale or purchase of securities, and that it is not necessary that misrepresentations or misleading statements be communicated through the mails or facilities of interstate commerce, and (3) that rule X-10B-5 was not rendered inapplicable to the securities purchases in that case by virtue of the fact, if established, that the purchases were made pursuant to conditions respecting directors' and shareholders' consent contained in an agreement and corporate by-law predating the rule.

The Commission also participated during the past fiscal year as *amicus curiae* in a number of cases which involved a construction of section 16 (b) of the Act, wherein there is accorded to a corporation the right to recover profits realized by officers, directors or large stockholders from purchases and sales or sales and purchases of the corporation's equity securities within a six months' period. In all of these cases, the courts were concerned with the problem of computing the profits which might be recovered by or for the particular corporation involved.

In *Steinberg v. Sharpe, et al.* [95 F. Supp. 32 (S. D. N. Y. 1950)], a stockholder of Bendix Home Appliances, Inc., sued an officer of the company, to recover profits that the officer allegedly made in the sale of certain shares of stock which he had purchased less than six months before. The securities had been purchased by the defendant pursuant to earlier employment agreements which allowed him to buy a specific number of Bendix shares at a specified price which was lower than the market price. The plaintiff claimed $11,571.20, the difference between the sales price and the cash actually paid under the terms of the option contracts. Recognizing, however, that the option itself had certain values, Judge Medina concluded that the cost basis of the stock was the cash actually paid pursuant to the option plus the value of the option on the date that it accrued and therefore allowed a judgment for the plaintiff in the amount of the difference between the sale price and the market price of the stock on the date the option accrued. The Commission had urged the conclusion reached by the court. On appeal, the Commission filed a memorandum in support of the findings of the district court and the court of

appeals rendered per curium a memorandum opinion affirming the decision of the lower court [190 F. 2d 82 (C. A. 2, 1951)].

In *Blau v. Hodgkinson et al* [S. D. N. Y. Civil Action No. 63-51], a security holder of Federated Department Stores brought an action to recover profits realized by directors of the company as a result of certain transactions in the company's securities. One of the defendants, acting pursuant to a stock warrant granted to him on October 2, 1944, had purchased a number of Federated's common shares at substantially less than the market price and then sold them within 6 months at the current market price. On May 24, 1951, the Commission filed a memorandum wherein it argued that the new rule X-16B-6,33 effective since November 30, 1950, should be applied in computing the cost basis of the securities, rather than the formula used in the Steinberg case. Under that rule, the recovery would be much less than that claimed by the plaintiff. The application of the rule was attacked on the ground that its retroactive feature was unconstitutional. The Commission also urged that an earlier payment by the defendant of less than that owed to the corporation was immaterial, the corporation being unable to satisfy a claim so as to prevent stockholders' actions arising under section 16 (b); and that the acquisition, by other defendants, of shares of Federated's common stock by the exchange of their holdings in Federated's subsidiaries for shares in Federated, would constitute a ^purchase" of stock within the meaning of section 16 (b). After the close of the fiscal year, the court rendered a decision upholding the Commission's contentions.

The case of *Gratz, et al, v. Claughton* [187 F. 2d 46 (C. A. 2, 1951) cert, denied, 341 U. S. 920 (1951)] reaffirmed the principle of computation established in *Smolowe y. Delendo Corporation* [136 F. 2d 231 (C. A. 2, 1943) cert denied, 320 U. S. 751 (1943)] to the effect that, in the case of trading subject to section 16 (b), maximum profits are required to be returned to the corporation. The court also upheld the Commission's contention that a proper venue was New York where the securities were traded on the New York Stock Exchange, as well as in a district where the defendant is found or is an inhabitant or transacts business. Certiorari was denied by the Supreme Court.

In *Rattner v. Lehman, et al.* [98 F. Supp. 1009 (D. C. S. D. N. Y. 1951)] the question arose as to what portion of the profits of a partnership earned by trading in the securities of a corporation in which one of the partners was a director, was recoverable. It was decided that the partnership's profits, except for the director's proportionate share, could not be recovered by the corporation. An appeal was taken subsequent to the close of the fiscal year. Similar problems were involved in *Eversharp, Inc., et al. v. Bobbins* [S. D. N. Y. Civil Action No. 46-225, Nov. 20, 1950] but negotiations between the parties resulted in a settlement of the case.

PART III

ADMINISTRATION OF THE PUBLIC UTILITY HOLDING COMPANY ACT OF 1935

The Public Utility Holding Company Act of 1935 was passed by the Seventy-fourth Congress following an extensive investigation by the Federal Trade Commission. That investigation disclosed a variety of abuses in public-utility holding company finance and operations, the more significant of which are enumerated in section 1 (b) of the act: (1) Inadequate disclosure to investors of the information necessary to appraise the financial position and earning power of the companies whose securities they purchase; (2) the issuance of securities against fictitious and unsound values; (3) the overloading of operating companies with debt and fixed charges thus tending to prevent voluntary rate reductions; (4) the imposition of excessive charges upon operating companies for various services such as management, supervision of construction and the purchase of supplies and equipment; (5) the control by holding companies of the accounting practices and rate, dividend and other policies of their operating subsidiaries so as to complicate or obstruct State regulation; (6) the control of subsidiary holding companies and operating companies through disproportionately small investment; (7) the extension of holding company systems without relation to economy of operations or to the integration and coordination of related properties.

In this section the Congress expressly stated that it was the policy of the act, in accordance with which all other sections are to be construed, to meet the problems and eliminate the evils enumerated above.

The regulatory provisions of the Holding Company Act fall principally into three basic categories: (1) Those designed to bring about geographical integration and the financial and corporate simplification of public-utility holding company systems; (2) the day-to-day surveillance of the financing, servicing arrangements, intercompany transactions and other operations of those registered holding company groups which will continue under the active regulatory jurisdiction of the Commission as integrated regional utility systems; and (3) miscellaneous provisions of the act, not concerned with regulation of the continuing systems, but designed principally to control the growth of additional holding company situations. The act does not confer any rate-making authority upon the Commission; in the over-all its purpose is not to conflict with but to supplement and strengthen State regulation.

INTEGRATION AND SIMPLIFICATION -- OVER-ALL SUMMARY

By the time the statute was enacted in 1935, the holding company device had attained a position of dominance over the major portion of the electric and gas utility industry of the country. Fifteen holding companies controlled 80 percent of all electric energy generation; 20 controlled 98.5 percent of all transmission of electric energy across State lines; and 11 controlled 80 percent of all natural gas pipeline mileage. The properties

acquired by these vast combinations, not only in the utility field, but also in many other types of business, were frequently widely scattered and bore little or no functional relationship to one another. The over-all impact of the act upon this structure has been reflected in the return to independent ownership of large numbers of electric and gas utility and other utility companies, the elimination of large numbers of multi-tiered holding companies, the consolidation of many corporations, and the dissolution of many others.

At one time or another from June 15, 1938, to June 30, 1951, a total of 2,175 companies have been subject to the active regulatory jurisdiction of the Commission as components of registered holding company systems. Of this number 211 were holding companies, 925 were electric or gas utility companies, and 1,039 were utilities other than electric or gas and a wide variety of other enterprises. The latter included brick works, ice plants, movie theatres, laundries, and even a baseball club. By the close of the past fiscal year there were but 444 companies subject to regulation, including only 64 holding companies, 195 electric and gas utilities, and 185 non-utility companies.

(charts omitted)

An even more revealing aspect of this achievement is the elimination from the national scene of holding company scatteration, stretching in some instances from coast to coast and from the Canadian border to the Gulf. This drastic realignment is reflected in the following table setting forth the number of states in which registered holding company systems conducted utility operations as of July 1, 1940, when the section 11 program was getting under way, and as of June 30, 1951. Upon completion of section 11 cases now in progress, the latter figures will be reduced still further.

(chart omitted)

While the scaling down of holding company systems during the past 15 years has been spectacular, the properties subject to the act on June 30, 1951, continued to represent an important segment of the electric and gas utility industries of the nation. As of that date, there were registered with the Commission 40 holding company systems with aggregate system assets of approximately $12,913,000,000, before deduction of valuation reserves. These figures may be compared with 46 registered systems and assets of $12,822,000,000 on June 30, 1950. The net increase of $91,000,000 during the year despite divestments of $104,782,000 is accounted for by the continuing growth of the industry. This high rate of expansion of plant facilities was occasioned initially by the almost uninterrupted increase in business activity since the close of World War II and more recently by the defense expenditures touched off by the Korean conflict. It is not expected to diminish to any great extent in the immediate years ahead.

The release from active regulatory jurisdiction of 1,731 corporate entities, however, falls far short of accounting for all of the progress achieved in the integration and

simplification of holding company systems under section 11 of the act. From December 1, 1935, to June 30, 1951, 240 companies with aggregate assets of $6,099,111,000, before deduction of valuation reserves, have been divested by holding companies, but, because of their relationships to other holding companies, remain subject to the jurisdiction of the Commission.

(chart omitted)

The great bulk of these companies and properties represents parts of holding company systems, such as American Gas and Electric Company, which either have achieved or are expected to achieve full compliance with the geographical integration and corporate simplification requirements of the act. It is not yet possible to calculate the final results of all section 11 problems which remain to be solved, but it is estimated that approximately 20 holding companies will emerge as streamlined, regional systems with some 250 companies and aggregate assets of $7,000,000,000, before deduction of valuation reserves. In addition there will be a number of other systems, such as Texas Utilities Company, which not only have complied with the standards of section 11, but also qualify for exemption under section 3 from nearly ail of the provisions of the act.

In addition to the drastic simplification of complicated corporate superstructures and the nation-wide realignment of utilities on an efficient, integrated, regional basis, the financial integrity of the industry has been greatly strengthened and utility investors have received "down-to-the-rails" income-paying securities of sound utility enterprises.

Operating utilities, which have been subject to the active regulatory jurisdiction of the Commission, have removed $1,500,000,000 of inflationary items from their property accounts as a result of the combined efforts of this Commission, the Federal Power Commission, and the various State commissions. Assuming an average allowed rate of return for rate-making purposes of 6 percent, this represents an aggregate annual saving to consumers of $90,000,000 and, in addition, has removed fictitious values which were misleading to investors.

Depreciation accruals and depreciation reserves have also been increased to more adequate levels thus strengthening the over-all asset protection of security holders. Summary data for all Class A and B electric utilities show an increase in depreciation and amortization reserves from 11.6 percent of total utility plant in 1938 to 20.5 percent at the close of 1950. [Footnote: Eight other electric companies with higher common equity ratios were also divested in the same period. However, because of their stronger equity position no corrective action m respect to capital structure was necessary.] Significant as this increase is, these figures do not reflect the full improvement -- the earlier figure being weighted by the large metropolitan companies most of whom had adequate reserves even at that time, while the latter figure relates to properties a substantial proportion of which has been added during the past decade and therefore possessing a

much longer anticipated life than the relatively old plant which the industry possessed in 1938, comparatively little capacity having been added during the depression years.

Despite the drastic elimination of inflationary items from plant accounts and increases in depreciation reserves, both of which tended to reduce common stock equity to an actual investment basis, the capital structures of many companies have undergone substantial improvement.

An adequate equity cushion to absorb the vagaries of business conditions is an important attribute of a good security. A computation has been made of the capital ratios of 18 electric utility companies released from Commission jurisdiction showing the marked improvement from 1940 to the date of release in the period 1946-48. [Footnote: Eight other electric companies with higher common equity ratios were also divested in the same period. However, because of their stronger equity position no corrective action m respect to capital structure was necessary.] As of 1940, and after adjustment for plant write-up eliminations, these companies had an average debt ratio of 61 percent, preferred stock 22 percent, and common stock and surplus of 17 percent. At the close of the year of their respective divestments, the average proportion of debt was reduced to 55 percent, preferred stock 16 percent, and common stock and surplus had increased to 29 percent.

The generally excellent financial condition of the electric and gas utility industries at the present time is indicated by the average capitalization percentages of the Class A and Class B electric utilities and straight natural gas operating utilities as of December 31, 1950, set forth in the following table:

(chart omitted)

One of the most unhealthy abuses uncovered by the Federal Trade Commission in its exhaustive investigation of holding company practices was the pyramiding device which enabled a few individuals to acquire control of large sections of the gas and electric utility industry. The real investors in the system who supplied the capital for the growth of the industry were effectively disfranchised by the pyramiding of holdings, and by such devices as voting trusts, the control of proxy machinery, interlocking directors and officers, management contracts, etc. This inequitable distribution of voting power was one of the evils which section 11 (b) (2) of the act was designed to eliminate. It led to excessive leverage and made it practically impossible for a security holder near the top of the pyramided structure to evaluate his holdings or to estimate the impact upon him of a slight change in the earnings of the underlying operating companies. Investors in the holding companies were in effect trading on the equity or buying on margin. Sometimes they made substantial profits during the 1920-1929 period of rising markets; but after the stock market crash of 1929 they had to pay dearly. Prior to the passage of the act in 1935, holding companies such as Foshay Company, Middle West Utilities Company, Tri-Utilities Corporation, Atlantic Gas and Electric Corporation, American Commonwealth Power Corporation, Utilities Power and Light Corporation, North American Gas and

Electric Company, Midland United Company, Midland Utilities Company, Standard Gas and Electric Company, Associated Gas and Electric Company, etc., were either in acute distress or in bankruptcy or receivership.

The failure of the pyramiding device is illustrated graphically in the fate of investors who placed their funds in "preferred" stocks of holding companies. As of December 31, 1940,3 preferred stocks of holding companies had a total face value (on the basis of involuntary liquidation preference) of $2,501,723,000; of this total, more than half, or $1,442,168,000 were in default. The total outstanding arrears on holding company preferred stocks, as of this date, aggregated approximately $476,000,000.

Mismanagement and exploitation of operating companies by holding companies, through excessive service charges, excessive common stock dividends, upstream loans, other extortionate inter-company transactions, and an excessive proportion of senior securities, led to serious defaults even on operating company preferred stocks. Of preferred stocks of operating companies in holding company systems totaling $1,658,677,000 (involuntary liquidation preference) at December 31, 1940, approximately $453,434,000 were in default. Total outstanding arrears on such operating company preferred stocks aggregated $165,176,000.

By June 30, 1951, this condition had been largely cured and, at the operating company level, there are virtually no preferred dividend arrearages or defaults on indebtedness in the electric and gas utility industries today. Furthermore, both industries have been able to finance successfully a post-war expansion program of unprecedented proportions now running at over $2,500,000,000 per year.

There have been some securities, of course, which never had any real basis of value even at the time of their original issuance, and quite naturally these received no participation in the final stages of reorganization of the holding company systems. On the whole, however, most holders of the junior and senior securities of holding companies not only have not lost in the reorganization and realignment process, but they have reaped substantial gains in the bargain.

Perhaps the best means of illustrating this is to examine the situations with respect to some of the larger holding company systems which have undergone drastic reorganization, including, in some instances, dissolution of the holding company. The following table shows the market values of their common stocks as of the date when each such holding company registered under the act, and of a recent date, September 24, 1951. In the table the figure for the earlier of the two dates represents the market price per share of common stock multiplied by the number of common shares then outstanding. The figures relating to the current date represent the market price per common share as of such date multiplied by the number of common shares then outstanding (excluding additional shares, if any, issued between the two dates), plus (1) the amounts of cash distributions of capital to the holders of such shares; (2) the market values, as of the

current date, of portfolio securities distributed to the common stockholders as capital distributions (excluding dividends in kind distributed in lieu of ordinary cash dividends); (3) the excess of the current market value of portfolio securities offered to security holders on rights over the price at which such rights could have been exercised by the security holders; and minus (4) amounts paid to the holding company by the common stockholders,, in several instances, directly in cash or indirectly as withheld dividends, in order to procure a capital distribution. The table also sets forth comparative increases in the Dow Jones Utilities Averages and the Dow Jones Composite Averages (based on industrials, rails and utilities).

As noted, the percentages of increase in market values of the common stocks listed in the table are derived from a comparison of market values obtaining at different dates of registration with those obtaining at a single current date. In some cases, general market conditions varied materially at the different registration dates, as indicated by the varying Dow Jones index figures. Accordingly, the comparative performances of these common stocks should not be measured against one another. Rather, they should be compared with the performances of the Dow Jones index figures for the same periods of time, thereby eliminating the effects of general market improvement during such periods.

It is quite apparent from the foregoing table that common stockholders of holding companies have generally benefited from the reorganizations accomplished pursuant to section 11 of the Holding Company Act. The lower percentage increases in some cases may be explained, at least in part, by the relatively better financial condition of those systems at the time of registration.

The benefits of reorganization, however, have not been limited only to common stockholders. Senior security holders have likewise been materially aided by these same reorganizations. To demonstrate this, there is tabulated below the market values of the debt securities and preferred stocks of these same holding companies as at the dates the companies registered under the act, and the capital distributions of cash and securities, taken at market values as at September 24, 1951, made to these senior security holders in retirement of their securities. The notes appearing at the end of the table show accumulated dividend arrears on the preferred stocks which were eliminated in the course of the reorganizations.

(chart omitted)

INTEGRATION AND SIMPLIFICATION -- SURVEY OF INDIVIDUAL SYSTEMS

During the past fiscal year the program of enforcement of the integration and simplification requirements of section 11 has continued unabated. A major portion of this streamlining and realignment process which has contributed so much to the revitalization

of the utility industry is now complete and many of the accomplishments of the past year represent the final culmination of several previous years of work. For example, National Power & Light Company completed the divestment of its subsidiary companies and is no longer a registered holding company. Reorganization of Washington Gas and Electric Company was effected in the fall of 1950 with the divestment of its holdings in Southern Utah Power Company through distribution of the common shares to its bond holders and general creditors. After five years of intermittent proceedings under section 11 (b) (2), Eastern Gas & Fuel Associates consummated its financial reorganization plan, and its parent holding company, Koppers Company, Inc., has reduced its stockholdings in Eastern to less than 5 percent. Long Island Lighting Company also completed its reorganization into a single operating company and, since the close of the fiscal year, has been granted an order under section 5 (d) thereby ceasing to be a registered holding company. Another accomplishment of the year was the successful reorganization of Pittsburgh Railways Company with the newly reorganized company replacing more than 50 predecessor companies. [Footnote: This contraction is not reflected in the divestment data tabulated above, but it is reflected in the dissolutions and consolidations of companies shown in the table on page 4 supra. It accounted for half of the total reduction in the numbers of companies subject to the act from 543 on June 30, 1950, to 444 on June 30, 1951.]

The number and asset volume of divestments for the past fiscal year was substantially smaller than for the previous period which had witnessed the consummation of reorganization and dissolution plans in several of the largest systems. A decline in the volume of divestments can be expected as the work of integration and simplification nears completion. During fiscal year 1951, 16 companies with assets of $103,740,000 were divested and are no longer subject to the Holding Company Act. In comparison, 78 companies with assets of $2,231,000,000 were divested in the preceding year.

Despite the overall progress witnessed during the past 15 years, however, a substantial volume of work remains to be accomplished. Final disposition is yet to be worked out with respect to nearly 200 companies with aggregate assets of almost $6,000,000,000. [Footnote: Before deduction of valuation reserves.] Among the systems which still presented major section II problems on June 30, 1951, were the following:

American Natural Gas Company (retainability of Milwaukee Solvay Coke Company).

American Power & Light Company (disposition of Washington Water Power Company and Portland Gas & Coke Company).

Central Public Utility Corporation (merger of Consolidated Electric & Gas Company into Central Public Utility Corporation and other problems).

Cities Service Company (simplification of the corporate structure of Arkansas Natural Gas Company and redistribution of voting power among its security holders; retainability of other gas utility properties in the Cities Service system).

Eastern Utilities Associates (reorganization of the system). Electric Bond and Share Company (retainability of its holdings in United Gas Corporation; reorganization of American & Foreign Power Company).

General Public Utilities Corporation (divestment of properties not retainable under the provisions of section 11).

International Hydro-Electric System (section 11 (d) proceedings).

New England Electric System (disposition of non-retainable gas properties).

New England Public Service Company (liquidation and dissolution).

Pennsylvania Gas & Electric Corporation (liquidation and dissolution).

Southwestern Development Company (simplification and integration) .

Standard Power & Light Company and Standard Gas & Electric Company (numerous problems including the retirement of the preferred stocks of Philadelphia Company and the preferred of Standard Power and Standard Gas; final disposition of all holding companies in the system).

Wisconsin Electric Power Company (problem related to the retainability of the system gas properties).

Several additional systems have unresolved section 11 problems relating to the retainability of gas or transit properties in combination with electric operating facilities.

A review of accomplishments of the major systems in effecting compliance with section 11 during the past fiscal year is set forth in the following summary descriptions.

American Power & Light Company

On August 22, 1942, American Power & Light Company ("American") then a subholding company subsidiary of Electric Bond and Share Company ("Bond and Share"), was ordered to dissolve, because its existence constituted an undue and unnecessary complexity in the Bond and Share system. At the time of the issuance of this dissolution order American controlled directly or indirectly 35 subsidiaries, 16 of which were public utility companies. American's capital structure then consisted of long term debt, two classes of cumulative preferred stock with heavy dividend arrearages, and common stock.

By the beginning of the fiscal year American had completed the major phases of its program of compliance with section 11. The steps taken are reported in the 15th and 16th Annual Reports. At present American controls only two utility subsidiaries, The Washington Water Power Company ("Washington") and Portland Gas & Coke Company ("Portland").

On February 15, 1951, American notified the Commission of its intention to negotiate for the sale of either the common stocks or the utility assets of Washington to Public Utility Districts located in the State of Washington. American was prevented from consummating the proposed sale, however, by the issuance of a decree by the Superior Court of the State of Washington on March 28, 1951, prohibiting the Public Utility Districts from acquiring the common stock of Washington under the proposed transaction.

Subsequent to the close of the fiscal year American filed a section 11 (e) plan proposing a cash distribution of $2 per share to each of its common stockholders. In setting a hearing date on this new proposal the Commission specified that certain additional issues were to be considered. These issues include (a) what further steps should be taken by American in order to comply with the Commission's order of August 22, 1942, directing its dissolution, (b) whether the Commission should apply to an appropriate U. S. district court pursuant to section 11 (d) to enforce this order and (c) whether the Commission should approve some plan which would provide, among other things, for the distribution of American's holdings of the common stock of Washington to its stockholders.

After the close of the fiscal year (October 15, 1951) the Commission approved this plan and, in addition, ordered American to file within 20 days a plan providing for the distribution of Washington's stock, as proposed by resolution of the board of directors promptly after January 1, 1952, in the event that American had not by that date filed a notification of a proposed sale of such stock pursuant to Rule U-44 (c). [Footnote: Holding Company Act Release No. 10820.]

Portland, the other utility subsidiary of American, has had on file with the Commission an extensive plan of reorganization which would materially reduce the interest of American in this enterprise. After the close of the fiscal year (August 29; 1951) the Commission issued its findings arid opinion on this plan indicating that it would approve the proposal if amended to provide, among other things, that 90 percent of the new common stock of the reorganized company be allocated to the preferred stockholders, the balance to be allocated to American, owner of all of Portland's presently outstanding common stock. [Footnote: Holding Company Act release No. 10740.] The plan was so amended and later approved by the Commission. [Footnote: Holding Company Act release No. 10812.]

American & Foreign Power Company, Inc.

American & Foreign Power Company, Inc., ("Foreign Power"), is a sub-holding company in the Electric Bond and Share Company ("Bond and Share") system. It controls a mutual service company and more than 60 holding and operating utility companies located throughout Central and South America, Cuba, Mexico, and India. Since the operations of all of Foreign Power's subsidiaries are outside of the United States, the Commission's principal concern is with respect to simplification of the company's corporate structure and its relationship to its parent, Bond and Share. Foreign Power's capital structure at December 31, 1950, consisted of debentures, notes payable to Bond and Share, notes payable to banks, three classes of preferred stock with dividend arrearages aggregating more than 433 million dollars, common stock and option warrants.

Foreign Power and Bond and Share jointly filed a plan for the reorganization of the former in October 1944, which after extensive hearings and amendments was approved by the Commission on November 19, 1947. [Footnote: Holding Company Act releases Nos. 7815 and 7849.] The plan was subsequently approved by the United States District Court for the District of Maine but the company was unable to effectuate the financing necessary to consummate the plan. For this reason both the district court and the Commission subsequently vacated their orders approving it. On May 2, 1949, the Commission issued an order pursuant to section 11 (b) (2) requiring Bond and Share and Foreign Power to take steps to reorganize the latter company in such a manner that its resulting capital structure would consist only of common stock plus such an amount of debt as would meet the applicable standards of the act. [Footnote: Holding Company Act release No. 9044.]

On January 16, 1951, Foreign Power, joined by Bond and Share, filed a new plan of reorganization under section 11 (e) of the act. [Footnote: Holding Company Act release No. 10362.] Extensive hearings were held during the fiscal year. Shortly after the close of the year, and after extensive negotiations between the companies and the organized security holders' committees who have appeared in the proceedings, a compromise was agreed to and an amendment to the plan was filed reflecting that compromise. The plan, as amended, provides for the following allocations for security holders other than Bond and Share; for each share of $7 Preferred stock -- $90 principal amount of new 4.8 percent Junior Debentures and 3.75 shares of new common stock; for each share of $6 Preferred stock -- $80 principal amount of new 4.8 percent Junior Debentures and three shares of new common stock; for each share of Second Preferred stock, Series (A) $7 -- 0.85 of a share of new common stock; for each share of outstanding common stock -- l/50th of a share of new common stock.

The option warrants are to be cancelled. Bond and Share would receive 3,856,723 shares (55.7 percent) of the new common stock for its present holdings of Foreign Power securities, including $49,500,000 of notes due 1955 and sizeable amounts of the various classes of preferred stock, common stock and option warrants presently outstanding.

Hearings on the plan, as amended, were completed after close of the fiscal year and the Commission thereafter approved the plan.

Cities Service Company

Cities Service Company ("Cities") at the time of its registration in 1941 was the top holding company in a system containing 125 companies of which 49 were electric and gas utility companies. Consolidated assets totaled approximately one billion dollars. This system owned or operated properties in each of the 48 States and in several foreign countries. Utility properties were held by three sub-holding companies, Cities Service Power & Light Company, Federal Light & Traction Co. and Arkansas Natural Gas Corp., each controlling one or more utility systems.

In proceedings under section 11 (b) of the act the Commission found that Cities should be limited in its operations to those of a single integrated gas utility system and required the disposition of its other interests. [Footnote: Holding Company Act releases Nos. 4489 and 4551.] However, Cities expressed a desire to retain instead its non-utility businesses and, accordingly, the Commission modified its section 11 (b) (1) order so as to permit Cities to effectuate compliance by disposing of all of its utility interests. [Footnote: Holding Company Act release No. 5350.]

Cities Service Power & Light Company was liquidated and dissolved in August 1946, and its portfolio holdings were at that time transferred to Cities. Federal Light & Traction Company had also substantially completed liquidation proceedings.

On February 9, 1949, the Commission instituted proceedings with respect to Arkansas Natural Gas Corp., the third subholding company, and Cities under section 11 (b) (2) and other sections of the act raising issues among others, with respect to the corporate structure of Arkansas Natural, distribution of voting power among its security holders, and with respect to the organization and history of Arkansas Natural and the relation of Cities Service thereto. [Footnote: Holding Company Act release No. 8842.] Arkansas Natural filed a plan under section 11 (e) on January 26, 1950, designed to effectuate compliance with the requirements of section 11 (b). [Footnote: Holding Company Act release No. 10372.] It provided, among other things, for simplification of the company's corporate structure and for the disposition by Arkansas Natural Gas, as a partial liquidating dividend, of its stockholdings in Arkansas-Louisiana Gas Company. Its other subsidiary, Arkansas Fuel Oil Company, will be merged into Arkansas Natural Gas. The plan treats the holdings of Cities on the same basis as the holdings of the public security holders in Arkansas Natural Gas. One of the issues presently being considered in connection with the fairness of the proposal is whether there is any basis for requiring the subordination of the interest of Cities or of any other stockholder to the interests of other security holders of Arkansas Natural Gas. A number of hearings have been held, but at the close of the fiscal year the record had not been completed.

Cities consummated the simplification of its capital structure in 1947, and eliminated three series of preferred and preference stocks with accumulated dividend arrears of approximately $50,000,000. Since that time it has disposed of its direct interest in the common stock of several utilities including Public Service Company of New Mexico, Ohio Public Service Company and The Toledo Edison Company, applying the proceeds derived from the sales of these holdings to the reduction of its debenture indebtedness. At the close of the fiscal year the Cities system included 59 corporate entities. However, of this number only seven companies were engaged in utility operations.

Eastern Utilities Associates

Eastern Utilities Associates ("EUA") is a Massachusetts voluntary association having three direct subsidiary companies, Blackstone Valley Gas & Electric Company ("Blackstone"), Brockton Edison Company ("Brockton") and Fall River Electric Light Company ("Fall River") and one indirect generating subsidiary company, Montaup Electric Company ("Montaup"). During the past fiscal year the corporate changes and expansion program of this system were closely associated with the major reorganization plan now on file with the Commission.

After extensive proceedings, the Commission issued an order under section 11 (b) on April 4, 1950, which provided, in part, that EUA shall, within one year, terminate its existence and distribute its assets to its shareholders pursuant to a fair and equitable plan or, within one year, acquire a minimum of 90 percent of the outstanding common stock of all of its subsidiary companies and reclassify its common and convertible shares into a single class of stock. The order further provided, in effect, that in the event of the adoption of the latter alternative, EUA, within the one year period, would sever its ownership or control of the gas utility properties owned by Blackstone. [Footnote: Holding Company Act release No. 9784.]

On May 17, 1950, EUA filed its reorganization plan under section 11 (e) for the purpose of complying with this order. After public hearings, step 1 of the plan was approved by the Commission on August 17, I960. [Footnote: Holding Company Act release No. 10040.] EUA borrowed $9,094,000 on short term promissory notes and, with the proceeds, acquired from the New England Electric system its interest in Fall River consisting of 118,161 shares of capital stock. In addition, it acquired 11,721 shares held by the public. As a result EUA now holds 98.5 percent of the total voting power of Fall River. EUA has also caused to be organized a new holding-operating company, named Eastern Edison Company, for the purpose of acquiring the properties and assets of EUA, Brockton, Fall River and Montaup and holding the securities of Blackstone.

The subsequent permanent financing of Eastern Edison Company will require the issuance of approximately $44 million of securities. The plan contemplates that $28 million will be raised through the public sale of bonds, $12,500,000 through the sale of preferred stock, and $3,500,000 through bank borrowing. Eastern Edison Company also

proposes to acquire the capital stock held by minority stockholders of its subsidiary companies. Thereafter EUA proposes to distribute to its common and convertible shareholders the new common stock of Eastern Edison. EUA will then transfer its remaining assets to Eastern Edison and dissolve.

Hearings on the amended reorganization plan were reconvened in May, 1951.

Electric Bond and Share Company

The Electric Bond and Share Company ("Bond and Share") system was the largest to register under the act. At the time of its registration in 1938, it controlled 121 domestic subsidiaries including five major subholding companies with combined assets of nearly $3,500,000,000. These subholding companies were American & Foreign Power Company, Inc. ("Foreign Power"), American Gas and Electric Company ("American Gas"), American Power & Light Company ("American Power"), Electric Power & Light Corporation ("Electric Power") and National Power & Light Corporation ("National Power"). Bond and Share has disposed of its holdings in American Gas and National Power. Electric Power has been dissolved and has been succeeded by Middle South Utilities, Inc., which like American Gas is expected to remain as a registered holding company. [Footnote: These companies are discussed in the following section entitled "Progress of Continuing Holding Company Systems."] American Power has been partially liquidated and Bond and Share now holds 7.8 percent of its new common stock. Proceedings with respect to Foreign Power, in which Bond and Share continues to hold a substantial interest, are pending before the Commission and are described above under a separate heading.

As indicated in the 16th Annual Report, the Commission issued an order on June 19, 1950, directing the Bond and Share pay to holders of certificates issued in respect to the $6 preferred stock an amount of $10 per share plus interest of 5.45 percent as compensation for delay in payment and that no further payment should be made to holders of certificates issued in respect to the $5 preferred stock. Payments totaling $100 per share had previously been made to holders of both classes of preferred stock. Following unsuccessful appeals from the Commission's order by the company, Bond and Share paid an aggregate of $12.34 per share to certificate holders in respect to the $6 preferred stock, thus completing the final step in the reorganization of the company's capital structure to a one-stock basis. [Footnote: In re Electric Bond and Share Co., 95 F. Supp. 492 (S. D. N. Y., 1951), cert, denied. Electric Bond and Share Co. v. S. E. C., 341 U. S. 950 (1951).]

In the past Bond and Share had filed plans with the Commission contemplating the divestment of all of its public utility holdings in the United States in order that its status might be changed to that of an investment company. It has applied for relief, however, from its commitment to dispose of the stock of United Gas Corporation ("United"), a large gas utility system, received by it in connection with the dissolution of Electric

Power. Hearings with respect to this request have been concluded and the matter has been submitted to the Commission for decision.

In February 1950, Bond and Share acquired upon the reorganization of American Power common stocks of that company's subsidiaries, Florida Power & Light Company ("Florida"), Montana Power Company ("Montana"), Minnesota Power & Light Company ("Minnesota"), Texas Utilities Company ("Texas") and new common stock of American. Power with a commitment to dispose of all of these holdings within one year. During the past fiscal year all shares of Texas Utilities and Minnesota Power and a portion of its holdings in Florida and Montana have been sold or distributed. At June 30, 1951, Bond and Share still held 18,709 shares of Florida and 138,708 shares of Montana which it expects to dispose of before the close of 1951. An extension of time has been requested in respect to the disposition of its holdings of 183,050 shares of American Power.

United and its subsidiaries are presently engaged in a construction program which will require the expenditure of approximately $170 million during the years 1951 and 1952. The major item of this program relates to the construction of more than one thousand miles of large diameter pipe line to be built as a grid over the present system in order to provide a more balanced withdrawal and distribution of gas supply from presently connected and newly developed fields, to increase the flexibility of the present system, and to enable United to meet increased gas requirements of present customers and new customers which it proposes to serve.

On March 23, 1951, the Commission approved a joint application of United and its subsidiary, United Gas Pipe Line Company ("Pipe Line"), permitting United to undertake temporary short term bank borrowing up to $25 million, the proceeds to be used to purchase $25 million of Pipe Line's first mortgage bonds. [Footnote: Holding Company Act release No. 10463.] In May 1951, approval was given to certain proposals of United and its two subsidiaries, Pipe Line and Union Producing Co. ("Union"), providing for the issuance by Pipe Line to United of $48,127,000 of mortgage bonds due in 1971, in exchange for United's holdings of similar amount due 1962. United also extended to 1971 the due date on $34 million of outstanding debentures issued by Union and owned by United. [Footnote: Holding Company Act release No. 10581.]

On June 21, 1951, a number of major financing transactions designed to finance a portion of the proposed construction program were approved by the Commission. [Footnote: Holding Company Act release No. 10636.] It authorized (1) the issuance and sale by United, pursuant to a rights offering to its stockholders, of 1,065,330 shares of new common stock; (2) the issuance and sale by United of $50 million principal amount of first mortgage bonds; (3) the issuance and sale by Pipe Line to United of $25 million principal amount of Pine Line's first mortgage bonds and $45 million of its sinking fund debentures; (4) the repayment by Pipe Line to United from the proceeds of the sales of securities of $7 million of unsecured indebtedness.

The rights offering to United stockholders was made on June 29, and Bond and Share was permitted to acquire its proportionate share of the new offering, 287,065 shares, and to exercise its oversubscription privilege if available. The offering was heavily oversubscribed. The public offering of $50 million of United first mortgage bonds was consummated on July 26, 1951.

On June 28, 1950, Bond and Share and United entered into a contract with National Research Corporation ("National Research"), a non-affiliated company engaged in industrial research. The contract was not to become effective, however, until either approved by the Commission or declared not subject to its jurisdiction. Under the terms of the contract, which will expire on December 31, 1955, National Research will engage in certain research work in an effort to develop new processes or products based on natural gas and its constituents. Such services are to be performed by National Research at cost plus certain amounts for overhead, such costs to be shared equally by Bond and Share and United. The contract provides that Bond and Share and United, between them, are committed to expend in each year on work to be done by National Research minimum amounts ranging from $150,000 in 1950 to $250,000 in 1955.

Bond and Share, while urging approval of the contract on its merits, questioned the jurisdiction of the Commission in this matter. The Commission found, however, that the venture provided for by the contract and the interests of Bond and Share and United therein clearly fall within the purview of sections 9 (a) (1) and 12 (f) of the statute. As previously indicated, the retention of United common stock by Bond and Share is before the Commission for determination. In advance of such determination, the Commission approved the proposed research program on condition that if Bond and Share is subsequently denied relief from its commitment to dispose of the common stock of United it will forthwith withdraw from and terminate all interest in the research contract. [Footnote: Holding Company Act release No. 10237.]

On July 11, 1950, Bond and Share entered into an agreement with a non-affiliated holding company, The Southern Company ("Southern") , which provided for the acquisition by Southern and the sale by Bond and Share of the latter's holdings of 254,045 shares of the common stock of Birmingham Electric Company ("Birmingham") in exchange for 381,067-1/2 shares of the common stock of Southern. Southern proposed to merge the electric properties of Birmingham with those of its subsidiary, Alabama Power Company and cause Birmingham to divest itself of its transportation properties to non-affiliated interests. The proposal would not constitute a complete divestment by Bond and Share of Birmingham since it would permit Bond and Share to continue with an indirect interest in that company through ownership of Southern's common stock.

On August 24, 1950, the Commission issued an order approving the proposed transaction but requiring, among other things, that Bond and Share divest itself of any direct or indirect interest in the common stock of Southern within one year from the date of acquisition. The order also required the disposition of Birmingham's transportation

properties within one year from the date of the acquisition by Southern of the Birmingham stock. [Footnote: Holding Company Act release No. 10055.]

In January 1951, Bond and Share's subholding company subsidiary, National Power & Light Company ("National Power") effected the divestment of its subsidiary, Lehigh Valley Transit Company, together with its four subsidiary transportation companies. The properties were sold for $810,500 to the Cincinnati, Newport and Covington Railway Company, a non-affiliated enterprise. During subsequent months National Power also disposed of its remaining stockholdings in Pennsylvania Power & Light Company and reduced its assets to a limited amount of cash and cash items. On June 26, 1951, the Commission issued an order approving a plan by which Bond and Share sold its common stock holdings of National Power to Phoenix Industries Corporation ("Phoenix"). [Footnote: Holding Company Act release No. 10640.] This corporation is a closely-held corporation formed primarily to engage in, or to invest in, other companies which engage in commercial activities considered to have good prospects for growth, development and expansion. Its desire to acquire a controlling interest in National Power was related to the large number of the latter company's stockholders, its listing on the New York Stock Exchange and the fact that its assets consisted entirely of cash available for investment. It was indicated that Phoenix upon acquisition of National Power would cause National Power to invest in companies of the same general character as those in which Phoenix plans to invest and that neither company will, directly or indirectly, invest in public utility companies.

In its order approving the sale of stock by Bond and Share the Commission modified the dissolution order directed to National Power so as to permit the continued existence of that company and indicated that, upon consummation of the sale, National Power will have ceased to be a holding company pursuant to section 5 (d) of the act.

General Public Utilities Corporation

This company is the top holding company emerging from reorganization of the former Associated Gas and Electric Company system. Reference is made to the 15th and 16th Annual Reports which outline briefly the steps taken in earlier years to bring about integration and simplification of this highly complex structure. In 1938 this system consisted of 164 companies including 11 subholding companies operating in 26 States and in the Philippine Islands. While the present holding company system controlled by General Public Utilities Corporation ("GPU") represents but a segment of the former Associated system, certain problems remain to be resolved before it can be brought into complete conformity with the standards of section 11.

In May 1951, hearings on the company's section 11 (b) (1) proceedings were concluded. The Division of Public Utilities of the Commission at that time indicated its view: (1) that the electric, coal mining, water, and steam heating properties of Jersey Central Power & Light Company, Metropolitan Edison Company, New Jersey Power & Light Company,

and Pennsylvania Electric Company (other than minor steam heating properties of the latter company located at Clearfield, Pa.) constitute a single integrated electric utility system and reasonably incidental businesses, and are retainable by GPU; (2) that the properties of Northern Pennsylvania Power Company and of its subsidiary, The Waverly Electric Light & Power Company, the gas properties of Jersey Central Power & Light Company, and the steam heating properties of Pennsylvania Electric Company referred to above are not retainable under the standards of section 11 (b) (1) of the act; and (3) that the Commission's order of August 13, 1942, directing, among other things, the divestment by GPU of its interest in the Philippine subsidiaries should be reinstated forthwith. At the same time, GPU indicated that it was not opposed to the prompt entry by the Commission of an order embodying the views of the division. After the close of the fiscal year the Commission entered such an order.

Construction requirements during the past year have made it necessary for the GPU system to undertake the issue and sale of 504,657 shares of its common stock through a rights offering to its common stockholders. This offering was made on June 16, 1951. Gross proceeds amounted to approximately $8,365,000. [Footnote: Holding Company Act release No. 10622] These funds, less fees and expenses, are being employed by GPU for investment in the common stocks of its domestic utility subsidiaries to meet their expansion requirements. GPU has also made capital contributions to certain subsidiaries from treasury cash. In addition, its domestic subsidiaries sold to the public $5,750,000 of mortgage bonds and $2 million of preferred stock. Virtually all of the proceeds derived from these sales have also been applied to meet construction requirements.

International Hydro-Electric System

At the time of registration International Hydro-Electric System ("IHES"), a Massachusetts voluntary association, owned directly Gatineau Power Company ("Gatineau"), a Canadian public utility company, and two wholesale electric utilities operating in the United States. It also owned the equity in New England Power Association which, since its reorganization, is known as New England Electric System. IHES is now in process of liquidation and dissolution under section 11 (d) of the act. It functions under the authority of Bartholemew A. Brickley as trustee, who was appointed by the United States District Court for the District of Massachusetts in November 1944.

Earlier steps taken toward the eventual liquidation and dissolution of IHES are described briefly in the 15th and 16th Annual Reports. On April 19, 1949, the Trustee submitted a "Second Plan" of four parts to effect the eventual liquidation and dissolution of IHES and on July 1, 1949, after approval of the Commission, Part I of the plan was consummated. [Footnote: Holding Company Act release No. 9120] This consisted of a partial payment on outstanding 6 percent debenture indebtedness in default since 1944, reducing the outstanding principal amount of each $1,000 debenture from $700 to $600. At the close of the last fiscal year the trustee was also authorized to consummate Part II of the plan and retired the company's 6 percent debentures by repaying the balance of $15,940,800

($600 per debenture) which was then outstanding. The requisite amounts of cash were obtained through the exchange or sale of 340,000 common shares of Gatineau and through consummation of a bank loan of $9,500,000. [Footnote: Holding Company Act releases Nos. 9535 and 9917]

Hearings were resumed in November 1950, on Part III of the Trustee's Second Plan in which it is proposed to retire the preferred and class A stocks of IHES by issuing in exchange therefor eight trustee certificates for each preferred share and one trustee certificate for each class A share. Under Part IV of the Trustee's plan, a 60 day takedown privilege would be afforded to the certificate holders, under which each certificate holder would be permitted to pay his aliquot share of the Trustee's net obligations including the bank debt and receive his aliquot share of the portfolio assets. Thereafter, the balance, if any, due on the bank debt would be satisfied by a sale of assets, the expenses of administration would be paid, the remaining assets would be ratably distributed and the holding company would be dissolved.

Hearings on Part III of the Trustee's plan and various counterproposals were closed on February 20, 1951. At the end of the fiscal year the staff filed its recommendations indicating that Part III would be fair and equitable if amended to provide seven trustee certificates in exchange for each preferred share and one trustee certificate for each class A share. It was recommended that other counter-proposals be disapproved. All parties have been given an opportunity to file objections to the staff recommendations and at the close of the fiscal year the matter had not yet been argued orally before the Commission. In a collateral proceeding, the Trustee applied for authorization to make quarterly payments of 87 1/2 cents per share to the preferred stockholders pending final liquidation. No dividends have been paid on the preferred stock since July 15, 1934. This request is pending before the Commission.

Koppers Company, Inc. Eastern Gas & Fuel Associates

Koppers Company, Inc., is a large industrial organization engaged in the production, manufacture, and sale of coal tar products, forest products, coke and gas, machine shop and foundry products, and in the design and construction of various types of coke ovens, chemical plants and other structures. It has been a public utility holding company by virtue of its stock ownership of Eastern Gas & Fuel Associates ("Eastern"). The latter company, which is engaged in a large measure in the production, transportation, sale and conversion of coal, is a public utility holding company because of its ownership of the outstanding voting securities of two gas utility companies operating in the Boston area.

Both Koppers and Eastern filed applications pursuant to section 3 of the act for orders exempting them and their subsidiaries from all provisions of the act because of the intrastate character of their utility operations and on the ground that they were only incidentally public utility holding companies. Subsequently, however, Eastern filed a notification of registration as a holding company which filing purported in substance to

limit the effect thereof to the corporate simplification provisions of the act and Koppers filed a notification of registration purporting to limit its effect to the geographic integration provisions of the act.

In proceedings subsequently instituted under section 11 (b) (1) of the act, the Commission, in June 1945, ordered Koppers with its consent to sever its relationship with Eastern and its subsidiaries by disposing of its security holdings of those companies. [Footnote: Holding Company Act release No. 5888]

In May 1945 the Commission also instituted proceedings under section 11 (b) (2) against Eastern and these proceedings were consolidated with those involving a plan filed by that company in the same year. [Footnote: Holding Company Act releases Nos. 5827 and 5877] The plan as originally filed provided for the retirement of Eastern's outstanding 6 percent cumulative preferred stock and common stock through the issuance of a new common stock, 85 percent of which was to be allocated to the preferred holders and 15 percent to the common stockholders. At the close of the hearings in January 1947, the allocation was amended to provide 79.01 percent for the preferred holders and 20.99 percent to the common stockholders. The record was closed in March 1947, but because of changed circumstances the hearings were reconvened in 1948 for the purpose of adducing additional evidence. [Footnote: Holding Company Act release No. 8096] On December 31, 1948, arrearages on the preferred stock amounted to $35.50 per share, aggregating $13,281,899.

In January 1949, Eastern again amended its plan by further reducing to 73.08 percent the proposed allocation of new common stock to the 6 percent preferred stockholders. The proceedings were the subject of vigorous disputes by various contending stockholder representatives. In February 1950, the Commission directed Eastern to reclassify the 6 percent preferred stock and common stock into one new class of stock and indicated that an 87 percent -- 13 percent allocation plan could be approved. [Footnote: Holding Company Act release No. 9633] Because of the wide fluctuations in Eastern's earnings due to changing conditions in the coal business, the Commission was confronted with a most difficult task in its evaluation of past and future prospects of the company necessary to determine the fairness of the allocation. The plan was subsequently amended to meet suggestions of the Commission and was approved in March 1950. [Footnote: Holding Company Act release No. 9725] In June the United States District Court for the District of Massachusetts entered its order approving the plan which was consummated in October 1950.

As a result of the plan Koppers' holdings of about 78 percent of Eastern's common stock and 13 percent of its preferred stock were converted into 22 percent of the new common stock. Through subsequent sales to various purchasers Koppers has reduced its holdings to 4.6 percent and is under order to divest itself of this remaining interest. The matter of Eastern's application for exemption from all provisions of the act is still pending before the Commission.

Mission Oil Company
Southwestern Development Company

The stock of Southwestern Development Company ("Southwestern") is owned 47.28 percent by Mission Oil Company ("Mission"), representing virtually the only assets of that company; 51 percent by Sinclair Oil Corporation ("Sinclair") and 1.72 percent by minority interests. Sinclair also holds about four percent of the stock of Mission. Mission and Southwestern are registered holding companies; Sinclair, primarily engaged in the production and refining of petroleum products, has been granted an exemption from the provisions of the act. [Footnote: 2 S. E. C. 165, sub nom. *Consolidated Oil Corporation*.]

At the time of its registration in 1936, the Southwestern system proper comprised seven wholly owned subsidiaries (four gas utilities, two small gas transmission companies and one natural gas production company) which supplied the natural gas requirements of about 50 communities in the Panhandle area of Texas. In addition to these operations, Southwestern had substantial interests in other important natural gas production and transmission companies. It held all of the capital stock of Canadian River Gas Company ("Canadian River") and a substantial interest in Colorado Interstate Gas Company ("Colorado"). These two companies are known as the "Denver line," constituting in effect a single operating and business unit. Southwestern also had at that time an interest in Texoma Natural Gas Company and Natural Gas Pipeline Company of America. These two companies, sometimes described as the "Chicago line," constitute a natural gas transmission system furnishing gas to Chicago and certain intermediate cities en route.

The Southwestern holdings remained without substantial change until 1947 when its interest in the two companies comprising "Chicago line" was sold to a non-affiliated company.

In June 1951, after numerous conferences with the staff, Mission and Southwestern filed with the Commission a section 11 (e) plan designed to conform its system to the integration and simplification requirements of the statute. In substance the plan provides that (a) Mission will be liquidated and Sinclair will divest itself of its stockholdings in Southwestern, (b) the rights to the natural gasoline in the natural gas reserves of Canadian River, "in place", will be transferred to a new company, the stock of which will be issued to Southwestern and distributed by it to its stockholders, (c) the two companies, Colorado and Canadian River, constituting the "Denver line," will be merged, (d) Southwestern will also distribute its holdings of stock in the merged Colorado-Canadian River Company to its stockholders and (e) for purposes of facilitating these proposed distributions, Southwestern and Colorado will reclassify their outstanding common stocks. The Commission has instituted cross-proceedings under sections 11 (b) (1) and 11 (b) (2) and hearings upon the consolidated matters were initiated early in August 1951. [Footnote: Holding Company Act release No. 10668]

If this plan is successfully consummated Southwestern will remain with its wholly owned subsidiaries including four gas utilities with a field of operations confined generally to the north Texas area. The stock of Southwestern will be publicly held.

New England Public Service Company

New England Public Service Company ("NEPSCO"), at the time of its registration,. had five major operating subsidiaries of which two operated in Maine, one in New Hampshire and two in New Hampshire and Vermont. It also owned through an industrial subsidiary, five textile mills, a paper company and a forest products manufacturing company. As a result of simplification proceedings instituted by the Commission under section 11 (b) (2), the company was directed in 1941 to reorganize on a one stock basis or in the alternative to liquidate and dissolve. The management of NEPSCO elected to liquidate and subsequent steps have been taken toward this end.

On June 19, 1950, the Commission reached its decision as to the amounts to be paid on the certificates of contingent interest issued in connection with the retirement of NEPSCO's Prior Lien Preferred Stock and it ordered that the $7 Series receive an additional payment of $12.25 per share and the $6 Series $2.25 per share, together with compensation for delay in payment at the rate of 5.5 percent per annum from October 10, 1947. [Footnote: Holding Company Act releases Nos. 9931 and 9982] The findings of the Commission with respect to these amounts were subsequently approved and enforced by the United States District Court for the District of Maine in November 1950. These sums represented the final payments in connection with retirement of the Prior Lien Preferred Stock.

Subsequently, the Commission and the court approved an amendment to the section 11 (e) plan of NEPSCO which provided for the reduction of its outstanding bank loan by the use of proceeds derived from the sale of 260,000 shares of common stock of Central Maine Power Company, renewal of the unpaid balance, and a program for full payment by October 11, 1952. The changes also included removal of restrictions on the payment of dividends on NEPSCO preferred stock and an accounting quasi-reorganization. [Footnote: Holding Company Act release No. 10087] Proceeds derived by NEPSCO from the sale of Central Maine Power Company common stock permitted a reduction in its bank loan of approximately $4 million. The company also applied $2,132,000 returned to it from funds deposited in escrow for payment of amounts found due on the preferred stock certificates of contingent interest. These payments, together with funds generated from current earnings, have brought the outstanding amount of the loan down to $1,310,000 at June 30, 1951.

In June 1951, NEPSCO filed a new plan providing for the distribution of its remaining assets to the holders of its junior preferred and common stocks and for its liquidation and dissolution. This plan is intended to effectuate complete compliance with the Commission's order of May 2, 1941. Superimposed on NEPSCO is Northern New

England, a voluntary association, which owns approximately one-third of NEPSCO's common stock. Northern New England is under Commission order to liquidate and dissolve, but it is awaiting consummation of a final plan by NEPSCO in which the participation to be accorded to the common stock of the latter company will be determined, before it can take the required steps to complete liquidation.

Pennsylvania Gas & Electric Corporation

Pennsylvania Gas & Electric Corporation ("Penn Corp"), which filed its registration statement with the Commission in November 1936, had at that time 19 subsidiary companies. Its utility operations were conducted in sections of New York, Pennsylvania, Massachusetts, Rhode Island and Virginia. The system included 15 gas utility companies, three wholesale gas companies and one service company. Three of the utility subsidiaries, North Penn Gas Company ("North Penn"), Pennsylvania Gas & Electric Company, name later changed to York County Gas Company ("York County"), and Saugerties Gas Light Company ("Saugerties") were also subholding companies.

In January 1942, the Commission instituted a proceeding under section 11 (b) (2) with respect to York County and Penn Corp. [Footnote: Holding Company Act release No. 3251] Thereafter, two subsidiaries were merged into York County and a recapitalization plan of that company was approved by the Commission in December 1944 providing for corporate simplification and a program of debt reduction. [Footnote: Holding Company Act release No. 5480] The plan was consummated during 1945 after approval by the United States District Court for the Middle District of Pennsylvania. Two of Penn Corp's Virginia subsidiaries were combined in 1944 and, in July 1946, this company was divested by Penn Corp. [Footnote: Holding Company Act release No. 6769]

In September 1948, the Commission issued an order pursuant to sections 11 (b) (1) and 11 (b) (2) directing Penn Corp to sever its relations with its subsidiaries, Newport Gas Light Company, York County and North Shore Gas Company, and to change its preferred and common stock to a single class of stock. [Footnote: Holding Company Act Release No. 8490]

Penn Corp disposed of its interest in North Shore shortly thereafter and, in 1949 and 1950, sold its holdings of York County and Newport. Its investment in another subsidiary, New Penn Development Corporation, was also sold during 1950. Subsidiaries in New York were merged into Crystal City Gas Company. An order of the Commission, dated December 22, 1949, approved this merger and also directed that Penn Corp liquidate and dissolve. [Footnote: Holding Company Act Release No. 9574] As a result of successive divestments and the merger, Penn Corp's holding company system was reduced to four gas companies operating in Pennsylvania, one company, Crystal City, operating in New York, and a mutual service company. The Pennsylvania companies were merged, as of December 31, 1950, into a single company, North Penn, with Crystal City as its sole subsidiary.

In the latter part of 1950, Penn Corp. sought the approval of this Commission with respect to a proposed sale of the capital stock of Crystal City to certain non-affiliated interests. After hearings thereon the Commission found that there had not been a maintenance of competitive conditions in the negotiations for such sale and disapproved the proposed transaction. [Footnote: Holding Company Act Release Nos. 10322 and 10613]

The final portion of Penn Corp's section 11 plan contemplates the liquidation and dissolution of that company and distribution of capital stock of North Penn pursuant to a proposed allocation to holders of Penn Corp preferred and Class A common stock. A cash payment of $0.10 per share is proposed for holders of the Class B common. Hearings on this proposal were concluded in July 1951.

Standard Power & Light Corporation
Standard Gas & Electric Company

The Standard holding company system presented, at the time of its registration, an extreme example of the evils of corporate pyramiding and scatteration of properties. In 1936, it consisted of 105 active companies operating in 20 states and in Mexico, including the two top holding companies, Standard Power & Light Corporation ("Standard Power") and its subsidiary, Standard Gas & Electric Company ("Standard Gas"). By June 30, 1951, the system had been reduced to 15 companies and further contraction is in prospect.

As reported in the 16th Annual Report, Standard Gas, in 1949, filed an amended plan for the simplification of the corporate structure of the system of its holding company subsidiary, Philadelphia Company ("Philadelphia"). Several provisions of the plan have already been carried out including the reorganization of the gas properties in the Philadelphia system under the ownership of Equitable Gas Company ("Equitable"), the sale of Equitable common stock and $11 million of debentures of Equitable held by Philadelphia, the retirement of Philadelphia's outstanding funded debt, amounting to approximately $36 million and the redemption of Philadelphia's $6 Preference stock, aggregating $10 million in par value. [Footnote: Holding Company Act Release Nos. 9740 and 9766] Pursuant to an amendment to the plan submitted on July 11, 1950, Duquesne Light Company ("Duquesne"), a subsidiary of Philadelphia, issued $19,500,000 of bonds and preferred stock to the public the proceeds of which were used to finance its construction program and to repay outstanding bank loans. The Duquesne five percent preferred stock, aggregating $27,500,000, was refunded by the issuance to Philadelphia of a new series of four percent preferred stock in consideration of $27,200,000 in cash and the transfer to Duquesne of all of the stock of Philadelphia's direct subsidiary, Cheswick and Harmer Railroad Company. [Footnote: Holding Company Act release No. 10044]

The amended plan as it now stands proposes that the Duquesne four percent preferred stock be used by Philadelphia in an exchange program to retire its own six percent preferred stock and the six percent preferred of Consolidated Gas Company of the City of Pittsburgh, an inactive subsidiary of Philadelphia, on which Philadelphia has guaranteed certain dividends. The proposed bases of exchange are: one share of Duquesne's four percent preferred stock together with $3.50 in cash, for each share of Philadelphia's six percent preferred ' and 0.85 of one share of Duquesne's four percent preferred for each share of Consolidated Gas preferred. The plan also provides that Philadelphia five percent preferred stock shall be retired by the payment of $11 in cash for each share and that its $5 preference stock be retired in a manner not yet specified. Aggregate par values of these various preferred stock issues is approximately $31,700,000.

Hearings before the Commission relating to the retirement of the six percent and five percent preferred stocks of Philadelphia and the preferred stock of Consolidated Gas were completed in April 1951 and the matter is now awaiting the decision of the Commission.

During the fiscal year, both Standard Gas and its parent Standard Power, were permitted by the Commission to withdraw their 1943 and 1944 section 11 (e) plans, which had been previously approved but never consummated. The Standard Gas plan which had provided for its recapitalization was allowed to be withdrawn because of changes in conditions occurring during the course of litigation. The Standard Power plan was allowed to be withdrawn because its provisions were linked to the consummation of the Standard Gas recapitalization. [Footnote: Holding Company Act releases Nos. 9960 and 10385]

In February 1951, Standard Gas filed a new section 11 (e) plan with the Commission. The plan includes four steps. Step I would effect the retirement-of Standard's $7 and $6 Prior Preferred stock; Step II is intended to effectuate the liquidation and dissolution of Standard Gas and the delivery to the holders of its $4 cumulative preferred stock and common stock, shares of Philadelphia Company common stock; Step III will eliminate the minor subsidiaries of Philadelphia and, if feasible, Pittsburgh Railways Company; and Step IV proposes either the dissolution of Philadelphia and the distribution to its common stockholders of its holdings of Duquesne or, if Pittsburgh Railways is not disposed of as part of Step III, the disposition by Philadelphia of most of its holdings in Duquesne and its continuance primarily as a holding company for Pittsburgh Railways until disposition of that company is accomplished. Hearings are currently being held on Step I of the plan.

Pursuant to Step III of the plan, the Commission, on July 3, 1951, approved a joint application by Philadelphia and Equitable Real Estate, a non-utility subsidiary, which provided for the transfer of all of Equitable's assets to Philadelphia and dissolution of the subsidiary. [Footnote: Holding Company Act release No. 10652] In a prior decision the Commission also approved the dissolution of Equitable Sales Company, another subsidiary of Philadelphia. That step was effected in December 1950. [Footnote: Holding Company Act release No. 10190]

In December 1950, Standard Gas finally liquidated its investments in Market Street Railway Company ("Market Street") after step one of a modified plan of liquidation and dissolution of Market Street had been approved by the Commission and the United States District Court for the Northern District of California. [Footnote: Holding Company Act release No. 10172] Pursuant to that plan Market Street paid Standard Gas $512,500 in cash in settlement of its open account indebtedness amounting to $707,189 plus a substantial amount of accrued interest, and it executed a full and complete release of all claims which it held against Standard Gas and Standard Power and any of their subsidiaries. The Standard Gas holdings of junior preferred and common stocks of Market Street were declared worthless since there were not sufficient assets to satisfy the claims of the senior preferred stock.

Standard Gas completed its divestment of Louisville Gas and Electric Company in October 1950 by disposing of its remaining holdings of 137,857 shares of common stock for $4,331,329. [Footnote: Holding Company Act release No. 10136]

The United Corporation

The United Corporation ("United") registered as a holding company in March 1938. at which time its portfolio was comprised principally of the common stocks of four holding company subsidiaries. These subsidiaries, together with the percentage of voting control held by United, were as follows: The United Gas Improvement Company, 26.2 percent; Public Service Corporation of New Jersey, 13.9 percent: Niagara Hudson Power Corporation ("Niagara Hudson"), 23.4 percent; and Columbia Gas & Electric Corporation (now the Columbia Gas System, Inc.), 19.6 percent. United also had other substantial interests, principally in utility holding and operating companies.

In 1941, United filed a plan pursuant to section 11 (e) for divestment of control of its statutory subsidiaries whereby United would not vote the securities of any of its statutory subsidiaries or have any interlocking officers or directors and would proceed when advantageous to it, to reduce its holdings in each of its statutory subsidiaries to less than 10 percent of the outstanding voting securities of such subsidiaries. Proceedings on that plan were consolidated with proceedings instituted by the Commission under sections 11 (b) (1) and 11 (b) (2). After the development of an extensive record, the Commission found that the plan was not appropriate nor fair and equitable and could not be approved. [Footnote: United Corporation, 13 S. E. C. 854] While it found that dissolution of United would be appropriate it noted the management's expressed desire to change the nature of United's business to that of an investment company. Under the circumstances, the issuance of a dissolution order was withheld but the Commission directed that United correct the inequitable distribution of voting power by recapitalizing with a single class of stock and cease to be a holding company.

Shortly before the entry of the Commission's order in 1943 and subsequent thereto, various subsidiary as well as non subsidiary holding companies of United underwent extensive reorganizations under section 11. A large number of indirect subsidiaries of United have been divested and United has effectuated the retirement of all of its outstanding preference stock largely through the exchange of securities of reorganized subsidiaries. Substantial blocks of portfolio securities have also been disposed of through market sales.

In October 1949, the Commission approved a plan filed by United by which it substantially reduced its investment in Niagara Hudson through the distribution of a special dividend of Niagara Hudson stock to its own shareholders. [Footnote: Holding Company Act release No. 9431] Approval of that plan was conditioned by the Commission upon a prompt filing by United of a comprehensive and detailed program under section 11 (e). Pursuant to this requirement United submitted a new proposal in November 1949 and after successive modifications, the Commission on June 26, 1951, issued its final order approving the plan as amended. [Footnote: Holding Company Act releases Nos. 10614 and 10643] It provided that holders of less than 100 shares of United common stock may surrender their shares for cash in the amount equal to the average net asset value of such stock based on the average of the closing market prices of United's portfolio during the term of the offer. Holders of 100 or more shares of United common stock were offered the opportunity during the same period to exchange their stock for an amount of Niagara Mohawk Power Corporation ("Niagara Mohawk") common stock having an average market value equal to 97 percent of the average net asset value of the United stock surrendered. Such average net asset value was also based on the closing market prices of United's portfolio securities during the period of the exchange offer. Up to 700,000 shares of common stock of Niagara Mohawk were offered for exchange by United under this plan. United also proposes to sell its entire interest in its common stock in South Jersey Gas Company and to reduce its remaining holdings of voting securities of public utility companies to an amount not to exceed 4.9 percent of the outstanding voting stock of such companies.

Shortly after the close of the fiscal year United undertook the exchange offer approved by the Commission and 362,616 shares of United common stock were exchanged for 69,566.6 shares of Niagara Mohawk common stock. In addition, 95,051 shares of United common were surrendered for cash at a purchase price of $4.43 per share. Approximately 557,130 shares of United were held by holders of less than 100 shares and hence were eligible for the cash purchase offer. Proceedings to review certain aspects of the plan are pending in the Court of Appeals for the District of Columbia.

Washington Gas and Electric Company

Washington Gas and Electric Company ("Washington") registered as a holding company on December 1, 1935, and at that time it was a subsidiary of North American Gas and Electric Company. Subsequently, North American Gas and Electric was liquidated

pursuant to a section 11 (e) plan which was approved by the Commission in 1943 and enforced in the United States District Court for the District of Delaware. [Footnote: 14 S. E. C. 835] Washington had filed a petition in bankruptcy in the United States District Court for the Southern District of New York on September 29, 1941, and, pursuant to order of the District Court for the District of Delaware, the common stock of Washington was turned over to its trustee to be held by him subject to order of the District Court for the Southern District since the common stock had been found to be valueless by the Commission and the District Court of Delaware.

At the time of the filing of its petition in bankruptcy, Washington had three subsidiaries, Oregon Gas and Electric Company, Southern Utah Power Company and Dominion Electric Power, Limited. Washington was also engaged directly in the electric and gas utility business in the State of Washington. The principal electric properties of Washington had been taken by Public Utility Districts in condemnation proceedings in November 1940 and, in the course of reorganization, the remainder of its electric properties were taken in similar proceedings in 1942. Subsequently, the trustee of Washington sold the assets of Oregon Gas and Electric and additional assets of Washington, including its interest in Dominion Electric.

During the proceedings, Washington paid its First Mortgage Bonds in full and caused Southern Utah to refund its debt and to recapitalize on the basis of one class of common stock. As a result Washington received new common stock of Southern Utah in exchange for its former holdings of three classes of that company's stock. On January 24, 1949, the Commission approved a plan submitted under section 11 (f) by the trustee of Washington. [Footnote: Holding Company Act release No. 8801] The plan was accepted by the bondholders and general creditors of Washington and confirmed by order of the United States District Court for the Southern District of New York on October 5, 1949. It was subsequently directed to be consummated by orders of the court dated April 14, 1950, and July 27, 1950. Pursuant to the plan, Washington has divested itself of its interest in Southern Utah, and retains only its gas utility operations. The common stock of Washington is being distributed to the holders of Washington's First Lien and General Mortgage Bonds and to its general creditors. No participation was accorded to its preferred or common stockholders.

On May 29, 1951, the Commission issued an order pursuant to section 5 (d) declaring that Washington had ceased to be a holding company and canceling the effectiveness of its registration subject to a condition reserving jurisdiction over the terms, provisions and amount of all debt securities which may be issued in connection with the plan of reorganization. [Footnote: Holding Company Act release No. 10585] The order also provided that such jurisdiction would be deemed to have been released upon the filing with the Commission of due proof that Washington had obtained approximately $150,000 through the issuance and sale of additional common stock. A statement filed on June 28, 1951, by counsel for Washington indicates that this stock offering has since been successfully consummated.

Wisconsin Electric Power Company

Wisconsin Electric Power Company ("Wisconsin") is an operating-holding company controlling a utility system serving electricity in Wisconsin and Michigan and natural gas in Wisconsin. Steam heating service is provided in Milwaukee and Waukesha, Wisconsin. The company also has a transportation subsidiary operating transit facilities in Milwaukee and adjoining suburbs.

On August 15, 1950, the Commission issued an order pursuant to section 11 (b) (1) instituting proceedings to determine what properties may be retained in Wisconsin's electric holding company system. Hearings are presently in progress on these matters. The company recently offered its transportation properties for sale to the City of Milwaukee. In the event these properties are sold the major remaining problem will concern the retainability by Wisconsin of its natural gas utility business. Representatives of the City of Milwaukee and of the Wisconsin Public Service Commission are participating in the proceedings before the Commission.

PROGRESS OF CONTINUING HOLDING COMPANY SYSTEMS

The utility holding company groups expected to continue under the jurisdiction of the Commission as completely integrated, regional systems consist in general of three major types. The first is the electric holding company system, which usually consists of one holding company above a number of interconnected electric operating companies. In this category are included such systems as American Gas and Electric Company, Central and South West Corporation, The Southern Company, and Middle South Utilities, Inc. A significant characteristic of this type of system is the efficient use of large-scale, centralized generation coupled with economical long-distance transmission of energy.

The second type is the natural gas holding company system, which frequently controls gas-transmission as well as gas-distribution properties. Systems of this class include the Columbia Gas System, Inc., American Natural Gas Company, and Consolidated Natural Gas Company. The third type is the operating-holding company system. In these instances the holding company derives a substantial proportion of its income from its own utility operations but also retains one or more subsidiary operating companies. Examples of this type include the Delaware Power & Light Company, Ohio Edison Company, and Interstate Power Company.

In order to achieve the degree of integration contemplated in section 11 and to justify their continuing existence, these holding companies must do more than simply establish physical interconnections among their subsidiary companies. There must be a realization of important economic and engineering benefits obtainable only by the knitting together of a compact group of operating properties having basic functional relationships with one

another. In addition, the parent holding companies must be in a position to furnish sound and constructive assistance to their operating subsidiaries in the financing of expansion programs. The strength of each system rests heavily upon the underlying financial stability of its subsidiaries.

The following summaries provide a review of the more important actions taken by the Commission during the past fiscal year in respect to operations of a number of the continuing systems. It should be noted that several of these systems are still faced with residual problems under section 11 (b) (1) and 11 (b) (2) of the act, and during the past year they have made several property dispositions intended to eliminate some of their nonretainable holdings. In a limited number of cases, registered holding companies may eventually be able to qualify for exemption from the act pursuant to the provisions of section 3 (a).

Certain of the holding companies described in the preceding section may also remain as parts of continuing systems upon resolution of their existing section 11 problems.

American Gas and Electric Company

American Gas and Electric Company ("American Gas") is the largest of the continuing regional holding company systems with consolidated assets in excess of $678,000,000. Its operations, almost wholly electric, extend over a seven state area from Kentucky to Michigan.

In December 1950, the Commission permitted American Gas to undertake an exchange offer designed to acquire all of the outstanding common stock (162,030 shares) of Central Ohio Light & Power Company ("Central Ohio'-) in exchange for American Gas common stock on the basis of 0.72 of a share of American Gas common stock for each share of Central Ohio common stock. [Footnote: Holding Company Act release No. 10294] Central Ohio, an independent electric operating utility, had service areas in two sections of Ohio about 100 miles apart and not interconnected. Under the plan outlined by American Gas, expenditures of almost $1,500,000 were proposed in order to interconnect the facilities and coordinate the operations of Central Ohio with The Ohio Power Company, an operating subsidiary of American Gas. The exchange proposal proved highly successful and American Gas reported that as of March 12, 1951, it had acquired 98 percent of the outstanding common stock of Central Ohio.

American Gas, with Commission approval, has also eliminated one subsidiary from its system, Union City Electric Company ("Union City"). Since the power requirements of Union City were furnished entirely by The Ohio Power Company, Union City no longer served a useful purpose in the system as a separate corporate entity. Its property therefore was transferred to Ohio Power and the company was dissolved.

The American Gas system serves a territory which, within the last two years, has experienced a tremendous expansion in the tempo and scope of defense production. The system has therefore been carrying on an extensive construction program to meet the additional demands for service and to replace existing properties with more efficient facilities. Its construction program will require expenditures during the years 1951 through 1953 of approximately $288 million. During the past fiscal year the Commission has approved system financings aggregating in excess of $68 million. This was accomplished by advances to subsidiaries, bank loans and mortgage debt and common stock offerings. Among these was a successful rights offering made by American Gas to its stockholders of 339,674 shares of common stock without the aid of underwriting or dealer solicitation. A substantial portion of the net proceeds of $17,619,000 derived from this offering has been reinvested in the equities of the subsidiary operating companies. [Footnote: Holding Company Act releases Nos. 10453 and 10475]

American Natural Gas Company

American Natural Gas Company ("American") and its subsidiaries now constitute an integrated gas transmission and distribution system bringing natural gas from the Hugoton field in Texas to areas in the States of Michigan and Wisconsin. [Footnote: The status of one non-utility subsidiary, Milwaukee Solvay Coke Company, remains to be determined.] The development of the American system was effected by the parent company's divestment of certain non-retainable holdings and the application of cash proceeds derived from these sales to investment in a newly organized gas transmission pipe line, the Michigan-Wisconsin Pipe Line Company. The latter enterprise serves to link the gas utility subsidiaries of American with a source of fuel some eight hundred miles to the south.

The past four years have witnessed the rapid growth of the Michigan-Wisconsin Pipe Line Company as a major long distance transmission system. The first and second phases of the project have been substantially completed and now permit an annual gas delivery capacity of 110 billion cubic feet, the maximum presently authorized by the Federal Power Commission. Capitalization of the pipe line company includes $66 million of bonds, $25 million of common stock owned by American and $20 million of bank loans due July 1, 1952.

On April 5, 1951, Michigan Consolidated Gas Company, one of the principal gas utility subsidiaries of American, acquired the assets of its wholly owned subsidiary, Austin Field Pipe Line Company, in exchange for the cancellation of $7,295,039 of advances, the surrender of all of the outstanding stock and the assumption of all liabilities of the Austin company. [Footnote: Holding Company Act release No. 10327]

In order to meet a continually increasing demand for fuel the American system has undertaken a substantial amount of new financing during the past year. At June 1951 total system construction requirements were estimated at approximately $45 million. In

November 1950, Milwaukee Gas Light Company, another subsidiary, issued and sold at competitive bidding $27 million of mortgage bonds and $6 million of sinking fund debentures to the public and $3 million of common stock [Footnote: Holding Company Act releases Nos. 10169 and 10188] to its parent, American. In early July 1951, Michigan Consolidated Gas Company sold publicly $15 million of bonds at competitive bidding and to its parent, American, $5 million of common stock, which, it was estimated, would meet its requirements through 1951.

In order to preserve a balanced capital structure within the system it has been necessary for the parent holding company, American, to make several offerings of its own common stock from time to time. In August 1950, it issued and sold, pursuant to a rights offering, 304,406 additional common shares. In June 1951, another rights offering to its common stockholders resulted in the sale of 334,935 shares of common stock. [Footnote: Holding Company Act releases Nos. 10054 and 10610] Aggregate proceeds of the two offerings were $15,900,000.

The Columbia Gas System, Inc.

The Columbia Gas System, Inc. ("Columbia Gas") is the parent holding company in an integrated natural gas utility system providing service in seven states. Its properties embrace both distribution and transmission facilities. To meet a continuously increasing demand for natural gas as a house-heating fuel and for new defense requirements, construction expenditures totaling over $37 million were made by the system in 1950, and projected expenditures for 1951 involve an additional amount of $68 million. The completion of this program is dependent, however, upon the availability of certain critical materials. Cash requirements for these undertakings have been met, in part, through the sale at competitive bidding by Columbia Gas of $90 million principal amount of debentures in July 1950. Although a portion of this offering was used to retire $58 million of debentures outstanding, the balance was made available for construction needs.

The indenture under which these debentures were issued permits the company to issue debt to the extent of 60 percent of its total capitalization. Columbia Gas indicated that, while it is presently of the opinion that a debt ratio of not more than 50 percent is desirable, it felt that a substantial amount of additional borrowing capacity might be necessary in periods of heavy construction which would temporarily bring the debt ratio above this level. The Commission recognized the desirability of such flexibility and permitted the declaration covering issuance of the debentures to become effective. It indicated, however, that it considered 50 percent to be the desirable proportion of debt for the system and noted that its approval was not to be construed as an indication that the issuance of debt to the full limit permitted by the indenture would be approved under all circumstances. [Footnote: Holding Company Act releases Nos. 9993 and 10012]

Cash derived by Columbia Gas from its sale of securities has been reinvested in several of its subsidiary operating companies through the purchase of installment promissory

notes. The aggregate of such investments during the fiscal year 1951 was $25,600,000. Columbia Gas has also purchased 122,000 additional shares of the common stock of its subsidiary holding company, Atlantic Seaboard Corporation. The proceeds of this financing have been applied to meet construction requirements. [Footnote: Holding Company Act release No. 10648]

Interstate Power Company

Interstate Power Company is an operating-holding company which, together with its two subsidiaries, is engaged principally in the electric utility business in Minnesota, Iowa, Wisconsin, Illinois, and South Dakota.

Following a complete financial reorganization of the company in 1948 pursuant to a section 11 (e) plan Interstate's rapidly expanding business necessitated the raising of substantial amounts of additional capital. The company's financial structure at that time was still far from ideal and, in the process of meeting its new capital requirements, the company and the Commission were faced with the problem of effecting steady improvement in the system's equity ratio so that future financing could be facilitated on a sound and economical basis. This objective has been achieved with marked success. Interstate's common equity has increased from 17 percent of total capitalization and surplus at the time of its 1948 reorganization to about 27 percent by the middle of 1950.

To finance its 1951 construction program Interstate arranged for short term bank borrowings in the aggregate amount of $4,500,000.

By order dated February 16, 1951, the Commission approved borrowings to the extent of $2,500,000, reserving jurisdiction over the remaining portion pending consideration by the company of plans to effect additional common stock or other equity financing in the near future. [Footnote: Holding Company Act release No. 10398]

During the past fiscal year the Commission also approved an Adjusted Compromise Plan with respect to the distribution of 944,961 shares of Interstate's new common stock which had previously been placed in escrow pending determination as to whether the holdings of Ogden Corporation (former parent company of Interstate) should be subordinated to those held by the public. [Footnote: Holding Company Act release No. 10400] The plan was directed to be enforced by the United States District Court for the District of Delaware in its order dated March 16, 1951. Distribution of the escrowed assets to the holders of Interstate's formerly outstanding securities was initiated a month later.

Middle South Utilities, Inc.

Middle South Utilities, Inc. ("Middle South") controls a utility system serving the three state area embracing Arkansas, Louisiana and western Mississippi. The company was organized in May 1949 to acquire from Electric Power & Light Corporation the latter's

holdings in Arkansas Power & Light Company, Louisiana Power & Light Company, Mississippi Power & Light Company and New Orleans Public Service, Inc., and a small land company. Middle South is now an integrated regional holding company system deriving the major portion of its revenues from sales of electricity. Certain of its nonretainable natural gas and transportation operations, and its interest in the land company, have been disposed of during the past fiscal year.

On September 6, 1950, the Commission approved the sale by Arkansas Power & Light Company of its entire gas utility assets, consisting of distribution systems in 23 small towns and cities in Arkansas. [Footnote: Holding Company Act release No. 10077] These properties were sold to the newly formed Midsouth Gas Company ("Midsouth") which was organized by a group of investment banking firms. Midsouth agreed to pay Arkansas Power in cash an amount equal to the net book cost as of December 31, 1949, of the gas properties and also for other assets transferred and conveyed under the purchase contract.

On December 20, 1950, the Commission also approved the sale by Arkansas Power & Light Company of its holdings of common stock of Capital Transportation Company. The sale was made to a non-affiliated transit company for a total consideration of $575,000. [Footnote: Holding Company Act release No. 10300]

The Middle South system has estimated that its construction expenditures for the year 1951 will total approximately $48,450,000, of which $25,000,000 is to be raised by new financing. In November 1950, the Commission approved the sale at competitive bidding of $10 million of mortgage bonds by Louisiana Power & Light Company, and in March 1951 approval was granted for the issuance and sale by the parent holding company of 450,000 shares of its own common stock at competitive bidding. [Footnote: Holding Company Act releases Nos. 10193, 10228, 10438 and 10458] Middle South has employed the proceeds of this offering, together with other available cash, to purchase $8 million of additional common stock of Arkansas Power & Light Company.

New England Electric System

New England Electric System ("NEES") and its subsidiary companies constitute the largest utility organization in New England. The system's total revenues from operations for the year 1950 amounted to approximately $107 million, 82 percent of which was derived from the sale of electricity, 10 percent from gas and 8 percent from transit operations. The system has 35 subsidiary companies of which 21 furnish electricity, at retail, in Massachusetts and Rhode Island. Two generating companies and a transmission company operating in New Hampshire and Vermont supply electricity on a wholesale basis.

During the past fiscal year, Narragansett Electric Company, a subsidiary operating company, acquired the property of its own subsidiary, Rhode Island Power Transmission Company, which was subsequently dissolved. In October 1950, NEES sold its interest in

Fall River Electric Light Company to Eastern Utilities Associates, a non-affiliated holding company, for $7,608,000. In March 1951, NEES also disposed of its investment in the United Electric Railways Company which operates in the Providence, Rhode Island, area.

NEES has made considerable progress during the year with respect to its plan for the consolidation of certain electric properties into larger operating companies. This plan is closely associated with the separation and disposal of the system's gas properties. The merger of the electric properties of eight subsidiary companies located in the central part of Massachusetts into one electric company was consummated in February 1951 and, at the same time, the gas properties of certain combination gas and electric companies in this area were separated and regrouped into four gas companies. On July 14, 1951, NEES invited proposals for the purchase of all or part of the system's gas properties.

After many modifications, the reorganization plan of Green Mountain Power Corporation ("Green Mountain"), a subsidiary of NEES, was approved by the Commission and ordered enforced by the United States District Court for the District of Vermont at the close of the fiscal year. [Footnote: Holding Company Act releases Nos. 10524, 10595 and 10625] The plan, among other things, provided for the exchange of new common stock for the company's then outstanding preferred stock, the issuance and sale, for cash, of additional shares of new common stock and the settlement of possible intra-system claims. Since NEES was allowed no participation in the reorganized company, Green Mountain is now an independent operating utility.

It is estimated that construction expenditures for the NEES system for the years 1949 to 1952 inclusive will total $122 million. In addition cash demands to meet sinking fund requirements and short term debt maturities require an additional $29 million. Of direct concern to the Commission has been the system's temporary and permanent financing program for this construction.

To provide temporary financing for the construction program, system companies from time to time have borrowed from commercial banks with indications that they expect to do permanent bond and capital stock financing and use the proceeds to retire the bank debt and to pay for construction. During the fiscal year, New England Power Company ("NEPCO") and Worcester County Electric Company ("Worcester County"), subsidiaries of NEES, each sold $12 million principal amount of bonds. [Footnote: Holding Company Act releases Nos. 10380, 10402, 10468, 10488] Although during the period certain subsidiary companies issued capital stock to NEES and used the proceeds thereof to retire bank debt, short term promissory notes to banks authorized or outstanding as at the end of the period aggregated $22 million. During July 1951, other subsidiaries had pending applications for Commission approval of an additional $6,175,000 of bank loans. Proceeds to be derived from the contemplated sale by NEES of its investments in gas and transportation properties are to be reinvested in the equity of its subsidiary companies in order to effect an improvement in the system's capitalization ratios.

New England Gas and Electric Association

New England Gas and Electric Association ("NEGEA") is a Massachusetts trust holding the common stocks of 11 utility companies all of which, except New Hampshire Electric Company ("New Hampshire") and Kittery Electric Light Company ("Kittery"), are engaged in the electric or-gas utility business in Massachusetts. In February 1951, NEGEA and New Hampshire filed an application with the Commission proposing the issuance by New Hampshire of 15,000 shares of preferred stock and 140,000 shares of common stock and the exchange of such stocks for all of its presently outstanding common stock which is held by NEGEA. The application further proposed the sale by NEGEA of New Hampshire's preferred stock to the public and the new common shares of New Hampshire to NEGEA's stockholders, both at competitive bidding. NEGEA also proposed to donate to New Hampshire its holdings of all of the common stock of Kittery prior to the issuance and exchange of the new securities. The Commission approved the proposed transactions in March 1951, but no bids were received for the purchase of the new preferred and common stocks of New Hampshire. [Footnote: Holding Company Act release No. 10424]

NEGEA is continuing the extensive construction program commenced prior to the past fiscal year. Gas plant additions have included facilities to utilize natural gas when it becomes available in the New England area. Estimated expenditures for the calendar years 1951 and 1952 aggregate $12,200,000, of which $2,200,000 represents expenditures necessitated by the introduction of natural gas. To finance this construction program the operating subsidiaries will use general corporate funds in the aggregate amount of $8,500,000, borrow $1 million from banks, and sell additional common stock to NEGEA in the amount of $2,700,000. The cost of adjusting customer-owned appliances for natural gas is to be financed through the issuance by subsidiary companies of 10-year unsecured sinking fund notes.

In June 1951, the Commission approved the issue and sale by NEGEA of 197,394 additional common shares in the form of a rights offering to holders of its common stock. [Footnote: Holding Company Act release No. 10592] The proceeds, amounting to $2,566,000, were used to repay bank loans in the amount of $1 million and to purchase additional common stocks of subsidiaries NEGEA is planning to raise approximately $3 million through the issue and sale of additional common shares during 1952.

The cash requirements of NEGEA during the past fiscal year have included the purchase of additional shares of common stock of Algonquin Gas Transmission Company, a natural gas pipeline company to be engaged in transporting natural gas to the New England area. [Footnote: Holding Company Act release No. 10504] NEGEA's interest in this subsidiary will be limited to $3 million or 37.5 percent of the total initial equity of the company. Participating with NEGEA are Eastern Gas and Fuel Associates, Texas Eastern Transmission Corporation, and Providence Gas Company. To finance the

Algonquin purchase NEGEA has negotiated short-term bank loans which will be refinanced on a permanent basis as soon as the line is in operation.

Northern Natural Gas Co.

Northern Natural Gas Company ("Northern") is engaged in the purchase, transmission and distribution of natural gas, which is carried from fields in Texas, Oklahoma, and Kansas to utility companies located principally in Minnesota, Iowa, and Nebraska. The company has one wholly owned gas utility subsidiary, Peoples Natural Gas Company, and is therefore a registered holding company. On September 25, 1950, however, Northern filed an application with this Commission pursuant to section 3 (a) (3) seeking exemption for itself as a holding company and for each subsidiary thereof as such from the provisions of the act. Hearings have been held on this application and the Division of Public Utilities has recommended denial of the application. The Commission has heard oral argument of the question and has taken the matter under advisement.

Since the end of World War II, increased demands on this system have necessitated large increases in its pipe line capacity, which at the end of 1950 stood at approximately 600,000 mcf a day. Additional construction planned and undertaken for the year 1951 contemplates a further addition of 225,000 mcf of daily capacity. The Commission has constantly urged that the financing of this construction be designed with a view to preserving as far as possible the substantial equity ratio which has been a characteristic of the system for many years. During the past two years the company has sold an aggregate of 810,000 shares of common stock by means of rights offerings with gross proceeds of $21,578,750, [Footnote: Holding Company Act releases Nos. 8963 and 9833] and has also sold $40 million of 2% percent serial debentures. [Footnote: Holding Company Act releases Nos. 9890 and 9921] The company estimates that its 1951 construction program will cost approximately $60 million and contemplates financing these expenditures on a long-term basis through the sale of $51 million of securities to the public. Temporary financing through $30 million of bank loans was permitted by the Commission on April 26, 1951. [Footnote: Holding Company Act release No. 10517]

Northern States Power Company

Northern States Power Company ("Northern States") is a holding-operating company engaged, either directly or through subsidiaries, in the electric and gas utility business in the states of Minnesota, Wisconsin, North Dakota and South Dakota, Although the system is expected to achieve ultimate compliance with the standards of section 11 (b), it is faced with some residual problems.

In this connection, the Commission in June 1950 authorized the sale of all of the physical properties of Interstate Light & Power Company (Ill.) a wholly-owned subsidiary of Northern States, to Northwestern Illinois Gas & Electric Company, a non-affiliated company, for the base price of $549,900. [Footnote: Holding Company Act release No.

9927] In the same order the Commission also authorized the sale by Interstate Light & Power Company (Wisc.), another wholly-owned subsidiary, of that part of its electric properties comprising its Platteville division to Wisconsin Power & Light Company, another non-affiliate, for the base price of $560,500. These property sales effected the disposition of outlying electric properties in northwest Illinois and southern Wisconsin which did not constitute a part of the Northern States' principal electric system.

By order entered October 13, 1950, the Commission authorized the-sale by Northern States of 175,000 shares of new preferred stock to provide a part of the capital required for completion of the system's post-war construction program, estimated to aggregate $163,500,000 to the end of 1951. [Footnote: Holding Company Act releases Nos. 10157 and 10174]

The company stated that further financing of approximately $25 million would be required for the completion of the current construction program in connection with which a material amount of common stock would be sold contingent upon market conditions. It is expected that Northern States will inaugurate another large scale construction schedule, to provide for rapidly growing demand.

Ohio Edison Company

Ohio Edison Company ("Ohio Edison"), formerly a subsidiary of The Commonwealth & Southern Corporation, is now an independent operating-holding company having one utility subsidiary, Pennsylvania Power Company ("Pennsylvania Power"). During the past year, the company and its subsidiary have undertaken several financing operations to provide funds for construction expenditures for the years 1951 and 1952 estimated to aggregate $57,800,000 in the case of Ohio Edison and $14,900,000 for Pennsylvania Power.

Ohio Edison has made two offerings of common stock. The first took place in October 1950 when it offered 396,571 shares through a rights offering to stockholders. This was followed in May 1951 by an additional rights offering of 436,224 common shares. [Footnote: Holding Company Act releases Nos. 10133, 10508, and 10540] The proceeds derived from these two sales totaled over $23 million which materially increased the company's common stock equity. As a result, Ohio Edison made a further investment of $1,200,000 in Pennsylvania Power by the purchase of 40,000 shares of the latter's common stock, all of which is owned by the parent company. In addition, Pennsylvania Power sold at competitive bidding in March 1951, $4 million par value of preferred stock. [Footnote: Holding Company Act releases Nos. 10426 and 10459] Shortly thereafter, Ohio Edison proposed the sale of its own preferred stock in the amount of $15 million, but because of unfavorable market conditions the offering was postponed.

The Southern Company

The Southern Company ("Southern Company") is the parent holding company of a system which survives the former Commonwealth & Southern group. The integrated system, which it controls, furnishes service through four electric utility subsidiaries in Georgia, Alabama, Florida and Mississippi. It is second largest of the continuing systems.

On August 24, 1950, the Commission approved the acquisition of Birmingham Electric Company ("Birmingham") through an exchange of common shares of the Southern Company and preferred shares of Alabama Power Company ("Alabama"), a subsidiary of the Southern Company, for common and preferred shares of Birmingham. The Commission's order required that the Southern Company and Alabama, which became the immediate parent of Birmingham, bring about the disposal of all interest in the transportation properties of the latter company not later than August 31, 1951. [Footnote: Holding Company Act release No. 10055] The sale of these properties was accomplished in June 1951. [Footnote: Holding Company Act releases Nos. 10551 and 10588]

During the calendar year 1950, capital expenditures of the Southern Company system totaled $70 million and present plans call for further additions to plant during the period 1951-1953 sufficient to effect a 38 percent increase in generating capacity over that installed by the end of 1950. In October 1950 the Southern Company sold one million shares of its common stock at competitive bidding [Footnote: Holding Company Act releases Nos. 10114 and 10129] and another sale of the same amount was consummated in April 1951. [Footnote: Holding Company Act releases Nos. 10454 and 10484] Total proceeds derived from these offerings aggregated approximately $21,900,000. These funds, together with additional amounts of treasury cash, were invested by the parent company in the common stock of its subsidiaries. In addition to this common stock financing, operating subsidiaries sold bonds and preferred stocks to the public yielding cash proceeds of over $34 million.

Southern Natural Gas Company

Southern Natural Gas Company ("Southern Natural") operates a natural gas pipeline system extending from gas fields in Texas, Louisiana and Mississippi to markets in Mississippi, Alabama and Georgia. Two of the company's subsidiaries are engaged in the distribution of gas in Mississippi and Alabama. Another subsidiary operates a 35 mile gas pipeline in Louisiana.

During 1950 Southern Natural commenced the largest program in its history for the expansion and extension of its pipeline system. Funds for the major portion of the cost of this construction were obtained initially from short-term bank loans in the amount of $20 million. [Footnote: Holding Company Act release No. 9935] Early in 1951 the Southern Natural sold $17,500,000 of its first mortgage bonds due in 1970, and 155,546 shares of additional common stock to yield aggregate proceeds of $22,666,250, [Footnote: Holding Company Act releases Nos. 10338 and 10351] which were used to repay the bank loans.

Upon consummation of this financing, the ratio of common equity to total capitalization and surplus of the system was approximately 44 percent.

Over the past five years, Southern Natural's gross plant account has doubled from about $50 million over $100 million.

Union Electric Company of Missouri

Union Electric Company of Missouri ("Union Electric") is an operating-holding company serving a sizeable area in the State of Missouri, including the City of St. Louis, and through its utility subsidiary, Union Electric Power Company, the southwest portion of Illinois. Union Electric is at present a subsidiary of The North American Company, a registered holding company, which, at one time, controlled 36 utility and 46 non-utility companies and through them operated in 10 States and the District of Columbia. Union Electric is the sole remaining direct utility subsidiary of The North American Company.

On December 29, 1950, North American Light & Power Company, a wholly-owned subsidiary of The North American Company, transferred pursuant to Commission approval its holdings of all of the common stock of its subsidiary, Missouri Power & Light Company, to The North American Company, in partial liquidation. Immediately thereafter. The North American Company transferred these holdings to Union Electric Company of Missouri, its direct subsidiary, in return for 600,000 shares of the latter's common stock. [Footnote: Holding Company Act release No. 10320] Union Electric, as a part of the transaction, agreed to dispose of several utility properties not capable of integration with its own properties and certain non-utility properties all of which were owned by Missouri Power & Light Company. Sales of an electric distribution system and of some ice manufacturing equipment were consummated prior to the close of the fiscal year.

Union Electric and its subsidiaries are engaged in an extensive construction program which will require expenditures for the years 1951 through 1955 of approximately $161 million. The funds required for the fiscal year were derived principally from the sale by Union Electric, in April and June 1950, of 700,000 shares of its common stock to The North American Company for $10 million and the sale, in December 1950, of $25 million of mortgage bonds to the public. [Footnote: Holding Company Act releases Nos. 9778, 9944, 10239, and 10268]

During the past year, Union Electric, together with four other utility companies, participated in the formation of a new corporation known as Electric Energy, Inc. This represented a significant development in the utility industry and in the history of administration of the act. The new company was organized to build and own a 500,000 Kw generating station at Joppa, Illinois, for the purpose of supplying one half of the power requirements of the Paducah, Kentucky, plant of the Atomic Energy Commission. The main question presented to the Commission for determination was whether, under

the standards of the act, the common stock of Electric Energy, Inc., amounting to $3,500,000, might be acquired by the organizers in the following proportions: Union Electric, 40 percent; Middle South Utilities, Inc., 10 percent; Kentucky Utilities Company, 10 percent; and Illinois Power Company, 20 percent. The first two of these companies were registered holding companies and the latter two were exempt holding companies. The remaining stock was to be acquired by Central Illinois Public Service Company, which was not a holding company subject to the act. The type of showing required of the applicants to support their proposed acquisitions would ordinarily necessitate extensive proof, consuming considerable time. Due to the importance of this project to the national defense and the expedition required in its building, the Commission decided that, since the project was not "business as usual", it merited postponement of "regulation as usual"; accordingly, it postponed to more normal times the taking of evidence which would be required to justify the acquisition of the stock and permitted the acquisition on an interim basis. [Footnote: Holding Company Act release No. 10340]

The proposed financing of this project by means of the sale of not more than $100 million of first mortgage bonds to two insurance companies and the sale of the $3,500,000 of common stock to the organizers also raised a serious question as to the propriety of such a capital structure. The Commission expressed the view that the problem raised by this unbalance in the capital structure could be resolved favorably, in view of the financial commitments of the Atomic Energy Commission which have the effect of guaranteeing repayment of a substantial portion of the indebtedness. [Footnote: Holding Company Act release No. 10639]

The United Gas Improvement Co.

The United Gas Improvement Company ("UGI") is a registered holding company, incorporated under the laws of Pennsylvania, having nine subsidiaries. Six are gas utility companies, one is a gas and electric utility company, and two are non-utilities. The operations of all subsidiaries are conducted within the State of Pennsylvania.

In April 1951, UGI disposed of its only subsidiary having out-of-state operations when it accepted a $1 million note from Delaware Coach Company in exchange for 10,000 shares of that company's common stock and sold the balance of 26,000 outstanding shares to an unaffiliated person for $400,000. [Footnote: Holding Company Act release No. 10477] Delaware Coach Company conducts a transportation business in Wilmington, New Castle, and Newark, Delaware. It also has two wholly-owned subsidiaries, Delaware Bus Company and Southern Pennsylvania Bus Company.

On June 15, 1951, the Commission approved a voluntary exchange plan, submitted by UGI, intended to reduce the substantial amount of minority interest investments in the portfolio of UGI. [Footnote: Holding Company Act release No. 10624] A substantial portion of these holdings had been received by UGI in exchange for the latter's

investments in holding companies which were reorganized under section 11 of the act. Under the plan, UGI offered to exchange for each unit of five shares of its own stock (to the extent of 363,285 shares), three shares of common stock of Philadelphia Electric Company and two shares of common stock of Consumers Power Company. Stockholders tendering from one to four shares of UGI stock received a cash payment in lieu of stock on an equivalent basis. Shareholders of U GI stock tendered 329,940 shares eligible for the exchange offer and 5,691 additional shares were retired by cash payment. As a result of these transactions, the outstanding capital stock of UGI has been reduced from 1,566,371 shares to 1,230,740 shares. UGI is under order to dispose of all of its remaining non-subsidiary security holdings.

Utah Power & Light Co.

Utah Power & Light Company ("Utah"), formerly a subsidiary of Electric Power & Light Corporation, is a registered operating-holding company subject to the active regulatory jurisdiction of the Commission by virtue of its ownership of voting securities in Western Colorado Power Company. Utah and its subsidiary are presently engaged in a construction program which will entail expenditures of approximately $44 million in the. years 1951 to 1953, inclusive. Expenditures for the calendar year 1951 are estimated at approximately $18 million.

On August 29, 1950, the Commission approved the issuance by Utah of $8 million of first mortgage bonds, as well as 166,604 shares of common stock, [Footnote: Holding Company Act releases Nos. 10063, 10096, and 10148] and, on March 8, 1951, it permitted the company to borrow from, certain banks amounts not to exceed $12 million evidenced by notes payable on December 15, 1951. [Footnote: Holding Company Act release No. 10429] This note indebtedness was expected to be retired after the close of the fiscal year through the sale of $9 million of additional mortgage bonds and 175,000 shares of new common stock. [Footnote: Holding Company Act release No. 10759] During the year the Commission also approved the company's proposal to amend its certificate of organization and by-laws so as to effect, among other things, an increase in the number of authorized shares of capital stock, an adjustment of its preemptive rights provisions, and a change in the date of stockholders' annual meeting. [Footnote: Holding Company Act release No. 9976] On April 30, 1951, the Commission approved an application by Utah to purchase from the Village of Arco, Idaho, the electrical distribution lines and facilities, together with a transmission line owned by Arco, for a cash consideration of $100,000. [Footnote: Holding Company Act release No. 10535]

The West Penn Electric Company

The West Penn Electric Company ("West Penn") is the parent holding company in a utility system deriving about 90 percent of its revenues from sales of electric power and servicing a territory located principally in Pennsylvania, West Virginia, and Maryland. Small adjacent sections of Ohio and Virginia are also served. West Penn was formerly a

subsidiary of American Water Works & Electric Company, Inc., which was liquidated in January 1948.

The West Penn system presently has in progress a construction program, which for the calendar years 1951 and 1952 contemplates the expenditure of more than $75 million. On February 21, 1951, the Commission approved the sale by West Penn of 320,000 shares of its common stock, at competitive bidding, with proceeds in excess of $8,500,000. [Footnote: Holding Company Act releases Nos. 10403 and 10431] In April 1951, bond financings undertaken by two of the subsidiary operating companies furnished additional funds of over $20 million. [Footnote: Holding Company Act releases Nos. 10428, 10476, 10487, and 10522]

The Commission now has before it a residual problem deriving from the liquidation of West Penn's former parent company, American Water Works & Electric Company, Inc. in October 1947, American Water Works & Electric Company, Inc., undertook to retire its outstanding publicly-held preferred stock. This was accomplished by cash payment of the liquidation preference of $100 per share and accrued dividends to October 15, 1947. Furthermore, at the direction of the Commission and with the approval of the United States District Court for the District of Delaware, escrow certificates were issued to the holders of the preferred stock as evidence of claims for such additional payments as the Commission might subsequently determine in fairness and equity should be made. In December 1950, after public hearings and the submission of briefs, the Division of Public Utilities submitted a recommended decision to the Commission proposing an additional payment of $10 per share plus compensation for delay in payment at the rate of 5.45 percent from October 15, 1947. On March 15, 1951, oral argument was heard and the Commission now has the matter under advisement.

ACQUISITIONS OF SECURITIES, UTILITY ASSETS AND OTHER INTERESTS

Under the provisions of sections 9 and 10 of the Holding Company Act the Commission passes upon numerous applications covering acquisitions of securities, utility assets or other interests. The major portion of these applications reflect the acquisitions by parent holding companies of securities issued by their subsidiaries. In this area, the Commission exercises jurisdiction over the manner in which parent holding companies finance the expansion of their subsidiary companies. This is one of the most important functions of the modern holding company. During the past fiscal year, for example, holding companies purchased securities of their subsidiaries totaling $216 million. The review of these intercompany security sales is important because of their effect upon the ultimate financial integrity of the utility operating subsidiaries. The maintenance of sound and balanced financial programming at this level is also an important aspect of the Commission's assistance to State regulatory commissions in preserving the stability of utility enterprises operating within their jurisdiction. Public utilities, unlike most other

industries, are usually faced with the problem of expanding plant facilities in periods of depression as well as prosperity. A high degree of financial flexibility is therefore essential in order to insure maintenance of adequate service to consumers.

A smaller proportion of the applications under section 10 relates to the acquisition of securities, assets or other interests outside the previous scope of operation of the applicant systems. In many cases these acquisitions reflect the growing trend of positive integration reported in earlier years. Important examples during the fiscal year 1951 included the American Gas and Electric Company's acquisition of the common stock of Central Ohio Light & Power Company, acquisition of the stock of Birmingham Electric Company by The Southern Company from Electric Bond and Share Company and other holders, the acquisition by Niagara Mohawk Power Corporation of certain properties from two non-affiliated companies in the State of New York, the purchase by Eastern Utilities Associates of additional common stock of Fall River Electric Light Company from New England Electric System, and the acquisition by a subsidiary in the Consolidated Natural Gas Company system of gas utility assets from a subsidiary of West Penn Electric Company. An exchange of property was also consummated between Louisiana Power & Light Company, a subsidiary of Middle South Utilities, Inc., and Gulf Public Service Company, Inc., a subsidiary of an exempt holding company.

Well over $1 billion of utility assets have been acquired by holding company systems and utility operating companies over the past several years thereby effecting a greater degree of integration of facilities.

FINANCING

During the 12 months ending June 30, 1951, 313 questions were presented to the Commission for determination pursuant to sections 6 and 7 of the act, under which the Commission is required to pass upon the issuance of securities, and assumptions of liability and alterations of rights of securities, by registered holding companies and their subsidiaries. A total of 326 questions were disposed of during the year, including a few carried over from the latter part of the preceding year. All but 37 of these related to issues of securities. In the fiscal year 1950, 337 questions were disposed of under sections 6 and 7.

Following the pattern established in 1948, financing during the past year has been predominantly for the purpose of meeting very heavy construction expenditures. On an industry-wide basis, expenditures of electric and gas utilities for the past year, exclusive of investment in natural gas transmission facilities, are estimated to have been in excess of $2,400,000,000. However, public offerings of securities for the fiscal year 1951 did not match in volume the total for 1950 which established a peak level for the industry. The tabulation set forth below includes all security sales for cash, plus refunding exchanges, by electric and gas utility operating companies which have been approved

under sections 6 and 7 of the act. The table also includes similar security sales by all other electric and gas utility companies in the United States which have registered their issues with the Commission under the Securities Act of 1933. The data for gas utilities cover only those companies which are engaged in the retail distribution of natural or manufactured gas. Private placements of securities not subject to either the Holding Company Act or the Securities Act of 1933 are separately identified, although the figures are at best rough estimates.

(chart omitted)

The over-all decline in financing volume can probably be attributed to the less favorable security markets prevailing since March 1951, when the Federal Reserve System withdrew support from the Government bond market, thereby inducing a substantial reduction in the prices of corporate bonds and preferred stocks. Market receptivity for preferred issues has been affected to a much greater degree than was the case with bonds and debentures, and the growth of private placements may also be traced, in part, to the same causes. An encouraging aspect of the over-all pattern of utility financing has been the sustained employment of common stock offerings, which contributes to the long-term stability of the industry.

With the further contraction in the numbers of companies subject to active regulatory jurisdiction under the act, as a result of divestments under section 11, there has been some corresponding decline in the volume of financing approved under sections 6 and 7, although the trend seems to be leveling off as the program of integration and simplification approaches completion. The expansion of the continuing systems is proceeding at a rapid pace, and their financing requirements account for approximately one-third of the total for the industry. Furthermore, the intensification of defense preparations and the persistence of a tense international situation suggest continuation of heavy cash requirements for an extended period.

The following tables analyze in detail the volume of securities sold for cash, or issued in exchange for refunding, by registered holding companies and their subsidiaries pursuant to authorization of the Commission under sections 6 and 7. Portfolio sales and issues in connection with reorganization are excluded. Significantly, these data reflect the use of a higher proportion of common equity financing by utility companies subject to regulation under the act than is the case for the industry as a whole, as reflected in the preceding tabulation.

(charts omitted)

In the fiscal year 1950, debt offerings of the electric and gas utilities in registered holding company systems represented 61.6 percent of the total financing of these companies, preferred stock accounted for 7.6 percent and common stock 30.8 percent. In 1951 the

proportions were as follows: debt, 60,0 percent; preferred stock, 11.3 percent; common stock, 28.7 percent.

One of the most important functions of the public utility holding company is the furnishing of capital to its subsidiaries. During the fiscal year 1951 holding companies registered under the act purchased for cash $119,389,000 of common stocks issued by their subsidiaries. In addition they purchased $102,290,000 of subsidiary debt securities and preferred stocks. To raise the cash required for the assistance, registered holding companies sold $218,159,000 of their own securities to the public, including $75,332,000 of common stock and $142,827,000 of debentures. In 1950 holding companies raised $299,909,000 through the sale of $114,984,000 of their common stocks and $184,925,000 of senior securities. With the proceeds they purchased $139,600,000 of the common stocks of their subsidiaries and $60,300,000 of subsidiary senior securities. With respect to both years the sales of debt securities by registered holding companies represent for the most part parent company financing in systems where the subsidiaries have little or no senior securities in the hands of the public thereby enabling the holding companies to issue senior securities without impairing the consolidated equity position of the system.

The role of holding companies in the financing of their subsidiaries today is in sharp contrast with the situation found by the Congress in the investigation which it conducted prior to passage of the act. During the seven-year period from 1924 to 1930 inclusive, public utility holding companies sold approximately $4,856 million of their securities to the public. The proceeds from this financing were devoted almost entirely to the purchase of outstanding securities. Only a negligible portion went into the construction of plant facilities. [Footnote: S. Rep. No. 621, 74th Cong., 1st sess., p. 15.] Furthermore, for a period of many years up to 1928, it was the general practice of holding companies to furnish capital to their subsidiaries in the form of demand notes or open account advances bearing interest of from 6 to 8 percent and in some large systems the holding companies followed the regular practice of compounding interest monthly or quarterly. [Footnote: S. Doc. 92, 70th Cong., 1st sess., pt. 72-A, chs. 5 and 6./S. Doc. 92, 70th Cong., 1st sess., pts. 23 and 24, pp. 218 et seq.] By comparison, registered holding companies have invested in excess of $540,000,000 in the common stocks of their subsidiaries in the period from July 1, 1947, to June 30, 1951.

Another important aspect of the financing of registered holding company systems during the past year has been the predominance of the rights offering as a vehicle for raising common equity money. Total sales of common stocks to the public by registered holding companies and their subsidiaries in 1951 aggregated $144,560,000, of which holding companies accounted for $75,331,000 and subsidiaries, $69,229,000. Of this amount 14 issues totaling $117,395,000 were sold by means of rights offerings. In one instance there was a substantial exercise of rights by a parent holding company. [Footnote: The parent, In the exercise of its rights, purchased 56.2 percent of this issue. There were four other rights offerings not included in the above totals for the fiscal year 1951 in which 94 or

more percent of the issue was purchased by parent holding companies. The amounts taken by outside stockholders were, in each case, negligible.] Stockholder acceptance was less than 100 percent in only three of the offerings.

Probably the most significant development in this group of issues was the growing importance of the non-underwritten rights offering. Only five offerings aggregating $37,897,000 were made with the aid of firm underwriting commitments. Four issues totaling $22,065,000 were offered without underwriting, but had the benefit of dealer solicitation. The remaining five rights offerings, amounting to $57,433,000 were sold without the benefit of underwriting or dealer solicitation assistance. All five were subscribed in percentages ranging from 106 to 188. In each of these cases the oversubscription privilege made an important contribution to the success of the sale.

The utility bond market suffered a sharp decline in the last four months of the fiscal year. No perceptible change in rates was evident until March 1951, when prices of outstanding utility issues began to weaken along with the prices on long term government bonds. The resulting uptrend in yields of outstanding issues, however, did not fully reflect the impact of the change upon new offerings. This becomes evident from a comparison of several successive utility offerings, all classified by the investment rating agencies as of generally comparable quality.

On December 7, 1950, an electric utility company offered $6 million of 30 year mortgage bonds at a cost of money to the company of 2.87 percent. On April 5, 1951, some time after the decline in government bond prices had set in, another electric utility of comparable credit sold $10 million of mortgage bonds of similar maturity at a cost to the company of 3.345 percent. This increase of almost one-half of one percent brought interest costs to the highest level in several years. Although there was some leveling off in new money rates in April, the relief was only temporary. On June 28, 1951, another offering of electric utility bonds bearing the same credit rating and maturity was made at a cost 3.675 percent. This issue represented the high point of interest costs for the period and the issue was quickly absorbed by institutional purchasers. Subsequent offerings in the same quality group were made at more favorable rates until early in September 1951, when yields again turned upward.

This marked change in money costs may have a considerable impact upon the industry. For a long period the low rates available on senior security offerings were a significant offset to increased operating expenses and, in the financing of new construction, they provided added assurance of an adequate return on new equity investment. Further increases in the cost of raising new capital may result in greater pressure on the utility rate structure, although throughout this period of weakness in the prices of debt securities and preferred stocks, utility common stocks have been readily saleable in substantial amounts, and utility managements on the whole have taken advantage of the opportunities presented.

COMPETITIVE BIDDING

Offerings of securities by issuing companies under sections 6 (b) and 7 of the act and portfolio sales by registered holding companies under section 12 (d) are required to be made at competitive bidding in accordance with the provisions of rule U-50. Certain special types of sales, including issues of less than $1 million, short term bank loans, issues the acquisition of which have been authorized under section 10 and pro rata issues to existing security holders are automatically exempt under clauses (1) through (4) of paragraph (a) of the rule. In paragraph (a) (5) the Commission retains the right to grant exemptions by order where it appears that competitive bidding is not necessary or appropriate to carry out the provisions of the act.

Securities sold at competitive bidding under rule U-50 from its effective date, May 7, 1941, to June 30, 1951, total in excess of $6,770,000,000. A tabular presentation showing the various classes of securities, number of issues and amounts, for the entire period and for the past fiscal year is set forth below:

(chart omitted)

The experience of the Commission in administering rule U-50 has adequately demonstrated its workability and effectiveness in maintaining competitive conditions and in achieving minimum costs of flotation. The Commission has always recognized, however, that flexibility in administration was a necessity and it has granted a considerable number of exemptions in cases where unusual circumstances were present. In the 10-year period since the rule became effective, 202 security issues totaling in excess of $1,566,000,000 have been exempted by Commission order from the competitive bidding requirements. Ten issues with a value of $151,772,000 were exempted in fiscal 1951. These are exclusive of the automatic exemptions. The following table summarizes these exempted sales by type of security and also shows the numbers and amounts of issues sold with and without underwriting arrangements.

(chart omitted)

REVISION OF REGULATORY PROCEDURES

Now that the task of integration and simplification of many of the holding company systems has been substantially completed, steps have been taken to streamline the procedures employed in regulation of the continuing systems down to the simplest possible dimensions. As a starting point, the Commission undertook during the past year a thorough-going revision of its Form U5S which is required to be filed annually by registered holding company systems. The modifications which were incorporated in the new form were designed to minimize reporting requirements and adjust its provisions to

the pattern of the surviving holding company systems. Under the revised form all registered holding companies in the same system may join in the filing of a single report. Another change permits copies of this report (less certain exhibits) to be filed by registered holding companies in complete satisfaction of all annual reporting requirements under sections 13 and 15 (d) of the Securities Exchange Act of 1934. Furthermore, the Commission abolished Form U-14-3, an additional filing heretofore required to be made annually by registered holding companies, as well as Forms U5-K and U5-MD which registered holding companies formerly had the option of filing in lieu of Form 10-K.

Eighteen of the 31 registered holding companies required to file reports under the Securities Exchange Act of 1934 elected to satisfy the requirements of that act for the calendar year 1950 by filing duplicate copies of the revised Form U5S. Additional systems are expected to take advantage of this procedure in the coming year.

The Commission presently has under study the revision of Form U-13-60 which is the annual filing required to be made by the service companies associated with holding company systems. The objective of this revision will likewise be maximum simplification, although it should be noted that the opportunities for integration with the reporting requirements under other statutes administered by the Commission are not nearly as great as in the case of Form U5S, because the utility service; company is a device peculiar to the registered holding company system.

INVESTMENT BOND AND SHARE CORPORATION

In the spring of 1951, the staff of the Commission made an investigation to secure additional details on the published story that three officers of Investment Bond and Share Corporation ("IBS") proposed to sell 80,000 shares of common stock of Eastern Kansas Utilities, Inc., to Kansas City Power and Light Company, both of which companies were formerly subsidiaries of United Light and Railways Company, a registered holding company. The investigation disclosed that the 80,000 shares proposed to be sold included 15,299 shares owned by IBS, a Delaware corporation whose principal offices are located in Chicago, Illinois. It further revealed that IBS, though a holding company as defined by the statute, for a number of years had taken no steps to effect its registration or to apply for exemption.

As a direct result of the investigation, IBS registered on July 2, 1951, and on August 8, 1951, submitted a plan under section 11 (e) designed to effect its ultimate liquidation and dissolution in compliance with the provisions of section 11 (b).

ORIGINAL COST STUDIES

On April 21, 1941, the Commission adopted rule U-27 which, as amended on. November 17, 1943, provides that every registered holding company and every subsidiary thereof, which is a public utility company and which is not required by the Federal Power Commission or a State commission to conform to a classification of accounts, shall keep its accounts in accordance with the designated systems adopted by the Commission for electric and gas utility companies. These systems specifically provide that utility? plant accounts shall be stated at the original cost incurred by the persons who first devoted the property to utility service.

Some field examinations of the utility companies' original cost and reclassification studies were begun in 1945, but it was not until later in 1946 that a staff of accountants was organized for this work and field audits undertaken on a comprehensive scale. As of June 30, 1951, the staff had completed the field audits of sixteen companies in various States which do not have regulatory commissions. During the intervening years, some of the reports filed with this Commission were transferred to other regulatory authorities for audit due to changes in applicable jurisdiction as a result of mergers, consolidations and divestments.

Formal proceedings have been completed and orders of the Commission have been issued with respect to nine of the sixteen companies examined. Amendments giving effect to the recommendations of the Commission's staff have been filed by five companies, and these matters will be closed at an early date. Recommended adjustments affecting accounts of the other two companies are still under discussion.

The results of examinations conducted by the Commission disclosed that the utility plant of the companies involved had an original cost value of approximately two-thirds of the amounts recorded per books prior to reclassification. The remaining one-third of the recorded amounts was transferred to adjustment accounts. Almost 75 percent of the difference between the amount recorded per books and original cost has been classified as Account 107, Plant Adjustments, and required to be written off immediately. The balance has been classified as Account 100.5, Plant Acquisition Adjustments, and will be amortized over a period of years, except in those cases where the company has elected to dispose of all adjustments immediately.

COOPERATION WITH STATE AND LOCAL REGULATORY AUTHORITIES

The policy of the Commission always has been to cooperate to the fullest extent with State and local regulatory authorities. Aside from the many informal contacts and conversations between the Commission and other agencies, which are too numerous to detail, there were several instances of cooperation during the past year which are worthy of mention.

An example of the type of cooperation which is possible between the Federal agency and a State Commission is an investigation which was conducted by this Commission at the request of a State Commission during the past year. Because of the confidential nature of the investigation it is possible to give the facts here only in outline. The investigation was conducted under powers granted by the act which, in part, authorizes the Commission at the request of a State Commission to

". . . investigate, or obtain any information regarding the business, financial condition, or practices of any registered holding company or subsidiary company thereof of facts, conditions, practices, or matters affecting the relations between any such company and any other company or companies in the same holding company system."

The State Commission had pending before it a rate proceeding, in the course of which question had arisen as to the cost of a power plant which had been constructed for a public utility company by a supplier of equipment. The equipment supplier, through the indirect ownership of securities, was an affiliate of the public utility company. The State Commission had doubts as to its jurisdiction over the equipment supplier and accordingly requested this Commission to conduct an investigation of the relationships between the utility and the supplier. The Commission ordered a private investigation and designated four senior staff members to conduct the inquiry. Hearings were held both in Washington and elsewhere. The State Commission was invited to have a representative attend the hearings, which were not open to the public, and a member of the State Commission did attend a portion of the hearings. Thereafter the Commission transmitted a confidential report of its investigators to the State Commission.

American Power & Light Company, a registered holding company in the Electric Bond and Share Company system, is under an order to liquidate and dissolve. On February 15, 1951, American notified the Commission of its intention to sell its entire interest in one of its subsidiaries, Washington Water Power Company, to certain public utility districts. Under the provisions of rule U-44 (c) promulgated under the act, the proposed divestment could be consummated without further proceedings unless, within 10 days after filing of the notice of intention, the Commission notified American that a declaration or other formal filing should be filed with respect to the proposed transaction. Thereupon the Commission issued an order to show cause in which, among other issues, the question was raised as to whether the Commission had jurisdiction to require American to file a declaration with respect to the sale of Washington Water Power to public utility districts. At the request of the State Commissions of Washington and Idaho the Commission moved its hearings to the territory affected in order to facilitate the presentation by local people of their views. Hearings were held in Spokane, Washington, at which a Commissioner of the Securities and Exchange Commission presided. The hearings were well attended, and any one who desired to be heard on the subject was given an opportunity to appear.

Green Mountain Power Corporation, a Vermont public utility company and a subsidiary of New England Electric System, made application pursuant to section 11 (e) of the act for approval of a plan of reorganization. The Vermont Commission was vitally interested in the whole program, and during the course of the proceedings its chairman and staff experts conferred with members of the Commission staff, resulting in a mutually helpful exchange of ideas. The Attorney-General of the State of Vermont appeared on behalf of the Vermont Commission at the hearings on the plan.

In August 1950 the Commission instituted proceedings pursuant to section 11 (b) (1) of the act directed to Wisconsin Electric Power Company and its subsidiaries. Wisconsin Electric Power Company is both a holding company and an electric utility operating company, with its property located in the State of Wisconsin. It also has a gas utility subsidiary and a transportation subsidiary, both operating in that state. Prior to a hearing in these proceedings representatives of the Commission's staff visited the offices of the Public Service Commission of Wisconsin and discussed the matter with members of its staff. Since the proceedings have been in progress, the scheduling of adjourned hearings has been made after determining what dates would be convenient for representatives of the State Commission, and copies of the transcript of testimony have been forwarded to it.

In connection with the preparation for hearing of proceedings under section 11 (b) (1) directed to General Public Utilities Corporation, to determine whether or not the company might retain its gas properties along with its electric properties, members of the Commission's staff visited the offices of the State Commissions of Maryland, Pennsylvania, New Jersey, New York, Massachusetts, Rhode Island, and Connecticut. This field trip was made for the purpose of obtaining statistical and other data regarding comparative cost of operations of manufactured gas utilities versus manufactured gas departments of predominantly electric utility companies. The Commission staff members were afforded full cooperation.

In the same case, but involving the question of the extent of the principal integrated electric utility system of General Public Utilities Corporation, an attorney and an engineer of the Pennsylvania Commission attended the Securities and Exchange Commission hearings as observers and had discussions with members of the latter Commission's staff with regard to the questions involved.

LITIGATION UNDER THE PUBLIC UTILITY HOLDING COMPANY ACT

During the fiscal year 1951 the Commission participated in 18 judicial proceedings involving issues arising under the Holding Company Act. Eleven of these proceedings concerned the enforcement of voluntary plans filed under section 11 (e) of the act, and the other seven were initiated by petitions to review orders of the Commission. Fifteen of these cases were finally adjudicated favorably to the Commission and the remaining three

were pending at the close of the fiscal year. Over the 16 years since enactment of the Holding Company Act, a total of 274 civil and criminal proceedings, exclusive of Bankruptcy Act proceedings, in which the validity or enforcement of the statute was in issue, have been initiated in the courts. Three proceedings were pending on June 30, 1951, and of the 271 which have been litigated to finality, only one case was terminated adversely to the Commission. In two other cases, decisions adverse to the Commission were vacated as moot. The Commission's activity in the courts during the 1951 fiscal year is shown in the following tables:

(chart omitted)

Actions to Enforce Voluntary Plans Under Section 11 (e)

Two applications for enforcement of voluntary plans were pending in United States district courts at the beginning of the fiscal year 1951. One of these plans related to the liquidation of Market Street Railway Co. The Commission had found that counsel for a preferred stockholders' committee was not entitled to receive a fee for his services since he had been acting in his own interest primarily rather than in the interests of the committee and of the company and that, although he had rendered valuable services, his failure to devote his time and efforts solely to the interests of his clients precluded him from being compensated for such services. [Footnote: Holding Company Act release No. 9376 (Sept. 30, 1949)] The district court agreed with the Commission on all phases of the plan except that which denied the attorney's fee and remanded the plan to the Commission for reconsideration. [Footnote: In re Market Street Railway Co., Unreported (N. D. Calif., No. 29,723, July 11, 1950)] The Commission took an appeal from the court's refusal to approve the denial of a fee, and a cross-appeal was also filed. The plan was then amended to separate into Step One the settlement of claims and the distribution of the major assets of Market Street, and into Step Two the attorney's application for a fee and certain other matters. The Commission approved Step One of the plan and reserved jurisdiction over Step Two. Upon application the district court approved Step One. [Footnote: Unreported (N. D. Calif., No. 29,723, Nov. 21, 1950)] An appeal from the district court's order was taken and was consolidated with the pending appeals. A stay was denied and Step One was consummated. These appeals were pending at the close of the fiscal year. The second plan provided for a partial liquidation of American Power and Light Company. The district court approved the plan without opinion and no appeal was taken.

Five applications for enforcement of voluntary plans were filed in United States district courts during the fiscal year. The first of these plans involved the question of what additional amounts, if any, should De paid to holders of certificates representing claims on $6 and $5 preferred stock of Electric Bond and Share Company which had been retired. The Commission decided, and the district court agreed, [Footnote: In re Electric Bond and Share Co., 95 F. Supp. 492 (S. D. N. Y., 1951)] that the holders of the $6 certificates were entitled to an additional $10 plus compensation for delay in receipt of

that amount, and that the $5 certificates were entitled to nothing more. Appeals were taken from the order of the district court and Bond and Share petitioned the Supreme Court to review the district court order. The Supreme Court denied Bond and Share's petition [Footnote: Electric Bond and Share Co. v. S. E. C., 341 U. S. 950 (1951)] and after the close of the fiscal year, the appeals were dismissed on stipulation of the parties.

One of the remaining four plans paralleled the Bond and Share case and presented the question what additional amounts, if any, should be paid to $7 and $6 prior lien preferred stockholders of New England Public Service Company. The Commission's determination that they should receive, respectively, $12.25 and $2.25 per share, plus compensation for delay, was confirmed by the district court and no appeals were taken from the enforcement order. [Footnote: In re New England Public Service Co., 94 F. Supp. 343 (D. Me., S. D., 1950)]

The third of these plans concerned the distribution of escrowed common stock of Interstate Power Company. The principal question presented was what participation should be accorded Ogden Corporation in its dual position as creditor and stockholder of Interstate vis-à-vis public security holders. The Commission found fair and equitable a compromise of the issues and the plan was approved by the district court. [Footnote: In re Interstate Power Co., Unreported (D. Del., No. 1003, 3-16-51). The Commission had approved and had applied for enforcement of a prior plan, but had requested and obtained a district court order remanding the proceeding for consideration of changed circumstances. See In re Interstate Power Co., 89 F. Supp. 68 (D. Del., 1950)] No appeal was taken from the Commission's order. A plan providing for a recapitalization of Green Mountain Power Corp. and a settlement of claims between Green Mountain and its parent, New England Electric System, was enforced without opposition. The remaining plan was pending in the district court at the close of the fiscal year.

Shortly before the close of the preceding fiscal year a plan of recapitalization of Eastern Gas & Fuel Associates had been approved by a district court. At the time of approval the court reserved jurisdiction to approve the amount at which the common stock of the company might be surrendered for which the stockholders would be paid in cash. The company petitioned for and was granted a supplemental order approving an amount of $11.00 per share as the settlement price.

Two plans were pending in United States courts of appeal at the beginning of the fiscal year. The first of these plans, approved by the Commission and the district court, involved the liquidation of The Commonwealth & Southern Corporation (Del.) in which the holders of option warrants were denied any participation. As originally submitted to the Commission this plan left undecided the disposition of residual assets of Commonwealth. Prior to consummation of the plan, it was amended to provide that the residual assets should be transferred to The Southern Company, a subsidiary holding company created to own the capital stock of certain former subsidiaries of Commonwealth. An investment banker's petition to intervene in the district court was

denied. During the fiscal year the court of appeals affirmed orders of the district court denying intervention [Footnote: In re Commonwealth & Southern Corp., 186 F. 2d 708 (C. A. 3, 1951)] and approving the plan, [Footnote: In re Commonwealth d Southern Corp., Adelaide H. Knight, Appellant, 184 F. 2d 81 (C. A. 3, 1950)] and petitions for writs of certiorari were subsequently denied. [Footnote: Knight v. Commonwealth & Southern Corp., et al., 340 U. S. 929 (1951)]

The second plan which was pending at the beginning of the fiscal year and which was affirmed related to an order of a district court which approved and enforced a plan for the dissolution of Federal Water and Gas Corporation. The appellants were officers, directors and controlling stockholders of a predecessor company, Federal Water Service Corporation, They asserted that the district court erred in approving that part of the plan which excluded them from participation as stockholders in the distribution of the assets of Water and Gas with regard to preferred stock of Water Service which they had acquired during the course of reorganization of Water Service. The Water Service plan had provided that they receive cash representing their cost of the Water Service preferred, and not new stock of Water and Gas, and the Commission's approval of that plan had been upheld by the Supreme Court. [Footnote: S. E. C. v. Chenery Corp., 332 U. S. 194 (194T), rehearing denied 332 U. S. 783 (1947)] The court of appeals held that the prior decision was *res judicata* and affirmed the district court enforcement order. [Footnote: In re Federal Water & Gas Corp., Chenery Corp., Appellants, 188 F. 2d 100 (C. A. 3, 1951)] The Supreme Court denied petitions for certiorari seeking review of the district court order [Footnote: Chenery Corp. et al. v. S. E. C. et al., 340 U. S. 831 (1950)] and of the court of appeals order. [Footnote: 341 U. S. 831 (1951)] At the end of the preceding fiscal year a court of appeals had reversed an order of a district court approving a plan for the reorganization of Long Island Lighting Company. [Footnote: Common Stockholders Committee v. S. E. C., 183 F. 2d 45 (C. A. 2, 1950)] Appellants had asserted on appeal that the Commission, in passing upon the plan of Long Island, had not given consideration to earnings which would accrue as the result of the reorganization and that in determining the fairness of the allocation of new securities the Commission had erred. The Commission petitioned for a modification of the decision of the court of appeals and for approval of the plan on the basis of a supplemental opinion showing that full consideration had been given to such benefits. The petition was granted during the fiscal year 1951. [Footnote: 183 F. 2d 52 (C. A. 2, 1950); certiorari denied 340 U. S. 834 (1950)] One proceeding involving reorganization plans of Niagara Hudson Power Corporation was pending in the Supreme Court at the beginning of the fiscal year. The Commission had held that the holders of option warrants were not entitled to participate in the reorganization. The district court had approved the plans, and the court of appeals had reversed the district court order on this one point. [Footnote: Leventritt v. 8. E. C., 179 F. 2d 615 (C. A. 2, 1950)] Petitions for a rehearing had been denied and the Commission and the company had petitioned for certiorari, which had been granted by the Supreme Court. During the fiscal year the Supreme Court reviewed the plan, reversed the order of the court of appeals and affirmed the order of the district court. [Footnote: S. E. C. v. Leventritt, 340 U. S. 336 (1951)]

Petitions to Review Orders of the Commission

Three petitions to review orders of the Commission were pending in United States courts of appeals at the beginning of the fiscal year and three petitions were filed during the fiscal year. In four cases the Commission's order was affirmed, and in the other two cases the appeals were dismissed.

Two of the petitions which were pending were from orders of the Commission approving various matters collateral to the reorganization of the Niagara Hudson Power Corporation system. The Commission had approved an application of The United Corporation to distribute approximately half of its holdings of Niagara Hudson common stock to its own common stockholders. The Commission's order was affirmed. [Footnote: Phillips v. S. E. C., 185 F. 2d 746 (C. A. D. C., 1950)] The other such petition sought review of an order of the Commission approving the exchange by United of common stock of Niagara Hudson for the capital stock of Niagara Mohawk Power Corporation, the surviving top company in the reorganization of the Niagara Hudson system. The appeal was dismissed without opinion. [Footnote: Phillips v. S. E. C., Unreported (C. A. D. C., No. 10,601, June 28, 1951)]

The third pending petition sought review of those provisions of an order of the Commission which denied a petition of a stockholder of International Hydro-Electric System for modification of a prior order directing the liquidation and dissolution of IHES. [Footnote: The order also approved a plan filed by the Trustee of IHES.] The Commission's order was affirmed. [Footnote: Protective Committee for Class A Stockholders v. S. E. C., 184 F. 2d 646 (C. A. 2, 1950)]

One of the three petitions filed during the fiscal year sought review of an order of the Commission which had denied a committee authority to solicit stockholders of The United Corporation for proxies in connection with a pending plan. The Commission found that the solicitation material contained false and misleading statements, and that the proposed solicitation would be detrimental to the pending reorganization proceeding. The Commission's order was affirmed. [Footnote: Committee for Common Stockholders v. S. E. C., 188 F. 2d 897 (C. A. 2, 1951)]

Another review proceeding was initiated by. two petitions seeking review of an order which granted to preferred stockholders of Federal Light and Traction Company an additional amount over that previously received, together with interest for delay in receipt of the payment. These petitions were consolidated on appeal. The court of appeals affirmed the Commission's order and certiorari was denied. [Footnote: Federal Liquidating Corp. v. S. E. C., 187 F. 2d 804 (C. A. 2, 1951), certiorari denied 341 U. S. 949 (1951)]

The third petition for review initiated during the fiscal year sought reversal of a Commission order which had denied the application of a registered holding company for an examiner's report with respect to the petition of the company in opposition to solicitation of stockholders. The appeal was dismissed for lack of jurisdiction. [Footnote: North American Co. v. S. E. C., Unreported (C. A. 2 (1950))] During the preceding fiscal year a United States court of appeals had affirmed an order of the Commission which prohibited a solicitation of voluntary contributions from stockholders to defray expenses of a committee. [Footnote: Halstead v. S. E. C., 182 F. 2d 660 (C. A. D. C. 1950)] During the fiscal year 1951 the Supreme Court refused to review the case upon a petition for a writ of certiorari. [Footnote: Common Stockholders Committee v. S. E. C., 340 U. S. 834 (1950)]

PART IV
PARTICIPATION OF THE COMMISSION IN CORPORATE REORGANIZATIONS UNDER CHAPTER X OF THE BANKRUPTCY ACT, AS AMENDED

Chapter X of the Bankruptcy Act provides a procedure for reorganizing corporations (other than railroads) in the Federal courts. The Commission's duties under Chapter X are, at the request or with the approval of the court, to participate in proceedings to provide the court and investors with independent expert assistance on the various legal and financial questions that arise in the proceeding and to prepare for the benefit of the courts and investors advisory reports on plans of reorganization. The Commission has no statutory right of appeal in a Chapter X proceeding, but it may participate in appeals taken by others.

COMMISSION'S FUNCTIONS UNDER CHAPTER X

The role of the Commission under Chapter X is different from that under the statutes which it administers. The Commission does not administer Chapter X. It acts in a purely advisory capacity. It has no authority either to veto or to require the adoption of a plan of reorganization or to render a decision on any other issue in the proceeding. The facilities of its technical staff and its recommendations are at the service of the judge and the security holders, affording them the views of experts in a highly complex area of corporate law and finance.

Generally, the Commission has sought to participate only in proceedings in which there is a public investor interest; $250,000 of publicly held securities is the rough guide used in deciding whether there is enough public interest to make it worth while for the Commission to participate. Sometimes the Commission has entered smaller cases, particularly when requested by the court, where public security holders are not

adequately represented, where it appears that the proceedings are being conducted in violation of important provisions of the Act, or where the Commission may otherwise be useful by participating.

Even where the public interest is too small to warrant active intervention by the Commission, the staff may follow a case and watch the course taken by the proceedings in order to make suggestions or comments on an informal basis when requested or when it is deemed desirable. Because of its nation-wide activity and its experience in Chapter X cases the Commission is able to respond to requests for help in the interpretation and application of the provisions of Chapter X. The Commission and its staff are often called upon by trustees or their counsel, other parties, referees, special masters, and judges for advice or comments.

SUMMARY OF ACTIVITIES

The Commission actively participated during the 1951 fiscal year in 64 reorganization proceedings involving the reorganization of 87 companies with aggregate stated assets of $774,252,000 and aggregate stated indebtedness of $498,184,000. During the year the Commission, with court approval, filed notices of appearance in 5 new proceedings under Chapter X. These proceedings involved 5 companies with aggregate stated assets of $3,243,000 and aggregate stated indebtedness of $3,028,000. At the close of the year, the Commission was actively participating in 53 reorganization proceedings involving 75 companies with aggregate stated assets of $729,402,000 and aggregate stated indebtedness of $454,852,000.

Some of the more important matters and issues with which the Commission was concerned during the last fiscal year in connection with its Chapter X functions are discussed in the following paragraphs :

Activities Relating to the Trusteeship

A fundamental feature of Chapter X is that in every case involving a corporation of substantial size an independent trustee is appointed to be primarily responsible for the operation of the corporation's business during the proceeding, to examine and evaluate the reasons for the debtor's financial difficulties, to appraise the ability and fidelity of its management and to formulate and file a plan of reorganization. The success of the reorganization depends largely on the thoroughness, skill, and loyalty with which he and his counsel perform their tasks. The Commission customarily examines the qualifications of trustees in the light of the standards of disinterestedness prescribed by the statute for trustees and their counsel.

In *Mosser v. Darrow*, a broadly significant case emphasizing the high fiduciary standards applicable to trustees, the Commission was upheld by the United States Supreme Court.

As reported in the Sixteenth Annual Report, the Commission had sought to surcharge a former trustee for profits made by his employees through trading in securities of the debtor's subsidiaries. The Court of Appeals for the Seventh Circuit reversed an order of the district court insofar as it surcharged the trustee. The Supreme Court in turn reversed the Court of Appeals and held that the trustee should be surcharged to the extent of the profits made by the trustee's employees. [Footnote: *Mosser v. Harrow*, 341 U. S. 267, 272 (1951)] In its opinion the Court pointed out that bankruptcy trustees are permitted no interest adverse to the trust because such interests "are always corrupting." Equity seeks, the Court stated, to avoid "delicate inquiries" into the conduct of trustees by exacting forbearance of all opportunities to advance their self-interest. Recognizing that "these strict prohibitions would serve little purpose if the trustee were free to authorize others to do what he is forbidden," the Court said: "We think that which the trustee had no right to do he had no right to authorize." To permit such conduct would, in the Court's opinion, open up opportunities for devious dealings in the name of others by the trustee. Answering the argument that a surcharge here creates a very heavy liability upon one who did not personally profit, the Court stated that, while courts are likely to protect trustees from disinterested mistakes in business judgment, a trusteeship is a serious business and is not to be undertaken lightly or so discharged, and that the most effective sanction for good administration is personal liability for the consequences of forbidden acts.

In one case, the Commission objected to the retention in office of a trustee who was also the court-appointed trustee of the debtor's parent corporation. The Commission pointed out that, since the parent company owned all the stock of the debtor, its position was adverse to that of the bondholders of the debtor and that the trustee stood in the position of the parent company and was thus subject to a conflict of interest. The Commission's recommendations were not taken by the district court. An appeal from the court's ruling was filed by a bondholder and is pending.

The statute permits the appointment of an "additional trustee" who may be a director, officer or employee of the debtor for the limited purpose of participating with the disinterested trustee in the operation of the business and the management of the debtor's property. The Commission has always held the view that this exception to the rule requiring a trustee to be completely independent and disinterested should not be used freely or loosely. It has been the Commission's position that the provision was intended only for the exceptional case where the services and experience of such a person are essential to the business operations of the trusteeship and would not otherwise be available; it was certainly not intended to detract in any degree from the fundamental purpose of eliminating management control of reorganization proceedings. During the past fiscal year, in the Chapter X case involving Ocean City Automobile Bridge Company the Commission had occasion to reiterate this position as *amicus curiae* in a brief before the Court of Appeals for the Third Circuit. The Commission also pointed out the dangers inherent in the appointment of additional trustees: the conflicts which may arise when business decisions affecting the interests of the management must be made,

the difficulties and embarrassment when the independent trustee must investigate the past conduct of such persons or their associates either in evaluating management or in determining whether causes of action exist. In accord with the Commission's view, the Court stated :

"The legislative history indicates that it was the intention of Congress that an additional operating trustee should be appointed only in those exceptional cases where the services of an individual who had been a director, officer or employee of the debtor were necessary to operate its business and manage its property and it was not feasible for the trustee to secure the services of the individual in question by employing him in the ordinary way. It was only in an unusual case of that kind that a director, officer, or employee of the debtor was to be appointed as an additional operating trustee."

The Court went further and held that, while an additional trustee may be an officer, director or employee of the debtor, he may not have any other conflicting relationship or interest as enumerated in the statute. Thus he may not be a creditor, stockholder, underwriter or attorney for the debtor or underwriter, or have any material interest adverse to any class of creditors or stockholders. The Court believed the exception for an "additional trustee" was not intended to open the door to persons who had a financial stake in the debtor's future which might make it difficult for them to act independently.

The Commission is also interested in assuring that the appointment of trustees does not in itself operate as a drain on the debtor's assets. In one case during the past fiscal year, the Commission felt that the continuation in office of two trustees was an unnecessary expense to the debtor. The two trustees had been appointed when the company was still in operation. Eventually, however, the business activities were terminated and the duties of the trustees became ministerial in nature. The business of the reorganization had become primarily a matter of the disposition of various claims in litigation. For this reason the Commission petitioned the court to reduce the number of trustees to one. The district court denied the petition and the question was appealed. The Court of Appeals for the Third Circuit reversed the lower court and directed that one of the trustees be removed.

Problems in the Administration of the Estate

One of the objectives of Chapter X is that judicial supervision of the reorganization process and creditor and stockholder participation therein is based upon complete and impartial information regarding the affairs of the debtor. Thus, the independent trustee, at the direction of the court, is required to investigate the acts, conduct, property, liabilities, and financial condition of the debtor, the operation of its business, and the desirability of the continuance thereof, and to transmit a report of his investigation to creditors and stockholders. Such reports aid the court in considering problems in the administration of the estate as well as the fairness and feasibility of a plan of reorganization, enable security holders and other parties to a proceeding to make helpful and effective

suggestions for a plan of reorganization and give security holders the necessary information to determine the desirability of accepting a proposed plan.

The Commission has continued its policy of consultation through its staff with trustees in connection with their investigations and the preparation of their reports. On the basis of its own investigations and its wide experience the Commission has been able to supply data and suggestions useful to the trustee. It has also continued to assist trustees in their investigation of possible claims against the old management and other persons.

In the Chapter X proceedings involving South Bay Consolidated Water Co., Inc., questions have been raised regarding the allowance of large debt claims asserted by New York Water Service Corporation, parent company of the debtor. These issues are still unresolved and may not require determination in view of the probable payment in full of the claims and interests of all public bondholders and preferred stockholders under a plan of reorganization with cash obtained from the condemnation of the debtor's property and from operations. The claims asserted by New York Water Service are based in part upon advances made to South Bay by New York Water Service and in part upon a note issued in 1931 by South Bay to Federal Water Service Corporation, which was the parent company of New York until 1947. New York Water Service acquired the note from Federal in 1947 as part of a divestment plan of Federal under the Public Utility Holding Company Act. New York Water Service paid $1,000 for the note, the principal amount of which was $227,000 with accrued interest of over $200,000. In addition to other defenses and counterclaims, investigation by the trustee, with the active assistance of the Commission's staff, revealed that if Federal had not made certain alleged excessive service charges, had not entered into certain real estate transactions in which South Bay sustained losses, and had paid to South Bay for certain properties the same price at which it contemporaneously sold those properties to New York Water Service, the large advances to South Bay would have been unnecessary and South Bay would not be faced with claims of over $1,000,000, including interest charges.

Claims directly against Federal arising out of the transactions mentioned above were asserted by the trustee and were settled by the payment of a substantial sum to South Bay. While the trustee and the Commission's staff were engaged in investigating the relationship of the debtor to New York Water Service and to Federal, the trustee was informed that Federal had proposed to compromise various claims that New York Water Service was asserting against Federal before the Commission under the Holding Company Act in connection with .the liquidation and distribution of Federal's assets. The proposal was to pay New York Water Service $250,000, including $7,000 to reflect minor claims presented by New York Water Service on behalf of South Bay. The trustee thereupon asserted his own claims on behalf of South Bay, based upon allegations respecting excessive service charges, over-payments for real estate sold to South Bay, underpayments for securities purchased from South. Bay, and claims that certain advances should have been made as equity capital investment. Negotiations ensued and an independent settlement was reached between Federal and the trustee of South Bay

under which South Bay was to receive $250,000. The settlement was approved by the Commission after a hearing upon notice under the Holding Company Act and by the District Court in the Chapter X proceeding.

During the past fiscal year one case presented a novel question arising put of the provisions of New York law. New York statutes provide that a corporate director who is the successful defendant in an action involving his directorship may assess his litigation expenses against the company. A director who had successfully defended an action brought by the trustee moved, under the authority of the statute, to assess his expenses against the trustee. The court held that assuming the statute to be applicable to an action brought pursuant to Chapter X the assessment could not be made because the statutory language did not provide for assessment against a trustee. The court did not, therefore, reach the question whether the statute constituted an encroachment on the jurisdiction of the bankruptcy court.

A recurrent question is whether the enterprise should be liquidated through a sale or continued as a going concern through an internal plan of reorganization. The Commission does not support the sale type of reorganization merely because of its simplicity or certainty of result, but urges a decision based upon what will yield the greatest benefit for creditors and stockholders. Where the decision has been made to sell the assets of the debtor, there has been some tendency to attempt to complete the sale as an administrative matter prior to, and not as part of, a plan of reorganization with its attendant safeguards for investors. The Commission has urged that where substantially all of the assets of the debtor are sold the sale should be a part of a plan of reorganization, unless some emergency is involved, such as the need to dispose of perishable property.

The Court of Appeals for the Third Circuit upheld the Commission's theory in *In re Solar Manufacturing Corp.* holding that no emergency is created when a prospective purchaser imposes a condition that his offer of purchase must be accepted within a short time. The Solar case was followed during the fiscal year in *In re American Bantam Car Co.* where the court, after hearing the Commission's argument, refused to set a hearing on a proposed sale. The judge advised the trustee that a plan of reorganization should be filed and if possible the purchase offer should be included in the plan. The Commission has consistently taken the position that when a sale is contemplated the trustee should develop competitive bidding by taking active affirmative steps in making known the availability of the property. Despite the fact that maintenance of competitive conditions, through public auction or otherwise, is called for in the best interests of security holders, the Commission has had occasion to overcome reluctance on the part of some trustees to develop real competition. The Commission has pointed out that even where the plan does not call for a public sale and competitive bidding, the plan may be successively improved by higher offers even after approval by the court and security holders.

Responsibilities of Fiduciaries

Assuring adherence to the high standards of conduct required of fiduciaries has continued to be one of the important activities of the Commission in Chapter X proceedings. We have indicated above our concern that the independent trustee be free from any conflicts of interest. The Commission is concerned also with the qualifications of other fiduciaries in the proceeding, such as indenture trustees, committees, attorneys, and other representatives of security holders.

In one case during the past fiscal year the Commission objected to the allowance of any fees to a firm of attorneys who had been subject to conflicting interests. The Commission pointed out that they had not only represented the petitioning creditors but also the debtor and the mortgagee in possession of the debtor's plant who was the debtor's landlord. In addition they represented the president of the debtor against whom the estate had a claim. The referee, following the Commission's suggestions, recommended that the attorneys be denied any fees. The court agreed that the rule of law required the disallowance of the attorneys' requests for fees. The same case also presented a different and unique question as to the allowance of fees. The president of the debtor requested compensation for his services as additional trustee of the debtor for the period up to his resignation. The Commission argued that there existed valid bases for the estate to assert claims against him because of his conduct as president prior to the proceeding and that the primary reason these claims were not pressed was the doubt that any judgment would be collectible. It was urged that the court had summary jurisdiction on an application for fees, in the circumstances here, to consider the clear liability of the president to the estate as offsetting any fee he might be entitled to. Both the referee and the court agreed with the Commission, and a fee was denied as in effect a set-off against the claims of the estate. The determinations in this case were affirmed after the close of the fiscal year.

Activities With Respect to Allowances

The Commission in its advisory capacity endeavors to protect the estate from excessive and inequitable charges for fees and expenses while at the same time providing fair treatment to applicants which will adequately compensate them for services rendered and encourage legitimate creditor and stockholder participation in the reorganization process.

The Commission itself receives no allowances from estates in reorganization. It attempts to obtain a limitation of the aggregate fees to an amount which the estate should fairly and can feasibly pay. In each case, the applications are carefully studied and recommendations are made in the light of applicable legal standards and, in general, on the basis of beneficial contributions to the administration of the estate and to the adoption of a plan of reorganization. Specific recommendations are made to the courts in cases in which the Commission has been a party and in which it is familiar with the services of the various parties and all significant developments in the case.

The Childs Co. case aptly illustrates the contribution the Commission may make in recommending allowances. Fees totaling $1,400,000 were requested; the Commission recommended approximately $750,000. The District Court originally awarded approximately $965,000, but on appeal the Court of Appeals for the Second Circuit reversed those allowances and, in remanding the case for further consideration, indicated that the Commission's recommendations, if adopted, would be considered affirmatively reasonable and properly allowable. At subsequent hearings in the District Court a substantial dispute existed over the proper interpretation of the opinion of the Court of Appeals. It was urged by various applicants that under the appellate court's decision, the District Court had discretion to allow more than the amounts recommended by the Commission if special findings were made showing the necessity therefor. The District Judge, however, doubted the propriety of increasing the recommended allowances and, following the suggestion of the appellate court, adopted the Commission's recommendations. The Court pointed out that there were no new facts or conclusions presented to him but that there was simply a disagreement as to the value of the services rendered, a matter upon which the Court of Appeals had plainly issued its mandate.

The matter of allowances frequently involves the application of section 249 which prohibits compensation or reimbursement of expenses where an attorney or other fiduciary has purchased or sold the securities of the debtor. In proceedings in the Chicago Surface Lines and Chicago Rapid Transit cases, the Commission objected to the allowance of fees and expenses for some participants on various grounds, among which was the fact that they had bought or sold securities during the proceedings. The Commission argued that these transactions were in contravention of the equitable rule which was codified by Section 249. The special master, overruling these objections, allowed fees and expenses to many of these applicants, and the District Court later affirmed the master's conclusions. The Court's action was based on its position that the reorganization proceeding had commenced as an equity receivership proceeding, had not come under Chapter X until 1944, and that, absent the strict application of Section 249, the Court had discretion as to whether to bar or permit compensation. In this respect, the decision is in conflict with other decisions.

The Commission has sought a rigid adherence to the provisions of Section 249 in a field where the underlying principles might easily be whittled away by exceptions and hardship cases. Supporting the Commission's position, strict application of Section 249 was made by the District Court in Norwalk Tire & Rubber Company case. The Commission urged that the application of the secretary of a debenture holders' committee be denied because his firm participated in several transactions involving securities of the debtor during the reorganization. The court stated that, while it felt that these transactions generally could be considered *de minimis*, the rigidity of Section 249 required that the request for fees be rejected.

We have mentioned above the matter of denial of fees to attorneys who represented conflicting interests in the American Acoustics case. In such cases, the denial of fees is a

prophylactic measure designed to implement the basic rule against divided loyalties and to assure that services will be rendered in the proceeding by those with a single-minded devotion to their cause. In the International Railway Company case, at the instance of the Commission, a bondholders committee had been held to be disqualified and was forced to withdraw because it had been organized by a management group with interests adverse to those of the public bondholders. Upon the presentation of applications for final allowances, members of this committee and their counsel were denied any fee for their services or reimbursement of expenses by the District Court in affirmation of the principle prohibiting fees to those subject to a conflict of interest in the reorganization proceeding.

During the past fiscal year, several cases presented the question of the propriety of awarding interim allowances prior to the completion of the reorganization proceedings. The matter of interim allowances presents the court with the difficult task of determining whether and in what amount the estate may safely make payments on account of administration costs prior to the completion of the reorganization. Since the extent of beneficial contribution to the administration of the estate or to the adoption of a plan of reorganization is the primary measure of the value of services rendered to the estate, an applicant's efforts cannot properly be evaluated until the proceeding is substantially completed. This fact militates against the allowance of interim fees except in the most unusual circumstances, and then only in a small amount. Where the trustee and his counsel devote a substantial portion of their time to the reorganization, they may require, as a matter of necessity, the payment of some money as current income. To secure adequate services by them it may be desirable to permit interim allowances, but even in such cases the Commission feels that interim payments ought not to be generous, otherwise procrastination and unnecessary work will be encouraged against the best interests of the debtor.

This position was upheld by the Court of Appeals for the Third Circuit in *In re McGann Mfg. Co.* The District Court had allowed interim fees and expenses to the trustee and his counsel, to counsel for the debtor, and to a committee. The Commission was not a party to the proceedings. On appeal, the Commission presented its views as *amicus curiae*. In reversing the District Court, the Court of Appeals stated that interim allowances are justified only where a trustee or his counsel regularly devotes a portion of his time, daily or weekly, to the affairs of the estate, especially where the trustee operates a business, but that interim allowances are not justified where the duties performed by them are not substantial. Pointing out that the trustee's activities were routine and ministerial in nature, the Court of Appeals held that the grant of interim allowances to the trustee and his counsel was an abuse of discretion. As to applicants other than the trustee and counsel, the Court agreed that only under extraordinary circumstances should interim allowances be granted to them, particularly since the proper measure of compensation to them is the benefit derived by the estate from their services which can normally be evaluated only after consummation of the reorganization. Hence the Court reversed the lower court on this point also.

Subsequently, in the Solar Company case, the Court of Appeals for the Third Circuit upheld, as a matter of judicial discretion, an allowance by the district judge of interim allowances to the trustees and their counsel. In its opinion, however, the Court stated that if it were exercising its own judgment in the first instance it would not have made an allowance to the trustees although it would to counsel who, it found, had done a great deal of work during the year. The trustees, on the other hand, were no longer operating a business and their duties had become simpler. However, the Court of Appeals did not feel it could substitute its own judgment for the District Court because the trustees had expended a great deal of time on the case.

An instance where unusual circumstances may warrant the awarding of interim allowances is represented by the American Fuel & Power Company case. There, the efforts of a committee and its counsel contributed substantially to the recovery of assets for the benefit of the estate. A great amount of time was spent over a period of many years, the services partook of the nature of trustee's services because the committee and its counsel took the laboring oar in the litigation, the efforts were successful, and, although a plan of reorganization had yet to be approved, the recovery of the fund was assured. In these circumstances the Commission felt that an interim allowance well below what might be allowed as a final fee could properly be made. The District Court has not yet acted upon the application.

PLANS OF REORGANIZATION UNDER CHAPTER X

The formulation and consummation of a fair and feasible plan of reorganization is, of course, the primary purpose of the proceeding under Chapter X. Accordingly, the most important function of the Commission under Chapter X is to aid the courts in achieving this objective.

Fairness of Plan

Basic to the Commission's approach to questions involving the fairness of reorganization plans under Chapter X is the fixed principle, firmly established by Supreme Court decisions, that full recognition must be accorded to claims in the order of their legal and contractual priority either in cash or in the equitable equivalent of new securities and that junior claimants may participate only to the extent that the debtor's properties have value after the satisfaction of prior claims or to the extent that they make a fresh contribution necessary to the reorganization of the debtor. A valuation of the debtor is essential to provide a basis for judging the fairness as well as the feasibility of proposed plans of reorganization. In its oral statements and in its advisory reports the Commission continues to urge that the proper method of valuation for reorganization purposes is primarily an appropriate capitalization of reasonably prospective earnings.

In connection with the fairness of plans and the treatment of claims against the estate, the Commission has given careful consideration to situations where, because of mismanagement or other misconduct on the part of a parent company or a controlling or affiliated person, the claims of the parent or affiliate should be subordinated to the claims of the public investors or these claims limited to cost. All the facts and circumstances in these instances are investigated since they form an integral part of the concept of the "fair and equitable plan. Questions of this kind assumed importance in several proceedings during the past fiscal year. In *In re Inland Gas Corporation*, the Court of Appeals for the Sixth Circuit had rendered a decision directing subordination of the claims of Columbia Gas System, Inc. to those of all other creditors. In the subsequent formulation of a plan the question arose whether Columbia's claims in Inland Gas Corporation should be subordinated to those of the public creditors of American Fuel & Power Co. and Kentucky Fuel Gas Co., which companies owned almost all of the stock of Inland Gas Corporation but practically no other assets. The District Court read the mandate of the Court of Appeals to require only that Columbia's interest in each corporation be subordinated to the other creditors of such corporation. This determination was appealed to the Court of Appeals and that Court was asked to interpret its prior holdings.

The Commission's position that the American Fuel system should be viewed as an integrated enterprise was upheld by the Court. The Commission urged that all public security holders of the three companies had been injured by Columbia's conduct and that the Court should interpret its former mandate to require the subordination of Columbia's claims not only to the claims of Inland's own creditors but also to those of American Fuel and Kentucky Fuel. The Court found that the holders of the notes secured by Inland stock were, in a very true sense, creditors or quasi-creditors of Inland and as such were entitled to participate in Inland's assets as creditors prior to Columbia. Having found a creditor status in Inland Gas for the American Fuel and Kentucky Fuel creditors, the Court did not make any provision for the slight Inland Gas stock interest (1.4 percent) held by public investors, as recommended by the Commission.

The Commission took the opposite position with respect to a contention, in the Inland Gas Corporation case, that the claims of American Fuel against Inland Gas, its majority-owned subsidiary, be subordinated or treated as capital contributions because of the under-capitalization of Inland Gas. Except for a single situation calling for limitation to cost, the Commission pointed out that the relationship between the two companies did not call for treatment of American Fuel's claims different from that of other creditors. No mismanagement or overreaching was shown; American Fuel was organized by the promoters of the system after Inland Gas was created and the American Fuel creditors were in the position of advancing funds to Inland Gas at a time when it needed capital badly; American Fuel creditors ought not equitably to be charged with the conduct of the promoters. The Court of Appeals agreed that this did not present a case for subordination and affirmed the holding of the District Court.

In the International Power Securities Corp. case an issue regarding subordination and limitation to cost was resolved by a settlement incorporated in a plan of liquidation which was recommended as fair and feasible by the Commission and approved by the Court in May 1951. The debtor had been organized to finance the development of hydro-electric power in Northern Italy and deal generally in the investment of funds. Its major assets became mortgages on the property of an Italian public utility, Societa Edison of Milan, and its income was largely the interest paid on those obligations. In 1940 it became impossible for the Societa Edison to make dollar payments, and the debtor consequently could not make interest payments on its own bonds, outstanding in the principal amount of more than $16,000,000. A petition for reorganization was filed in February 1941. After World War II Societa Edison sent a representative to this country to discuss that company's affairs and settlement of the debtor's claims against it. It was then learned that Societa Edison had acquired a large amount of the debtor's bonds at a substantial discount. It was subsequently alleged that while the representative was in this country, Societa Edison had purchased $1,250,000 principal amount of the debtor's bonds. These and other purchases would bring the total holding of Societa Edison in the debtor's bonds to $6,543,000 principal amount. Meanwhile agencies of the Italian government acquired $1,098,000 principal amount of the bonds from Italian nationals.

It was contended by a bondholders' committee that these bond-holdings should be limited to cost or subordinated completely to publicly held bonds or applied as a set-off because Societa Edison's relationship to the debtor and its bondholders was such that it could be considered the real obligor of the debtor's bonds, or at least a guarantor of them. Proceedings were commenced to determine the ownership and status of the bonds and orders were obtained from the court directing Societa Edison and the Italian Government to file claims. An application to restrain the transfer of the $1,250,000 of bonds in the custody of a bank in this country, however, was denied. On appeal the Court of Appeals for the Third Circuit reversed, holding that the injunction was within the jurisdiction of the court and that it was error for the court not to prevent the transfer of the bonds until the issues respecting their ownership and status were determined. Societa Edison did not file its claims, but proceeded with an offer of settlement. After extensive negotiations, a proposal was made under which the Italian Public Credit Institute would settle Societa Edison's obligations by the- issuance of $26,600,000 of bonds, equal to principal and interest of the Italian company's mortgage debt. For their holdings of the debtor's bonds of about $11,000,000 including interest, Societa Edison and the Italian Government agencies were to be allowed a credit of only $8,600,000, leaving $18,000,000 of Institute bonds to go to the American bondholders. In addition, interest and amortization terms of the proposal were made more favorable than other Institute bond issues as part of the settlement.

The trustee's plan, based upon acceptance of this settlement, contemplates issuance of liquidation trust certificates to bondholders upon which payments will be made by a trustee out of the funds received upon the Institute bonds held by the trustee until the bondholders are fully paid, principal and interest. The balance of payments starting in

1967, which would normally have been paid to the preferred stockholders of the debtor, in accordance with their priority, will, under the plan, become the property of the holders of subordinated liquidation trust shares. These subordinated shares will be purchased for investment by Italian interests for a net sum of $1,190,000 which, under the plan, will be apportioned between bondholders and preferred stockholders in compromise of their claims to this cash. The Commission did not render a formal advisory report, but informed the Court in a full oral presentation that it considered the plan fair and equitable. Thereafter the Court approved the plan. The required majorities of the bondholders and preferred stockholders voted in favor of the plan and in June 1951 it was confirmed by the Court.

In our Sixteenth Annual Report, we described in some detail the proceedings involving Silesian-American Corporation. We discussed the trustee's plan which incorporated a proposal by Swiss banks for the acquisition by them of securities of the proposed reorganized company, the transfer to the debtor of certain funds held by them to enable a cash distribution to be made to public bondholders, and the release of claims of the debtor against the banks. We also discussed the Commission's advisory report which concluded that the trustee's plan was unfair and unfeasible in important respects and that other plan proposals were either not fair or not feasible. We pointed out that the District Court had overruled our recommendations except for some minor points and that appeals had been taken by a bondholders' committee and other parties from the District Court's order approving the trustee's plan.

During the past fiscal year, the Commission actively participated in this appeal before the Court of Appeals for the Second Circuit, urging that the District Court committed error in approving the trustee's plan. In an elaborate detailed opinion, the Court of Appeals reversed the lower court's order. The case is of particular significance in the field of bankruptcy reorganizations because of the clear statement of the important weight which should be accorded advisory opinions of the Commission. The Court stated:

"* * * Since decision here is so highly a matter of judgment, indeed of shrewd appraisal of what may he the possibilities of lengthy litigation as against an immediate smaller payment in hand, we obviously cannot find any sure or pat answer. The trustee naturally urges that we must give strong weight to the decision below, suggesting that it must be sustained as a finding of fact based on the preponderance of credible evidence, and therefore not "clearly erroneous" under F. R. 52 (a). But we are not justified in thus oversimplifying this difficult problem, so much more one of forecasting the future than of restating the past. Naturally careful consideration is due the conclusion of the able district judge who has had this lengthy reorganization so long under his control. At the same time we cannot overlook the fact that the governmental agency charged with substantial responsibility in the premises, the Securities and Exchange Commission, has made an extensive investigation resulting in a detailed and helpful report with a reasoned conclusion which the trial judge has rather summarily rejected. If the considered findings of this agency, with so much better facilities for investigation than those possessed by

either this or the trial court, are to have any force beyond their initial impact below, then we think that they will largely offset the usual presumption accorded a decision of first instance. Otherwise much of the statutory purpose in creating an expert body for the consideration of technical problems will be set at naught. Compare 6 Collier on Bankruptcy Par. 7.30, 14th Ed. 1947. We have elsewhere stressed the importance of due regard for Commission findings, Finn v. Childs Co., 2 Cir. 181 F. 2d 431, 438; and we are clear that here, too, we must give weight to the detailed evaluation of the facts made by this reliable and experienced public agency and the conclusion reached, even though this was not accepted by the trial judge."

After discussing the history of the debtor and its affairs and the terms of the Swiss offer and the trustee's plan, the Court set forth the Commission's position at length "both because of its statutory responsibility and because of the thoroughness with which it has worked out its position." The Court then analyzed the principal issue in the case, the causes of action against the Swiss banks, and concluded, as had the Commission, that there was lack of an adequate showing that the adjustment with the Swiss banks embodied in the trustee's plan was fair or just, particularly in the light of what seemed to be strong indications to the contrary. The case was therefore remanded for further proceedings. The Court did not prescribe what these should be, indicating that a new plan might be substituted or action against the Swiss banks instituted here or in Switzerland. In any event, the Court directed that some detailed examination be made of the Swiss transactions, Swiss law and the position of the Swiss Government agency in charge of the transactions.

In view of this conclusion, the Court did not finally determine other issues in the case but as an aid to a reappraisal of those issues, commented upon them. The Court felt that certain claims of the debtor against a German mining company were uncollectible in point of fact. As to the correctness of the trustee's decision not to sue promoters of the debtor, the Court was divided in view, stating that it was clear that the promoters realized large profits but that it was not clear from the record whether the promoters, as charged by the Commission, were liable for a misleading bond circular, a write-up of the debtor's Polish assets and overvaluation of those assets and prospects. The suggestions of the Commission not followed by the lower court as to the details of the plan, including the issuance of contingency certificates to those who gave value for their securities, seemed to the Court to have merit.

In our Sixteenth Annual Report, we outlined the status of the reorganization proceedings involving Central States Electric Corporation, an investment company owning and controlling directly and through two subsidiaries assets of over $50,000,000. We mentioned the important problems involved in the effectuation of a plan of reorganization for the Central States system; the treatment of some of these problems in our advisory report on five proposed plans of reorganization; the adoption by the District Court of the Commission's recommendation that the trustees' plan be approved and other plans be disapproved; and the denial by the District Court of a request to stay a preliminary step

involving the dissolution of American Cities Power & Light Corporation, one of the subsidiaries, pending an appeal to the Court of Appeals for the Fourth Circuit. Briefs were filed and argument held on this appeal during the past fiscal year in July 1950. The Court of Appeals upheld the Commission's view of the case in a detailed opinion handed down in August 1950.

The Court dismissed the plans of reorganization proposed by certain junior security holder groups as objectionable "for reasons which the Commission has very clearly pointed out."

As to the contention of common stockholders that the case should be delayed until litigation against the former management shall be terminated, the Court quoted from the Commission's advisory report that "to request delay when immediate reorganization is practicable is to disregard the rights of creditors, as well as senior stockholders, * * * and to continue to subject them to the risk of loss." As to the argument that the trustees' plan of reorganization proposing a single open-end investment company for the system was a "liquidation," the Court agreed with the Commission that there was no basis for this conclusion, stating "This is just the sort of matter as to which the Securities and Exchange Commission is best qualified to judge and no good reason is suggested which would warrant the courts in substituting their judgment as to this for the expert judgment of the Commission." That stockholders might exercise their option under the charter of the reorganized company to redeem their stock was found not objectionable for another reason, since, as the Court stated, it is not the purpose of Chapter X to compel security holders to continue a business if they, the owners, desire otherwise.

On the question of valuation, the Court upheld the Commission's view that the proper method of valuing the assets of an investment company such as Central States is not prospective earnings but the realizable market value of the securities on hand. The Court pointed out that the case was to be distinguished from that of a business corporation where the value of the unit as a whole often exceeds the value of the separate parts due to the unitary functioning of all parts as a whole. The Commission's advisory report and brief were quoted from with approval.

The Court affirmed the holding that the senior preferred stockholders were entitled to share in the assets of the debtor on the basis of their liquidating preferences prior to junior stockholders and distinguished the line of cases under the Public Utility Holding Company Act where the rights of preferred stockholders are generally not considered matured. The Court also approved the plan provision which allocated additional compensation to the bondholders amounting to 5 percent of their claim because of their loss of seniority in the reorganized company through the issuance to them of new common stock.

The Commission filed a brief in opposition to petitions to the Supreme Court for writs of certiorari. The same contentions were raised by the junior interests, excluded from

participation in the physical assets of the debtor, that they raised in the courts below. Certiorari was denied in January 1951. In the meantime, the trustees' plan of reorganization was confirmed by the District Court as recommended by the Commission over the objection of the junior interests. An appeal to the Court of Appeals from the order of confirmation was dismissed. Thereafter certain common stockholders moved to dismiss the entire proceeding on the ground that the debtor was solvent and could pay its debts (debentures of $22,000,000, principal plus interest) through a sale of assets or by borrowing or a combination of both. The Commission opposed the motion to dismiss on the grounds that this issue had been decided in the prior appeal; that the need for and practicability of reorganization is the basic test to determine whether a case should be dismissed or not and not whether a debtor is or has become solvent; and that the reorganization of solvent debtors in need of rehabilitation is expressly contemplated by Chapter X. The District Court denied the motion. On appeal, the Commission filed a brief and argued in support of the order denying the motion. The Court of Appeals affirmed on several grounds. Of broad import in Chapter X is the Court's opinion that "the idea that jurisdiction over reorganization proceedings is lost because of a fortunate administration of the corporation's assets under the Court's direction is supported neither in law nor in common sense and is violative of the well settled rule that a court of equity, having once taken jurisdiction, will do complete justice in the premises." The Court of Appeals also pointed out that to dismiss the proceedings would have meant turning back control of the company to the former management against whom suit for a substantial sum was pending and that such a course was "hardly thinkable."

The Court of Appeals refused a stay of the proceedings, stating that for persons holding insignificant interests in so large an enterprise to hold up and delay a plan where the security holders having substantial interests had given their approval and the Commission, the District Court and that Court had likewise given their approval, is an abuse to which the Court would lend no encouragement. The mandate was directed to be issued in fifteen days unless application for certiorari were made to the Supreme Court. The common stockholders did apply for certiorari and the Commission, among other parties, filed a brief in opposition. Certiorari was denied in June 1951.

Thereafter the plan of reorganization was speedily consummated. A new open-end investment company, called Blue Ridge Mutual Fund, Inc., emerged as the reorganized company, resulting from the merger of Central States Electric Corporation and its subsidiary, Blue Ridge Corporation. American Cities Power and Light Corporation, another subsidiary, had been dissolved during the previous year. Common stock of the new company was distributed to the bondholders and 7 percent preferred stockholders of Central States and to the common stockholders of Blue Ridge in accordance with their interests. The new company commenced operations with about $45,000,000. Bequests for redemptions, which will substantially reduce the assets of the company, may be offset by sales of new stock. As permitted by the plan, an underwriting arrangement and a management contract were entered into, with the approval of the Court, with Reynolds and Company, an investment banking and securities firm. The new contracts were

reviewed by the Commission, not only from the point of view of Chapter X standards, but also to assure compliance with the Investment Company Act of 1940. It is contemplated that the new company will make a continuous offering of its stock as is the practice of other investment companies of this type. The Commission also closely reviewed the charter and bylaws of the new company to see that proper safeguards in the interests of investors were incorporated therein.

Feasibility of Plan

A prerequisite to the court's approval of a plan of reorganization is its feasibility. In order to assure a sound reorganization, which will not result in the debtor's return to Chapter X because of financial difficulties, the Commission gives a great deal of attention to the various factors affecting feasibility. Generally speaking, these factors involve the adequacy of working capital, the relationship of funded debt and the capital structure as a whole to property values, the adequacy of corporate earning power for interest and dividend requirements, the possible need for capital expenditures, and the effect of the new capitalization upon the company's prospective credit. The Commission's views of feasibility as relating to various types of enterprises have been announced in some detail in its advisory reports. Although no advisory reports were issued during the past fiscal year, the Commission's views on the subject of feasibility were expressed orally in several cases along lines previously set forth in its published reports.

Consummation of Plan

The Commission gives detailed scrutiny to the corporate charters, by-laws, trust indentures, and other instruments which are to govern the internal structure of the reorganized debtor. In general the Commission strives to assure to investors the inclusion of protective features and safeguards which its experience has shown to be desirable.

The Commission's interest in the entire reorganization process includes not only the consummation of the plan and the winding up of the affairs of the trusteeship (which may occur many years after a plan has been consummated) but may also extend to the interpretation and enforcement of the terms of the plans by the reorganized company. The value of such continued interest was shown by the decision of the Third Circuit Court of Appeals in *In Re Pittsburgh Terminal Coal Corp*., discussed at length in the Sixteenth Annual Report. During the past fiscal year, application for certiorari to the Supreme Court from this decision was opposed by the Commission on the ground that the decision of the Court of Appeals was correct in applying to the facts of this case the established principle that a bankruptcy court has jurisdiction to protect its decrees, to interpret, enforce and carry out the plan of reorganization and to prevent interference with the plan or its operation. The Commission also urged that the decision was not in conflict with other decisions and distinguished the decisions relied upon by the petitioner which held in general, that the Chapter X Court has no power to interfere in the affairs of a corporation after a plan has been consummated. The Supreme Court denied certiorari.

Another matter in connection with the consummation of plans of reorganization which has been of concern to the Commission is the problem of unexchanged securities. The Commission found that many security holders had not submitted their old securities in exchange for new securities or cash distributable under the plan. Chapter X provides that a period of not less than 5 years may be fixed by the judge within which security holders may make the exchange under the plan, after which they are barred. After some experience with the operation of this provision, the Commission concluded that, in the larger cases, 5 years may be too short a period, depending on the facts, and recommended a bar period of 10 years.

More important than the lengthening of the exchange period, the Commission believes that efforts to locate security holders must be intensified in order to reach as many investors as possible. The Commission has, therefore, urged trustees, exchange agents, and others who have the responsibility for distributing the new securities or cash, to send registered letters with return receipts requested, to publish notices in leading newspapers, and to retain professional tracers in the business of locating missing security holders.

PART V
ADMINISTRATION OF THE TRUST INDENTURE ACT OF 1939

NATURE OF TRUST INDENTURE REGULATION

The Trust Indenture Act of 1939 requires that bonds, notes, debentures, and similar securities publicly offered for sale, sold, or delivered after sale through the mails or in interstate commerce (except as specifically exempted by the Act) be issued under an indenture which meets the requirements of the Act and which has been qualified with the Commission.

Individual holders of bonds, notes, debentures, and similar debt securities often find it difficult and expensive to enforce their rights under indentures and generally must rely upon the trustee named in the trust indenture to protect them. The Trust Indenture Act of 1939 requires the inclusion in the trust indenture of specified provisions which facilitate the protection and enforcement of such rights. Thus there must be a corporate trustee free from stated conflicts of interest; such trustee must not after default, or within 4 months prior thereto, improve its position as a creditor to the detriment of the indenture securities; it must make annual and periodic reports to bondholders; it must maintain bondholders lists to provide a method of communication between bondholders as to their rights under the indenture and the bonds; and it must be authorized to file suits and proofs of claims on behalf of the bondholders. The Act prohibits exculpatory clauses used in the past to eliminate the liability of the indenture trustee to the indenture security holders and imposes on the trustee, after default, the duty to exercise the rights and powers vested in

it, and to use the same degree of care and skill in their exercise as a prudent man would use or exercise in the conduct of his own affairs. Specified evidence must be supplied by the obligor to the indenture trustee with respect to the recording of the indenture and with respect to conditions precedent to action to be taken by the trustee at the request of the obligor.

INTEGRATION WITH SECURITIES ACT OF 1933

The exemption provisions of the Trust Indenture Act of 1939 incorporate most of the exemptions contained in the Securities Act of 1933 and include certain other exemptions. The provisions of these Acts are so integrated that registration pursuant to the Securities Act of 1933 of securities to be issued under a trust indenture and not exempt from the Trust Indenture Act of 1939, is not permitted to become effective unless the indenture conforms to the requirements of the latter Act, and such an indenture is automatically "qualified" when registration becomes effective as to the securities themselves. An application for qualification of an indenture, covering securities not required to be registered under the Securities Act of 1933, which is filed with the Commission under the Trust Indenture Act is processed substantially as though such application were a registration statement filed pursuant to the Securities Act of 1933.

STATISTICS OF INDENTURES QUALIFIED

The Commission's work involved in the examination and qualification of indentures, like other phases of its securities regulatory activities mentioned elsewhere in this report, increased in volume during the 1951 fiscal year. During the year there were filed for qualification under the Trust Indenture Act 109 new indentures representing an aggregate amount of $2,025,131,091 of debt securities, compared with 96 filings representing $1,741,775,670 in the 1950 fiscal year. More detailed statistics follow:

(chart omitted)

During the 1951 fiscal year the following additional material relating to trust indentures was filed and examined for compliance with the appropriate standards and requirements:

Statements of eligibility and qualification under the Trust Indenture Act: 128

Amendments to trustee statements of eligibility and qualification: 5

Supplements S-T, covering special items of information concerning indenture securities registered under the Securities Act of 1933: 98

Applications for findings by the Commission relating to exemptions from special provisions of the Trust Indenture Act: 6

Reports of indenture trustees pursuant to sec. 313 of the Trust Indenture Act: 659

CHANGE IN FORM

Amendment of Form T-3. -- During the 1951 fiscal year the Commission amended Form T-3 to add a requirement that there be filed as an exhibit to applications for qualification of indentures on this form a copy of each prospectus, notice, circular, letter or other written communication which is to be distributed to security holders generally in connection with the issuance or distribution of the indenture securities. The reason for requiring the filing of this material is to facilitate the Commission's examination of such applications.

PART VI
ADMINISTRATION OF THE INVESTMENT COMPANY ACT OF 1940

The Investment Company Act of 1940 requires registration of, and provides for certain types of regulation of, investment companies -- companies engaged primarily in the business of investing, reinvesting, and trading in securities. Among other things, the Act requires disclosure of the finances and investment policies of these companies in order to afford investors full and complete information with respect to their activities; prohibits such companies from changing the nature of their business or their investment policies without the approval of their stockholders; bars persons guilty of security frauds from serving as officers and directors of such companies; regulates the means of custody of the assets of investment companies and requires the bonding of officers and directors having access to such assets; prevents underwriters, investment bankers, and brokers from constituting more than a minority of the directors of such companies; requires management contracts in the first instance to be submitted to security holders for their approval; prohibits transactions between such companies and their officers and directors except with the approval of the Commission; forbids the issuance of senior securities of such companies except in specified instances; and prohibits pyramiding of such companies and cross-ownership of their securities. The Commission is authorized to prepare advisory reports upon plans of reorganizations of registered investment companies upon the request of such companies or 25 percent of their stockholders and to institute proceedings to enjoin such plans if they are grossly unfair. The Act requires face amount certificate companies to maintain reserves adequate to meet maturity payments upon their certificates.

REGISTRATION UNDER THE ACT

During the 1951 fiscal year, 12 new investment companies registered under the Investment Company Act of 1940, of which 5 were open-end management companies (companies which redeem their shares on presentation by the stockholders) and 7 were closed-end management companies (companies in which the shareholder can realize on his security only by selling it in the open market). During the nearest comparable period for which data are available, the 12 months ended March 31, 1951, about 211 registered open-end management and closed-end management investment companies reported to the Commission sales to the public of approximately $594,000,000 of their securities and redemptions and retirements of approximately $336,000,000, leaving a net investment by the public in such companies over the period of approximately $258,000,000. As of June 30, 1951, 368 investment companies were registered under the Act, and on that date it is estimated that the value of their total assets was approximately $5,600,000,000. This represents an increase of approximately $1,000,000,000 in such valuation over the corresponding total at the beginning of the year.

The 368 investment companies registered at June 30, 1951, are classified as follows:

Management open-end: 154

Management closed-end: 105

Unit: 94

Face amount: 15

Total: 368

CHARACTER OF INVESTMENT COMPANIES REGISTERED DURING FISCAL YEAR

As indicated, 12 investment companies registered under the Act during the fiscal year. Of these, five were open-end management investment companies actively offering their securities to the public. One of these companies stressed as an advantage the fact that it charged no sales load in the purchase of its shares. Another proposed a so-called formula of investment designed to require purchase and sales of securities on the happening of specified events. As a result of examination by the Commission's staff, the prospectus of the company as finally used makes it clear that the so-called formula is not infallible and that losses can result from investment in the company.

None of the closed-end management companies registered during the year is offering or intends to offer its securities to the public. One of such companies was created in

connection with a merger of companies manufacturing locomotives and other heavy machinery as a repository for certain securities not necessary to the operation of the business of the combined companies. The stock of the investment company so formed was distributed to the stockholders of the locomotive company. Thus the investment company became publicly held and was required to register under the Act. Some others of the newly registered companies were created for similar reasons.

The remaining companies were required to register because of the fact that during the fiscal year the number of their stockholders reached 100 or more, thus removing the exemption in the Act for investment companies having less than 100 stockholders. The most interesting of these companies is Delaware Realty and Investment Company which owned approximately 33 percent of the voting securities of Christiana Securities Company, which in turn owned 27 percent of the common stock of E. I. du Pont de Nemours & Company, one of the country's largest industrial concerns.

SELLING LITERATURE

The Act requires literature (other than the statutory prospectus) used by issuers or underwriters in selling open-end investment company shares to be filed with the Commission within 10 days after such literature is first employed as selling material. During the preceding 1950 fiscal year there had been a substantial increase in the use of both literature purporting to describe investment companies generally and literature purporting to describe a specific company. Of considerable concern to the Commission was the fact that in a substantial number of cases this literature used by issuers, underwriters, and dealers to attract investors might be materially misleading in many respects. In addition, there was serious doubt that certain of such literature could be generally circulated under the Securities Act of 1933. Accordingly, before the beginning of the 1951 fiscal year the Commission with the cooperation of the National Association of Securities Dealers undertook a study of such literature in an attempt to eliminate any misleading elements contained therein. During the 1951 fiscal year there was promulgated, as a result of the cooperative effort of the Commission and the National Association of Securities Dealers, a Statement of Policy governing the contents of such literature. In addition, during the 1951 fiscal year, the Commission and the National Association of Securities Dealers worked out a procedure for submission of selling literature to staff members for scrutiny as to compliance with the Statement of Policy before such literature is used.

Furthermore, after considerable discussion the Commission permitted the use under certain circumstances of charts indicating the performance of investment companies as selling literature provided such charts were contained in a, standard book of reference, reflected the performance of a substantial number of investment companies, were prepared uniformly on a non-misleading basis, and were exhibited as a book to investors.

During the 1951 fiscal year, discussions were initiated between the National Association of Investment Companies and the Commission with a view to simplifying the registration requirements for such companies under the Securities Act and Investment Company Act, the objective being to obtain a short readable prospectus which would nevertheless fully inform investors as to the facts with respect to the particular company.

STATISTICAL DATA

The number of documents filed under the Act by registered investment companies during the fiscal years ended June 30, 1950 and 1951, together with other related statistics, are tabulated below:

(chart omitted)

APPLICATIONS FILED

One of the functions of the Commission under the Act is to pass on applications by investment companies for exemptions which the Act permits under appropriate standards.

Some of the most complex problems arise out of the provisions of the statute which forbid, in the absence of approval by the Commission, purchases or sales of property or securities among investment companies and their affiliated persons. To approve such transactions the Commission must find that they are fair as to price and involve no overreaching. As a result, the applications in many instances involve unusual questions of valuation and inside influence. During the year 21 applications of this type were filed.

During the fiscal year 78 applications were filed under the various provisions of the Act, 62 of these for orders of the Commission relating to exemption from requirements of the Act, and the remaining 16 for a determination of the Commission that the applicant has ceased to be an investment company within the meaning of the Act. At the beginning of the fiscal year 34 applications were pending. These pending applications, together with the 78 filed during the year, totaled 112 applications which required the appropriate examination and consideration of the Commission during the year. As a result of the Commission's action 71 of these applications were disposed of during the year and 41 were pending on June 30, 1951. The various sections of the Act under which these applications were filed, and the disposition of the applications during the fiscal year, are shown in the following table (since an application may involve more than one section of the Act, the numbers are not totaled):

(chart omitted)

CHANGES IN RULES, REGULATIONS, AND FORMS

Bonus, profit sharing and pension plans. -- Section 17 (d) of the Act authorizes the Commission to promulgate rules designed to prevent unfair use of their position by insiders to engage in joint transactions with the investment companies they manage or with companies controlled by such investment companies. To carry out this purpose the Commission in 1946 enacted rule N-17D-1 which in effect required submission to and approval by the Commission of bonus, profit sharing and pension plans granted by investment companies or their controlled companies for the benefit of officers or employees, prior to their adoption. During the last fiscal year, as a result of the Commission's experience with the original rule, it was amended to eliminate the necessity of prior submission to the Commission of a variety of bonus, profit sharing and pension plans. Among such plans no longer required to be submitted to the Commission for approval are pension plans for employees of investment companies in which the company's contributions are based on a percentage of annual payroll and the plan has been qualified as non-discriminatory under section 165 of the Internal Revenue Code. Similarly, all bonus, pension or profit sharing plans of companies controlled by investment companies (other than other investment companies) are exempted if no affiliated persons of the controlling investment company participate in the plans. Finally, payments of bonuses up to 5 percent of the net income of the investment company, giving effect to any net unrealized depreciation in its assets, may be paid without the necessity of approval by the Commission. It is believed that these amendments to the rule will substantially lessen the administration burden of both the Commission and registered investment companies, without sacrifice of adequate protection to investors in such companies.

Registration form for face-amount certificate companies -- The Commission during the year adopted a form of registration statement to be filed under the Act by registered face-amount certificate companies. These companies offer to investors certificates entitling their holders to a definite sum of money at the end of a prescribed period upon payments by the investor during such period, usually in monthly installments, of sums aggregating less than the amount to be paid by the company at maturity. The Act requires the companies to maintain reserves invested in qualified investments sufficient to meet the face amount of certificates held by investors at maturity. The new form, among other things, requires pertinent information to enable the Commission to determine whether such reserves are being maintained by the companies.

In addition to the new form a rule was adopted permitting the use of information previously filed by face-amount certificate companies with the Commission under the Securities Act of 1933 or section 15 (d) of the Securities Exchange Act of 1934. Both the form and the rule were previously published in draft form for comments and suggestions by the companies affected and other interested persons. Extended conferences were held with the representatives of some of the companies affected and the form adopted by the

Commission reflects the incorporation of a number of comments and suggestions so received.

Bonding of officers and employees of investment companies -- The Act empowers the Commission to require the bonding of officers and employees of registered investment companies who have access to securities owned and other assets of such companies. Pursuant to such statutory authority the Commission had adopted rule N-17G-1. During the fiscal year the Commission amended rule N-17G-1 by adding to such rule a definition of the terms "officers" and "employees." The amendment provides that for the purposes of this rule such terms shall include the depositor or investment adviser and its officers and employees in cases where the investment company is an unincorporated company managed by a depositor or investment adviser.

PART VII
ADMINISTRATION OF THE INVESTMENT ADVISERS ACT OF 1940

The Investment Advisers Act of 1940 requires the registration as investment advisers of persons engaged for compensation in the business of advising others with respect to securities. The Commission is empowered to deny registration to or revoke registration of any adviser who, after notice and opportunity for hearing, is found by the Commission to have been convicted or enjoined because of misconduct in connection with security transactions or to have made false statements in his application for registration. The Act makes it unlawful for investment advisers to engage in practices which constitute fraud or deceit; requires investment advisers to disclose the nature of their interest in transactions executed for their clients; prohibits profit-sharing arrangements; and, in effect, prevents assignment of investment advisory contracts without the client's consent.

Statistics relating to registration of investment advisers, fiscal year ending June 30, 1951

Effective registrations at close of preceding fiscal year: 1,043

Applications pending at close of preceding fiscal year: 13

Applications filed during fiscal year: 121

Total: 1,177

Registrations cancelled or withdrawn during year: 107

Registrations denied or revoked during year: 0

Applications withdrawn during year: 3

Registrations effective at end of year: 1,057

Applications pending at end of year: 10

Total: 1,177

Approximately 258 registered investment advisers represent in their applications that they engage exclusively in supervising their clients' investments on the basis of the individual needs of each client. The services of about 341 others are chiefly through publications of various types. 235 investment advisers are registered also as brokers and dealers in securities. Most of the remainder offer various combinations of investment services.

PART VIII
OTHER ACTIVITIES OF THE COMMISSION

COURT PROCEEDINGS

Civil Proceedings

Complete lists of all cases in which the Commission appeared before a Federal or State court, either as a party or as *amicus curiae*, during the fiscal year, and the status of such cases at the close of the year, are contained in the appendix tables.

At the beginning of the 1951 fiscal year there were pending in the courts 18 injunctive and related enforcement proceedings instituted by the Commission to prevent fraudulent and other illegal practices in the sale of securities, 21 additional proceedings were instituted during the year and 19 cases were disposed of, so that 20 of such proceedings were pending at the end of the year. In addition the Commission participated in a large number of reorganization cases under Chapter X of the Bankruptcy Act; in 15 proceedings in the district courts under section 11 (e) of the Public Utility Holding Company Act and in 14 miscellaneous actions, usually as *amicus curiae*, to advise the court of its views regarding the construction of provisions of statutes administered by the Commission which were involved in private lawsuits. The Commission also participated in 41 appeals. Of these, 8 came before the courts on petition for review of an administrative order; 17 arose out of corporate reorganizations in which the Commission had taken an active part; 2 were appeals in actions brought by or against the Commission; 9 were appeals from orders entered pursuant to section 11 (e) of the Public Utility Holding Company Act; and 5 were appeals in cases in which the Commission appeared as *amicus curiae*.

Certain significant aspects of the Commission's litigation during the year are discussed in the sections of this report devoted to the statutes under which the litigation arose.

Criminal Proceedings

The statutes administered by the Commission provide for the transmission of evidence of violations to the Attorney General who may institute criminal proceedings. The Commission, largely through its regional offices, investigates suspected violations and, in cases where the facts appear to warrant criminal proceedings, prepares detailed reports which are forwarded to the Attorney General. Commission employees familiar with the case often assist the United State attorneys in the presentation to the grand jury, the conduct of the trial, and the preparation of briefs on appeal. The Commission also transmits parole reports prepared by its investigators relating to convicted offenders. Where an investigation discloses violations of statutes other than those administered by the Commission, the Commission advises the appropriate Federal or State agency.

Indictments were returned against 2,133 defendants in 477 cases developed by the Commission prior to June 30, 1951. [Footnote: In discussions of criminal cases In previous annual reports the figure used for the number of defendants indicted was the sum of the number of defendants in all indictments returned. The figure currently used reflects an adjustment for the situation occasionally occurring where indictments which included common defendants were tried together. A similar adjustment has been made for the figure used for the number of defendants convicted. These adjustments eliminate seeming inconsistencies between figures previously appearing in the text and comparable figures contained in the appendices.] These figures include 48 defendants in 24 cases in which indictments were returned during the past fiscal year. At the close of the fiscal year 436 cases had been disposed of as to one or more defendants. Convictions had been obtained in 381 of these cases, over 87 percent, against a total of 1,135 defendants. [Footnote: The 55 remaining cases, which resulted in acquittals or dismissals as to all defendants, Included a number where the indictments were dismissed because of the death of defendants involved.] Convictions were obtained against 15 defendants in 12 cases during the past fiscal year. [Footnote: One of these cases is still open as to one defendant.] In addition, one defendant was convicted of criminal contempt during this period. A judgment of conviction was affirmed on appeal as to one defendant during the year, and two cases, each involving a single defendant, remained pending on appeal at the close of the fiscal year.

As in prior years, the criminal cases during the past year which were developed and prosecuted covered a wide variety of promotions. They included fraudulent securities sales in connection with the operation of purported investment plans, in connection with the promotion of various mining, oil and gas ventures, and in connection with the promotion of inventions and other new businesses. They also included frauds perpetrated by securities brokers and dealers and their representatives upon customers. In many of these fraudulent schemes, the defendants wilfully avoided compliance with the

registration provisions of the Securities Act of 1933, which are designed to provide investors with a full and fair disclosure of material facts about the securities being sold. As a result, a number of fraud cases involved violation of these registration provisions. In addition, in two indictments returned during the past year the charges were based solely on the violation of these registration provisions.

The fraudulent sale of securities in connection with the operation of purported investment plans was involved in the following criminal proceedings during the past year: *U. S. v. Frederick F. March* (N. D. Ill.) ("secret" financing plan); *U. S. v. Robert J. Gottle* (D. Mass.) (securities trading account); U. S. v. Jim May (S. D. Tex.) (grain trading venture); *U. S. v. Russell G. Hanson* (N. D. Ill.) (securities trading financing plan); and *U. S. v. Mercedes Buschman et al.* (W. D. Wash.) (note discounting plan). The defendants in the first two cases were convicted oil charges of obtaining funds from investors upon the representation that they would be used for legitimate investment purposes, whereas in fact the defendants converted such funds and used them in large part for gambling purposes. Similar fraudulent conduct is alleged in the Hanson case, in which an indictment was returned during the past year. The conversion of investors' funds also was involved in the May case, where the defendant was convicted during the past fiscal year. The indictment pending in the Buschman case, charges, among other things, that the defendants induced investors to purchase accommodation notes which the defendants had fraudulently obtained from various persons, upon the false representation that such notes had been issued by financially responsible persons and represented payments due on stock sold to these persons. In all of these cases the defendants also were charged with employing the fraudulent "Ponzi" technique, in that, in order to induce investors to make further investments, they returned to them as "profits" a portion of their capital contributions.

Convictions involving mining promotions were obtained during the past year in *U. S. v. Charles Phillips* (W. D. Tex.); *U. S. v. Lawrence L. Kelling* (D. Kan.) and *U. S. v. James Reese Dams, Sr. et al.* (D. Idaho). The sale of securities in Mexican gold mining and lumber ventures known as Orozona, S. A. & Transconstruccion, S. A. was involved in the first case and the second case related to the sale of pre-organization subscriptions of a corporation to be organized to develop a coal mine in Colorado. The indictments in these cases charged the defendants with misrepresenting the use which was to be made of the funds received from the sale of these securities and various other matters. In the last .case, Davis pleaded guilty to charges of violation of the registration provisions of the Securities Act in the sale of notes issued by him and secured by an interest in the production from certain mining properties located in Idaho and Oregon. Indictments were returned during the year in two other mining promotion cases: *U. S. v. Ernest R. Hennefer et al.* (D. Utah) and *U. S. v. William B. LaVey et al.* (D. Mont.). The former case related to the development of phosphate properties and involved the sale of stock of Utah Phosphate Company. The latter case involved the sale of stock of Victory Divide Mining Company in connection with a gold mining venture. The defendants in these cases were charged with making false representations with respect to the nature, amount and value of

the ore deposits controlled by these companies, the value of the stock, the profits which investors would receive and other matters. After the close of the fiscal year, convictions were obtained against certain defendants in each of these cases.

The fraudulent sale of securities relating to the promotion of various oil and gas properties resulted in convictions during the year in *U. S. v. George E. Baldwin* (N. D. Ill.); *U. S. v. Stacey Benderson* (W. D. Tenn.); and *U. S. v. Emory Stokes* (E. D. Tex.). The indictments in the first two cases alleged misrepresentations with respect to such matters as the quantity of oil production being obtained, the period in which investors would receive repayment of their investments and the amount of profits which they would receive. In the Stokes case, the defendant was charged with falsely representing, among other things, that he would act as agent for investors in purchasing oil and gas leases and that the amounts paid by investors for such leases represented the amounts he had paid to landowners' to obtain these leases. The indictment returned during the year in *U. S. v. Lawrence L. Kelling et al.* (D. Kan.), a pending case, includes charges of misrepresentation with respect to the amount of oil being produced.

After the close of the fiscal year, a conviction was obtained in *U. S. v. S. E. J. Cox et al.* (N. D. Okla.), another oil promotion fraud case in which an indictment was returned during the past year. The defendant Cox, who had a record of four previous federal convictions for oil and mining frauds, was convicted of fraudulently selling stock of Penner Oil & Gas, Inc. by means of a large scale mail campaign. Proof at the trial showed that at one time during the course of this promotion some 28 stenographers were employed to work on the company's sales literature and that orders for the printing of such literature called for as many as 58,000 pieces' per printing. According to the indictment some of the false representations made in these sales letters were that one block of leases controlled by the company should produce over 6,000,000 barrels of oil having a value in excess of $15,000,000, that another block of leases should yield a net profit of $7,000 per acre and that a net profit of $3,000,000 could be obtained from still other acreage. It was further charged that the defendant failed to disclose to investors that the "special process," which was represented as having been used in locating wells drilled by the company, was an instrument commonly known as a "doodle bug," based upon no scientific principle.

The fraudulent sale of stock in connection with the promotion of so-called "Road-A-Scopes," a device proposed to be installed along highways which purportedly would enable motorists to see around curves and over hills, resulted in the indictment during the year in *U. S. v. James P. Anderson et al.* (D. Ariz.). Among other things, it was charged that the defendants falsely represented that the proceeds from stock sales would be deposited in a trust account to be used only for the purpose of manufacturing and installing the Road-A-Scope device and that the defendants made false and extravagant statements regarding the income to be received from advertising placed on the Road-A-Scope device and failed to disclose to investors that the promotional company had never received any advertising revenues or other income except in a nominal amount. The

promotion of an allegedly new type of lawnmower was involved in *U. S. v. James D. Bobbroff et al.* (D. Nev.), where the indictment charged misrepresentations, among other things, with respect to the use which was to be made of the funds received from investors and the status of production of the lawnmowers involved. Convictions were obtained after the close of the fiscal year in both of these cases.

Misrepresentations with respect to the use of funds as well as numerous other matters are included in the fraud charges contained in the indictment in *U. S. v. Siegfried Bechhold et al.* (S. D. Fla.), a pending case, which involved the sale of stock and franchises of Ribbonwriter Corporation of America in connection with the promotion of a typewriter attachment device, known as "Rib-N-Rite," which allegedly would make duplicate copies by means of ribbons and thus eliminate the use of carbon paper.

The promotion of a small loan business at Jackson, Mississippi, resulted in a conviction during the year in *U. S. v. Paul A. Schumpert et al.* (S. D. Miss.), where the indictment charged fraud in the sale of stock of the National Acceptance Corporation. Among other things, this case involved payment of purported dividends to facilitate the sale of stock, without disclosure that such dividends had not been earned but were being paid out of capital and actually represented a partial return of the investors' own funds.

After the close of the fiscal year convictions were obtained against a number of defendants in *U. S. v. Alejandro D. Llanos* (D. Hawaii), in which the indictment alleged a wide-spread scheme to defraud residents of the Territory of Hawaii, principally plantation laborers, in connection with the sale of securities issued by the defendant Alejandro D. Llanos and others associated with him in what was loosely called "Llanos and Company." In the sale of these securities, it was charged that the defendants falsely stated to investors that the funds received from them would be wagered on "fixed" volley ball games or, in other instances, would be invested in various business enterprises with a guarantee against loss, or that the funds were needed to meet expenses in order to accomplish the withdrawal and distribution of millions of dollars among the "members of Llanos & Company." In this connection, according to the indictment, the defendants falsely represented, inter alia, that the defendants controlled a prominent California shipbuilding company, which was indebted to Llanos in the amount of $6,000,000 and that the Llanos group also had on deposit in an Hawaiian bank an additional $6,500,000 and that these tremendous sums ultimately would be distributed among the persons investing in "Llanos & Company."

Convictions involving securities brokers and dealers and their representatives were obtained during the year in *U. S. v. Wade F. Coley* (W. D. S. C.). where it was charged that the defendant while insolvent operated a securities business, converted customers' funds and securities, maintained false and fraudulent books and records, made false representations to representatives of the Commission and filed false and misleading financial statements with the Commission; and in *U. S. v. Eugene F. Luck* (S. D. Fla.) and *U. S. v. Paul R. Warwick, Jr.* (N. D. Tex.), in which cases the conversion of customers'

monies or securities constituted a part of the frauds charged. Similar fraudulent conversions are charged in the indictments returned during the year in *U. S. v. Richard E. Slaugenhaupt* (W. D. Pa.) and *U. S. v. Sidney W. Tuttle* (E. D. Pa.). After the close of the fiscal year, the defendant in the latter case was convicted.

In *U. S. ex rel S. E. C. v. Josiah Marshall Kirby* (N. D. Ohio), the defendant Kirby was convicted of criminal contempt, for continuing to act as an over-the-counter securities broker and dealer, without being registered under section 15 (a) of the Securities Exchange Act of 1934, in violation of preliminary and final injunctive decrees obtained in 1948 and 1949, respectively.

The indictment returned during the year in *U. S. v. Eldridge S. Price* (N. D. Ohio), charged violations solely of the registration provisions of the Securities Act of 1933, in connection with the sale in large amount of investment contracts involving oil and gas lease assignments on lands located in Runnels County, Texas. In this case it was charged that during a period of almost three years the defendant had caused to be carried through the mails for sale and delivery after sale to numerous purchasers investment contracts, evidenced by oil and gas lease assignments, coupled with collateral promises that oil wells would be drilled to prove the acreage involved, when no registration statement was in effect as to such securities with the Commission. After the close of the fiscal year, the defendant was convicted on these charges. In *U. S. v. G. L. Lloyd* (N. D. Ill.), a pending case, involving the former Chairman of the Board of Nu Enamel Corporation, an indictment was returned during the year, charging violations by Lloyd of the registration provisions of the Act in connection with sales of his stock of this corporation.

In the only appellate case involving criminal prosecution decided during the fiscal year, *Allen v. U. S.*, 186 F. 2d 439 (C. A. 9, 1951), certiorari denied 341 U. S. 948, the defendant's conviction for the fraudulent sale of securities in connection with the promotion of a number of mining companies was sustained.

COMPLAINTS AND INVESTIGATIONS

The Commission is authorized to conduct investigations and, except in criminal prosecutions, to institute and pursue its own remedies. In the main, these are injunctive actions in the United States District Courts or administrative proceedings before the Commission. Where criminal prosecution is sought the evidence is referred to the Department of Justice and the United States attorneys.

Information leading to investigations comes from varied sources. Frequently, violations are indicated by material required to be filed with the Commission, such as registration statements, annual and quarterly reports, ownership reports, etc. Other Federal agencies. State authorities and official and unofficial bodies concerned with finance and law enforcement cooperate in informing the Commission of suspected violations. However,

members of the investing public who write to the Commission or call at its offices to make inquiry or register complaints account for the bulk of the Commission's investigations. During the 1951 fiscal year, 10,100 letters were received relating to possible violations of the Securities Act and the Securities Exchange Act. In addition, many complaints were received by telephone and by personal interviews.

Letters and calls received and handled by the ten regional offices are not included.

The primary responsibility for investigation rests with the Commission's regional administrators whose investigators conduct most of the field work. The principal office also temporarily assigns personnel to assist regional offices in investigations.

Investigations are classified by the Commission as preliminary investigations and docketed cases. A preliminary investigation is one of limited scope for the purpose of determining whether a full scale investigation is warranted. If so, it becomes a docketed case. In many situations, it is determined at the outset that an extensive investigation is warranted and a docketed investigation file is opened. During the fiscal year, 1951, the Commission instituted a total of 665 new investigations. Of these, 367 were preliminary and 298 were docketed. In addition, 60 cases which were opened as preliminary were later docketed. During the same period, 413 investigations were closed, leaving 1,109 as the total of all investigations pending at the end of the fiscal year.

Many preliminary investigations are carried on by telephone, through correspondence, office research or limited interviews and often disclose violations of a minor nature not necessitating further investigation or the use of any sanction. Such violations, for the most part, occur either because of a lack of knowledge of the Federal securities laws or misinterpretation of these Acts. When such persons learn they are violating the law, they usually are quite willing to agree to take necessary corrective steps without the use of sanctions. This procedure serves the dual purpose of effectively preventing the continuance of minor violations and at the same time educating the public concerning the requirements of the Securities Acts. The following are examples, among many, of this type of case:

The controlling interest in a large chain of grocery stores was held by members of the same family. The chief stockholders, through underwriters, sold a considerable portion of their stock although not enough to transfer control out of the family. While the distribution was continuing, the chief stockholders were informed by representatives of the Commission that they were violating the law. They immediately cancelled all sell orders and, at considerable expense to themselves, were able to reverse most of the transactions. One of the brokers also bought back a considerable block of stock at a loss. In view of the good faith of the subjects in attempting to correct their error and the lack of substantial damage to the public, no action was taken.

In another instance, information reached the Commission that a committee representing a minority group of a Central European country was offering bonds for sale within the United States to ex-nationals of that country. Investigation disclosed that, while some of such persons had been solicited to purchase bonds, actual sales were *de minimus*. Those responsible denied any intent to violate the law, discontinued solicitation and returned the purchase price to the few who had responded to the offering. Hence the Commission took no action.

If the preliminary investigation shows the need of further inquiry, a case is docketed and a full and detailed investigation is made. The Commission has power to issue subpoenas and administer oaths to witnesses for the purpose of conducting investigations and may delegate such power to members of its staff. This power is used only when the investigation could not otherwise proceed. In each such instance, the facts disclosed by preliminary investigation and the reasons why subpoena power is necessary are presented orally to the Commission. If the Commission decides that proceeding by subpoena is justified, it issues an order which designates officers with the power to subpoena records, administer oaths and take testimony. Such power is limited to the specific subject matter of a particular investigation.

During the fiscal year 1951 the Commission delegated subpoena power by issuance of formal orders of investigation in 47 cases. Of these, 32 related solely to possible violations of the registration and anti-fraud provisions of the Securities Act of 1933 and possible violations of the Securities Act were included in seven other orders which also involved indicated violations of the Securities Exchange Act of 1934, the Investment Company Act of 1940 and the Investment Advisers Act of 1940. Seven orders related only to possible violations of the Securities Act of 1934 and one solely to the Investment Advisers Act.

When an investigation has been completed, a report is submitted to the appropriate Regional Administrator who, after review, forwards it to the principal office with his recommendation. That recommendation may take any one of several forms, among which are (1) reference to the Department of Justice for criminal action, (2) the institution of injunctive or other proceedings in the civil courts, (3) administrative action by the Commission, or (4) reference to another agency or department of the Federal Government or to State authorities, for appropriate action. In each instance, the report and recommendation of the Regional Administrator is reviewed by the staff of the Commission's principal office and the matter is then presented to the Commission in detail. All formal investigations (where subpoena power has been authorized) or where the Commission has officially taken some other action such as reference to the Department of Justice, are again presented to the Commission and reviewed by them before the files are ultimately closed.

In some instances, complaints appeared to involve violations of law but, upon investigation, did not justify action. As an example, the Commission received several

letters from stockholders of a long-established oil and gas producing company claiming that its management had entered into a deal to sell its stock to another company at a price which was inadequate. The minority stockholders had received the same offer but had not been given adequate information on which to base an informed judgment as to the acceptance of the offer. Investigation established that the price offered to minority stockholders was substantially over the market, that the deal between the controlling stockholders and the buyers had been negotiated at arms' length on the basis of competent reports by geological engineers as to the value of the underlying assets and that no violation of the Securities Act was involved.

In another case, information reached the Commission that the bonds of a Central American republic had been sold within the United States in violation of the registration provisions of the Securities Act of 1933. Various persons in the securities industry and others reported rumors that a large amount of such bonds were being sold or were about to be sold within the United States. Investigation disclosed that, while various American firms had from time to time submitted proposals to finance, by the sale of bonds, a program to develop the natural resources of the country, none had, as yet, materialized and no public offering of bonds had been made. The interested parties were instructed concerning applicability of the Securities Act to any future transactions involving public distribution of bonds in the United States. Some contractors and others who had received bonds for work and services apparently had contemplated disposing of them in this country without registration. Their plans were abandoned when it became known that the Commission was investigating the matter. The Commission's files in the matter were made available to the Bureau of Internal Revenue at its request in connection with possible violations of the tax laws.

In another instance the Commission received information that Chinese Communist interests, through their sympathizers in this country, were conducting a campaign to sell their bonds in the United States. This was reported to be a part of a larger movement throughout the world to force the sale of these bonds to persons of Chinese extraction under threat of reprisal against their relatives in China. Detailed investigation failed to disclose concrete evidence of the public offering or sale of such bonds within the United States, and therefore the matter was not subject to the jurisdiction of this Commission. However, in the course of the investigation, the Commission cooperated with the Federal Bureau of Investigation and other agencies charged with security protection and made its files available to them for security purposes.

Complainants sometimes seek personal retaliation rather than public benefit. A typical case occurred when an attorney complained to one of the Commission's regional offices that the stock of a cooperative apartment corporation had been sold in violation of the registration and fraud provisions of the Securities Act of 1933. The statement was sufficiently convincing to require detailed examination of books and records of the corporation and the taking of testimony from various witnesses. However, it turned out that no violations of law or other irregularities were involved, that the complainant was a

discharged employee of the corporation who had stated that he would "get even -- if it took all his life" and had made complaints not only to the Commission but to the Attorney General of the State and the District Attorney of the County.

The Commission enforcement investigations are confidential and no information may be divulged to persons other than Commission employees unless the Commission itself makes it public. Private litigation often arises from the same subject matter as Commission investigations. Frequently, litigants ask for the Commission's evidence to assist their causes. Such requests are denied unless unusual and compelling reasons require a contrary course. Such cases are extremely rare. However, the Commission, upon request, in proper cases makes its evidence available to Federal and state law enforcement authorities. Also, Committees of Congress have been provided with evidence touching upon subjects under their inquiry. Among these were the Senate Committee to Investigate Organized Crime in Interstate Commerce.

The Commission maintains constant liaison with other Federal and state enforcement agencies in the securities field. During the past fiscal year, the Commission opened its confidential investigation files in 19 cases to such agencies. In other cases, where the subject matter involves apparent violations of both Federal and state laws, the Commission's investigators and those of state securities authorities jointly conduct the investigation which may result in both state and Federal action. Also, a constant exchange of information as to securities enforcement action is maintained with state and Canadian authorities. The following are concrete examples of this type of cooperation:

In a typical case the subject of investigation who had formerly been convicted of grand larceny in New York in connection with a securities transaction and was also permanently enjoined from engaging in the securities business in that state was found to have sold approximately $15,000 worth of oil royalties to persons with whom he had come in contact in his business of sending food packages and cash to persons in Germany as agent for their friends. In these sales, the value of the oil royalties had been grossly misrepresented. The state authorities requested that the Commission turn its evidence over to them. While technically a violation of the fraud provisions of the Securities Act of 1933 was involved, essentially it was a local matter and lent itself to prosecution in the state courts. The Commission opened its files to the state authorities and permitted one of its investigators to testify, as a result of which charges were preferred against the defendant in the New York State Court, charging various violations of the state securities laws.

In another case, the Commission's investigation disclosed that the subject had swindled a Nebraska farm widow of approximately $18,000 in the sale of securities. Concurrently, the Nebraska authorities learned of the incident and requested access to the Commission's files. It appeared that the matter was one which lent itself more readily to state than Federal prosecution and the Commission made its evidence available to and otherwise cooperated with the state. As a result, the Governor appointed a special prosecutor who

obtained a conviction of the defendant, who was sentenced to twelve years in the State Penitentiary. The Assistant Director and Counsel of the Bureau of Securities in Nebraska described the cooperation between the Commission and his Bureau in part as follows:

There has always been a fine relationship and cooperation between the two agencies and the Securities and Exchange Commission has rendered a very valuable service in all of these matters which has permitted the obtaining of evidence beyond our control.

In summary, during the fiscal year, the Commission's investigative staff processed thousands of complaints and other communications, as a result of which 665 new investigations were undertaken. At the beginning of the period, 857 investigations were carried over. Within the year, 413 investigations were closed, leaving a total of 1,109 investigations pending at the end of the year. While only a comparatively small percentage of such investigations resulted in the imposition of coercive sanctions or reference for criminal prosecution, the effectiveness of the Commission's investigative activities may not be measured by this standard alone.

One of the principal results of the Commission's investigative activity has been the prevention of violation of the Federal Securities laws and the continuing education of the public and the investment industry in the application of those statutes and coercive sanction in all cases involving technical violations of the law has been found not to be necessary adequately to protect investors and serve the public interest.

(chart omitted)

Sales of Canadian Securities Within the United States

For many years, the Commission has attempted to stop the sale of unregistered Canadian securities in the United States. In all cases involving mass-mailing campaigns and telephone selling of such securities that we have been able to investigate fully, we have found the sales to be attended by fraudulent methods; in virtually all such cases the securities have proved to be worthless. Although evidence sufficient to convict the sellers of violations of the registration and fraud provisions of the Securities Act of 1933 is obtained in these instances, the Commission's efforts have been in a large measure thwarted because the existing extradition treaty with Canada does not permit rendition of the violators to the United States authorities for prosecution.

Practically all such illegal offerings emanate from Toronto, Ontario, and the securities are sold through intensive mail and telephone campaigns over the border to all parts of the United States. During the past two years, the Commission has obtained evidence establishing that upwards of 200 such unregistered Canadian issues have been offered for sale within the United States. The sales pattern is uniform and simple, though apparently convincing to many United States investors. The victim is first solicited by mail, told of the great money-making possibilities of the mine or oil well involved, and asked merely

to send his name and address on a prepaid post card. Within a few days he receives a telephone call from Toronto in which he is promised large and immediate profits if he invests at once. The salesman usually tells the victim that oil, gold or uranium (depending on the promotion) has just been discovered in large quantities and he is being let in "on the ground floor." The victims are almost always inexperienced in investment matters and persons who can ill afford the inevitable loss of their savings.

Complaints from the public, Better Business Bureaus and state authorities have been received in large number from all parts of the United States. Securities commissions and other authorities of many states have continued to issue cease and desist orders and injunctions where solicitations have been made in violation of their securities laws. Various newspapers, magazines and radio commentators, both American and Canadian, have performed a valuable service in educating the public to the danger involved in responding to such solicitations. The Post Office Department has continued to give full cooperation to the Commission in attempting to protect the public from these illegal mass mail campaigns. During the fiscal year, the Commission has provided the Post Office Department with evidence which resulted in the issuance of fraud orders against 41 such persons, and fictitious name orders against 4 individuals and firms. While this campaign has been partially successful, the ingenuity of the fraudulent brokers and dealers in Canada and the lack of sufficient personnel in the Post Office Department adequately to screen the mail has detracted from its efficiency.

During the fiscal year, the principal office of this Commission received 4,488 letters from persons who had been solicited to purchase unregistered Canadian securities. Each day the principal office and the ten regional offices receive telephone calls and personal visits from victims of this vicious "racket." Unfortunately, many such victims have parted with their savings prior to contacting the Commission.

Despite the failure of earlier attempts to negotiate a suitable extradition treaty to cover these cases, the Commission, in conjunction with the State Department, continued to press for necessary treaty revisions. After the close of the fiscal year, in October 1951, such a supplementary treaty was signed. If ratification is obtained and the treaty is implemented, as we expect it to be, by cooperative action on the part of local Canadian authorities, we should be in a position to provide adequate and much needed protection to our investors.

SECTION OF SECURITIES VIOLATIONS

In the first year of its existence the Commission established a section of Securities Violations for assistance in the enforcement of the various statutes which it administers and to provide a further means of preventing fraud in the purchase and sale of securities. This section has developed files which provide the basis of maintaining a clearing house of information concerning persons who have been charged with violations of various

Federal and State securities statutes. The specialized information in these files has been kept current through the cooperation of the United States Post Office Department, the Federal Bureau of Investigation, parole and probation officials, State securities commissions, Federal and State prosecuting attorneys, police officers, Better Business Bureaus, and members of the United States Chamber of Commerce. By the end of the 1951 fiscal year these records contained data concerning 54,887 persons against whom Federal or State action had been taken in connection with securities violations.

During the past year alone additional items of information relating to 5,168 persons were added to the records of this section, including information concerning 1,725 persons not previously identified therein.

Extensive use is made of this clearing house of information. During the past year, in connection with the maintenance and preventive application of these records, the Commission received 4,454 "securities violations" letters or reports (apart from those which are classified as "complaint enforcement") and dispatched 2,654 communications in turn to cooperating agencies.

ACTIVITIES OF THE COMMISSION IN ACCOUNTING AND AUDITING

The detailed provisions of the several Acts administered by the Commission contain wide recognition of the fact that much of the data necessary to investment or other financial decisions consists of financial statements and related material and that, accordingly, accountants and accounting perform a vital role in achieving the statutory objectives of full and fair disclosure, the prevention of fraud or inequitable and unfair practices, and control and regulation. Thus, for example, the Securities Act provides not only for inclusion in the registration statement and prospectus of data as to financial structure and other similar material but also provides for the furnishing of balance sheets and profit and loss statements. Similar provisions as to registration statements and periodic reports are contained in the Securities Exchange Act, the Holding Company Act, and the Investment Company Act. In order to ensure that in the furnishing of such financial information the statutory objectives as to investors and public protection are met, the Acts vest the Commission with broad authority in matters of accounting and financial statement presentation. The Securities Act, for example, authorizes the Commission to define accounting terms, to prescribe, among other matters, "the form or forms in which required information shall be set forth, the items or details to be shown in the balance sheet and earning statement, and the methods to be followed in the preparation of accounts . . ." Substantially equivalent authority is contained in the Securities Exchange-Act, and more comprehensive powers are embodied in the Holding Company Act and the Investment Company Act.

The Securities Act provides that the required financial statements shall be certified by "an independent public or certified accountant." The other three statutes above mentioned

provide that the Commission may require, and its rules do require, that such statements be accompanied by a certificate of independent public accountants. The value of certification has for many years been conceded but the requirement as to independence, long recognized by some individual accountants, was for the first time authoritatively and explicitly stated by its introduction into the statutes. Out of this initial provision in the Securities Act and the resulting rules established by the Commission there have grown concepts that have materially strengthened the protection afforded investors by eliminating certain unhealthy accountant-client relationships which theretofore were quite common.

Although the statutes administered by the Commission give it wide rule-making power, accounting, based as it is largely upon convention and existing financial and business concepts, is of such a nature that the Commission has not yet found it necessary or desirable in most areas to establish extensive accounting rules and regulations dealing with accounting problems. The Commission has prescribed uniform systems of accounts for certain public utility holding companies and for public utility mutual and subsidiary service companies. It has adopted rules under the Securities Exchange Act governing accounting and auditing of exchange members, brokers, and dealers. In the wider area dealing with industrial, commercial, and investment companies under the Securities Act, Securities Exchange Act, and Investment Company Act the form and content of most financial statements are governed by the Commission's Regulation S-X.

The rules and regulations thus established do not prescribe the accounting to be followed except in certain basic respects. In the large area not covered by such rules the Commission's principal reliance for the protection of investors is on the determination and application of accounting standards which are recognized as sound and which have come to have general acceptance. This policy of the Commission is expressed in Accounting Series release No. 4 (1938) (one of the series of such releases, of which there are now seventy-two, inaugurated in 1937 for the purpose of contributing to the development of uniform standards and practice in major accounting questions).

One of the inevitable results of this policy has been constant contact and cooperation between the Commission and accountants, both individually and through such groups as the American Institute of Accountants, the American Accounting Association, the Controllers Institute of America, the National Association of Railroad and Utilities Commissioners and others, and other regulatory agencies. The importance of, and necessity for, this cooperation is emphasized by the great influence and responsibility inherent in the Commission's authority over the several thousand financial statements filed every year with it by most of the important commercial and industrial companies in the United States.

The accounting staff of the Commission is organized to handle the many day-to-day accounting problems that arise in the course of its work and to provide central responsibility for aiding the Commission in matters of accounting policy. The chief

accountant has general supervision with respect to accounting and auditing policy and its application. He is assisted directly by a staff of trained accountants, and, in addition, by assistant chief accountants assigned to and responsible for the examination of financial data and other operating work in the Division of Corporation Finance, Division of Public Utilities, and Division of Trading and Exchanges.

Examination of Financial Statements

The majority of the accounting problems with which the Commission is concerned arise from examination of financial statements or other data required to be filed with the Commission. In general, deficiencies revealed by examination are called to the attention of the registrant by letter. These letters of comment and the correspondence! or conferences that follow have proved to be a most convenient aid in effecting corrections and improvements in financial reporting. Few matters involve prolonged discussion or dispute in spite of the tremendous volume of financial data reviewed each year by the Commission; and it is only in rare instances that formal procedures are necessary in order to procure disclosure.

Many problems arise as a result of inquiry by representatives of registrants, their accountants or counsel in advance of the actual filing of the material involved. Advance discussion of this kind is encouraged and experienced practitioners regularly follow this procedure in dealing with unique problems, thus saving valuable time for themselves and their clients. As a natural outgrowth of the fact that the Commission is the repository of a vast amount of financial data, the staff is frequently called on to aid in the preparation of studies of current problems such as those involved in formulating the background of legislative proposals.

Amendment of Regulation S-X

During the year a general revision of Regulation S-X, the Commission's principal accounting and auditing regulation relating to the form and content of financial statements filed with it, was accomplished. This regulation was originally adopted in February 1940 after extensive reconsideration of the predecessor requirements theretofore contained in the respective registration and annual report forms.

In the Commission's annual reports for the last two years reference has been made to the relatively infrequent (but important) new provisions added to the regulation since adoption and to the apparent need for a complete reappraisal of the regulation that would include within its scope reconsideration of all rules. These reports reviewed the efforts made, from the preliminary proposal sent out in September 1949 to the formally announced proposal on July 12, 1950, to obtain a wide expression of views not only as to staff suggestions but as to possible amendments to the regulation not sponsored by the staff.

Following the formal announcement of proposed amendments under the Administrative Procedure Act, as to which more than 3,000 persons received copies, again approximately 175 persons commented upon the proposals. The suggestions were carefully considered and in a number of instances formed the basis of changes incorporated in the final amendments. In addition, a special committee of the American Institute of Accountants, at its request, was informally heard by the Commission in support of its views on certain points it believed should be reflected in the revision. The final amendments were promulgated December 20, 1950, in Accounting Series release No. 70.

Among the amendments to Regulation S-X that are of major importance to registrants filing financial statements with the Commission and also to professional accountants whose reports must accompany such statements is a new provision contained in rule 1-01 (a) that in effect makes the previously referred to Accounting Series releases a part of the regulation. Many of such releases contain highly significant statements the applicability of which, under the amended rule, is not now likely to escape the attention of interested persons, and which, it should be clear, continue to reflect considered Commission policy. This is particularly important with respect to release No. 4, to which reference has been made above, because of its controlling provisions in areas where the largest volume of accounting problems fall.

The definitions of terms used in the regulation have now been made complete by bringing into rule 1-02 a substantial group of terms for which previously a reference to other regulations was necessary.

In Article 2 which deals with the certification of financial statements the provisions contained in rules 2-01 (b) and 2-01 (c) relating to the certifying accountant's independence as to a person were extended to any affiliate of the person, and the previous specification, in rule 2-01 (b), as to the interest in such person (or affiliate) that will result in the accountant being considered not independent was changed from "any substantial interest" to "any financial interest," thus conforming the rule to established Commission policy and to the prevailing practice in professional circles.

An important change was effected in rule 3-11 of the regulation. Before amendment the rule exempted public utility companies from the requirement, and otherwise universal practice, of deducting, on the balance sheet, depreciation, depletion, amortization or retirement reserves from the specific assets to which they apply. The amendment, adopted after full consideration of the conflicting views of interested parties, removes the exemption. Opposition to this change was confined to representatives of the public utility industry who were concerned about the possible effect in certain jurisdictions upon utility rate-making of showing utility plant accounts net of related reserves. The elimination of the exemption was predicated upon the belief that there was no necessary relationship between balance sheets prepared for investors or the public generally and the processes of regulating rates for utility services.

Previous Commission policy as to disclosure of certain commitments is now codified in rule 3-18 of the regulation. In addition to the provision in paragraph (a) for a statement of material firm commitments involving permanent investments and fixed assets there is required by paragraph (b) appropriate disclosure of annual rentals and other pertinent facts in cases where rentals or obligations under long-term leases are material. The development of policy in this respect was referred to in the annual reports of the last two years.

The rapid expansion of the number of corporate pension and retirement plans that began during World War II and continued to the present time focused considerable attention upon the proper accounting for the much enlarged liabilities and payments associated with the plans. The Commission's views were first discussed in the thirteenth annual report after extensive experience with the many pension plan problems that arose. Later, after additional experience and reconsideration of views, due in part to special problems introduced by the pension-plan results of union-company negotiations in several industries, notably the steel producing industry, the Commission's policy was again indicated in the sixteenth annual report. With this background, and after the benefit of discussion among leaders in finance and of comment prompted by announced proposals, there was included in rule 3-19 (e) the requirement that balance sheets should be accompanied by (1) a brief description of the essential provisions of any such plan; (2) an indication of the estimated annual cost of the plan; and (3) if the plan is not funded or otherwise provided for, a disclosure of the estimated amount that would be necessary to accomplish this.

One of the principal responsibilities of the Commission is to obtain for the investing public financial statements that are the most informative and which are the least likely to mislead, especially, those who are not experienced in the significance of such statements. In previous annual reports reference was made to a problem which has long been under consideration and which has been the subject of repeated exchanges of views between the Commission's staff and representatives of the American Institute of Accountants and other interested parties, namely, the concept of income and the proper form of income or profit-and-loss statement.

The main point of difference has been the propriety of excluding from the determination of Net Income, and the inclusion thereof in Earned Surplus, major items which are extraordinary in nature or which had their origin in prior years. A workable solution to this problem was commented upon as follows in Accounting Series release No. 70, issued on December 20, 1950, which announced the revision of Regulation S-X:

The principal new requirement pertains to Profit and Loss or Income Statements and is contained in Rule 5-03 (a) which states:

"All items of profit and loss given recognition in the accounts during the period covered by the profit and loss or income statements shall be included."

The inclusion of this requirement, which states a long established policy of the Commission, is deemed necessary because of the not always consistent practice followed by some registrants of excluding certain items from the profit and loss or income statements with the result that the amount shown thereon as net income or loss has been susceptible to misinterpretation by investors. Recognizing that there might be exceptional circumstances which would make it appropriate to deviate from this rule, but keeping in mind the Commission's responsibility for prohibiting the dissemination of financial statements which might be misleading to investors, Rule 5-03 was amended to read:

"Except as otherwise permitted by the Commission, the profit and loss or income statements filed for persons to whom this article is applicable shall comply with the provisions of this rule." [Underscored phrase added in revision.]

The purpose of this revision is to make clear to registrants that they are not forestalled from giving exceptional treatment to exceptional items when both the representatives of the registrant and the Commission are convinced that such treatment is appropriate.

Notwithstanding this provision, representatives of the Executive Committee of the American Institute of Accountants appeared before the Commission and proposed that either Rule 5-03 (a) be eliminated from the regulation or the requirements with respect to the presentation of the final section of profit and loss or income statements be amended to permit, where appropriate, the exclusion of extraordinary items from those making up the caption net income or loss.

To accomplish this, additional items, described in Rules 5-03 (17) and 5-03 (18), were added to those previously set forth in the regulation, and the last three items of the section pertaining to profit and loss or income statements (Rule 5-03) now appear as follows :

"16. Net income or loss.

"17. Special items. -- State separately and describe each item of profit and loss given recognition in the accounts, included herein pursuant to Rule 5-03 (a), and not included in the determination of net income or loss (Item 16).

"18. Net income or loss and special items."

Captions 17 and 18 are to be used in those instances where it is believed that the showing of a single unqualified figure of net income or loss might be misconstrued.

DIVISION OF OPINION WRITING

The Division of Opinion Writing aids the Commission in the preparation of findings, opinions, and orders promulgated by the Commission in contested and other cases arising under the Securities Act of 1933, the Securities Exchange Act of 1934, the Holding Company Act of 1935, the Trust Indenture Act of 1939, the Investment Company Act of 1940, and the Investment Advisers Act of 1940. These statutes provide for a. wide variety of administrative proceedings which require quasi-judicial determination by the Commission. Formal opinions are issued in all cases where the nature of the matter to be decided, whether substantive or procedural, is of sufficient importance to warrant a formal expression of views.

The Division of Opinion Writing is an independent staff office which is directly responsible to the Commission. It receives all assignments and instructions from and makes recommendations and submits its work to the Commission directly. It is headed by a director, who is assisted by an assistant director, supervising attorneys, and a staff of drafting attorneys and a financial analyst.

While engaged in the preparation of opinions assigned to the Division of Opinion Writing, the members of this division are completely isolated from members of the operating division actively participating in the proceedings and it is an invariable rule that those assigned to prepare such an opinion must not have had any prior participation in any phase of the proceedings with respect to which the opinion is to be prepared. Commission experts are from time to time consulted on technical problems arising in the course of the preparation of opinions and findings, but these experts are never individuals who have participated in the preparation of the case or testified at the hearing.

The director or assistant director of the Division of Opinion Writing, together with the members of the staff of the division who are assigned to work on a particular case, attend the oral argument of the cases before the Commission and frequently keep abreast of current hearings. Prior to the oral argument, the division makes a preliminary review of the record and prepares and submits to the Commission a summary of the facts and issues raised in the hearings before the hearing officer, as well as in any proposed findings and supporting briefs, the hearing officer's recommended decision, and exceptions thereto taken by the parties. Following oral argument or, if no oral argument has been held, then at such time as the case is ready for decision, the Division of Opinion Writing is instructed by the Commission respecting the nature and content of the opinion and order to be prepared.

In preparing the draft of the Commission's formal opinion, the entire record in the proceedings is carefully read by at least one member of the staff of the Division of Opinion Writing and in some cases a narrative abstract of the record is prepared. Upon completion of a draft opinion and abstract of the record, and after review and revision of the opinion within the Division of Opinion Writing, they are submitted to the

Commission. If the study of the record in the case by the Division of Opinion Writing has revealed evidence of violations warranting a reference to the Attorney General for criminal prosecution, or has disclosed the desirability or the need for any changes in administrative procedures or techniques, appropriate recommendations are made to the Commission at the time the draft opinion in the case is submitted.

The draft opinion as submitted may be modified, amended, or completely rewritten in accordance with the Commission's final instructions. When the opinion accurately expresses the views and conclusions of the Commission, it is adopted and promulgated as the official decision of the Commission. In some cases concurring or dissenting opinions are issued by individual Commissioners who wish to express their separate views on matters covered by the opinion adopted by the majority of the Commission. In such cases the Division of Opinion Writing is occasionally instructed to prepare drafts of such concurring or dissenting opinions and confers respecting them with the individual Commissioners involved, submits drafts directly to them, and makes such modifications and revisions as are directed.

The findings of fact, opinions, and orders adopted and promulgated by the Commission serve as an aid and guide to the bench and bar. With minor exceptions (e. g., certain opinions dealing with requests for confidential treatment) all are publicly released and distributed to representatives of the press and persons on the Commission's mailing list. In addition, the findings and opinions are printed and published by the Government Printing Office in bound volumes under the title "Securities and Exchange Commission Decisions and Reports."

The creation of the Division of Opinion Writing as an independent staff unit in 1942 was based on the view that the fair exercise of the Commission's adjudicatory functions in many types of cases made it appropriate that it be assisted in that function by members of its staff who were independent of units engaged in investigation or prosecution of cases. Originally initiated as a matter of Commission policy, the desirability of this arrangement was subsequently given express recognition in specific provisions of the Administrative Procedure Act, which in certain types of cases requires that there be a complete separation of function between quasi-prosecutory functions and quasi-judicial functions. The existence of the Division of Opinion Writing thus made it possible for the Commission, even before the passage of the Administrative Procedure Act, to meet fully the separation of function requirements contained in sections 5 (c), 7, and 8 of that Act.

The Commission, through its revised rules of practice, has sought to provide a flexible procedure which will be suited to the needs and desires of the participants in the proceeding before it, as well as guarantee to them the procedural safeguards required by the general principles of due process and the provisions of the Administrative Procedure Act. Thus, at the request of some participants, the Commission has in many cases availed itself of the assistance of the Division of Opinion Writing in the preparation of its findings even though separation of functions was not required by law.

In addition to its primary function, the Division of Opinion Writing is also given assignments of a general nature which are not inconsistent with the objective of the separation of the investigatory and quasi-judicial functions. Thus, the division has been assigned continuing joint responsibility with the office of the General Counsel in dealing with problems arising under the Administrative Procedure Act. It has also been given the responsibility of preparing a compilation of administrative decisions and other authorities under the various statutes administered by the Commission.

The Division of Opinion Writing assists the operating divisions of the Commission in the preparation of opinions in certain uncontested cases where participation by the operating division in the decisional process is proper under the Administrative Procedure Act. In some instances members of the Division of Opinion Writing are assigned to assist the Office of the General Counsel in connection with court appeals taken from Commission decisions initially drafted in the division.

Some of the more significant opinions issued by the Commission during the year are commented upon in this report under the discussions of the various statutes.

FOREIGN FINANCIAL AND ECONOMIC MATTERS -- THE INTERNATIONAL BANK

During the fiscal year 1951 registration statements covering $730,760,812 of securities issued by foreign issuers, governmental and private, were filed under the Securities Act of 1933. The largest of these issues was that of the State of Israel amounting to $500,000,000. Issues of the Government of Canada and Canadian provinces and municipalities aggregated $180,468,000. Canadian private issues accounted for most of the balance.

Following extended negotiations with the Ministry of Finance of the Japanese Government, through the Supreme Commander for the Allied Powers, the Japanese Government in November 1950 filed with the Commission a report under the Securities Exchange Act of 1934 relating to the status of the outstanding bonds. Upon the filing of this report the Commission withdrew its request that brokers and dealers refrain from effecting transactions in Japanese bonds, and dealings in these bonds were resumed on the New York Stock and New York Curb Exchanges.

Upon the announcement of the West German Government in March 1951 of its recognition of prewar external debts, the Commission consulted with the Department of State as to the eventual resumption of trading in bonds of German issues. In view of events which have taken place in Germany since these bonds were suspended from dealings and the lack of current information on the status of the bonds, the Department of State and the Commission concluded that it would not be in the interest of United States

foreign policy or of public investors to approve the resumption of trading in German bonds at this time. The Commission in a public statement of March 6, 1951 advised that "it does not intend to withdraw its request that brokers and dealers refrain from effecting transactions in German securities until assurances can be given to investors through validation procedures now under consideration that only bonds which will constitute 'good delivery' will be afforded a market in the United States and appropriate reports are filed under the Securities Exchange Act of 1934."

The Commission has participated in discussions which have been held by the Department of State with representatives of the holders of German dollar bonds and of the trustees and paying agents for these bonds on drafts of German legislation for the validation of all outstanding bonds of German public and private issuers denominated in foreign (non-mark) currencies. The Commission has also participated in the drawing up of an Executive Agreement between the United States and the Republic of Germany to implement this legislation as to dollar bonds. These drafts are having the consideration of the German authorities.

Through its representation on the Interdepartmental Committee on German Debts, the Commission has contributed to the establishing of principles and procedures for bringing about a settlement of the public and private prewar debts of Germany. The Commission is represented on this Committee and at conferences on the German debt problem by its Foreign Economic Adviser.

The Commission has also continued its representation on the Staff Committee of the National Advisory Council on International Monetary and Financial Problems and has continued to cooperate with other agencies concerned with the development and administration of the Government's foreign economic program. During the year its Foreign Economic Adviser has had frequent discussions with representatives of foreign governments who were seeking information upon the regulations, procedures and practices of the United States capital markets applicable to the raising of private capital by foreign companies through the issuance of securities.

By amendment to the Bretton Woods Agreements Act securities issued or guaranteed as to principal and interest by the International Bank for Reconstruction and Development are deemed to be exempted securities under the Securities Act of 1933 and the Securities Exchange Act of 1934. The Commission in consultation with the National Advisory Council on International Monetary and Financial Problems is authorized to suspend the provisions of this amendment at any time. The amendment requires the Commission to include in its annual reports to Congress such information as it shall deem advisable with regard to the operation and effect of the amendment, and in connection therewith to include any views submitted for such purpose by any association of dealers registered with the Commission. The Commission has received no views from such association of dealers.

In February 1951 the International Bank offered in the United States a new issue of $50 million 3 percent bonds due in 1976. In the distribution of these bonds the Bank did not, as in its previous bond issue, employ the method of competitive bidding but it formed a "sponsoring group" of commercial banks and investment firms whose function was to advise the Bank on its financing, arrange for sales to large institutional investors and for subscriptions by the "selling group" which consisted of 421 brokers and dealers. Of the $50 million of bonds offered, it is estimated that 98 percent was purchased by institutional investors such as insurance companies, pension and trust funds, savings and commercial banks. In this distribution the Bank made available to members of the sponsoring and selling groups a prospectus relating to the new bonds giving information about the Bank's structure and operations. It also filed with the Commission pursuant to regulation BW adopted by the Commission under the amendment to the Bretton Woods Agreements Act information comparable to that which would be required .if its securities had been registered under the Securities Act of 1933 and the Securities Exchange Act of 1934.

ADVISORY AND INTERPRETATIVE ASSISTANCE

The importance of the advisory and interpretative service maintained by the Commission is emphasized by the continued volume of inquiries received from attorneys, accountants, persons engaged in the securities business and members of the general public. Bequests relate to the applicability of the provisions of the various Acts administered by the Commission and the regulations thereunder to every phase of corporate financing.

While this informal advice primarily is intended to assist the public it is equally valuable to the Commission. Many problems which appear complicated to those persons unfamiliar with securities legislation can readily be solved by the staff attorneys who are expert in these matters. Those seeking help, however, are not confined to the uninformed and many novel situations arise which give concern to the veteran corporate lawyer. Often, by reason of this timely advice, violations of certain provisions of the Acts or the pursuit of improper procedure which otherwise might unwittingly result are avoided -- thus saving the Commission as well as the public much time and expense.

The Commission's readiness to render all possible assistance has encouraged the solicitation of preliminary advice to such an extent that it is not possible to determine to any degree of accuracy the number of possible violations that may have been avoided. However, during the 1951 fiscal year several thousand letters of an advisory nature were written by the Commission's central office. Many more questions were answered in personal or telephone conferences between members of the staff and the public. In addition, the Commission's ten regional offices answer thousands of inquiries during the year.

Uniformity of interpretations is maintained through a procedure whereby each regional office is advised concerning inquiries received in the central office originating from persons located in the region served by that office and whereby the central office reviews interpretations given by the regional offices. Also, all regional offices are advised by the central office concerning any unprecedented interpretation made at headquarters which has any general applicability or which relates to any unique situation.

CONFIDENTIAL TREATMENT OF APPLICATIONS, REPORTS, OR DOCUMENTS

The Commission is empowered to grant confidential treatment, upon application by registrants, to information contained in reports, applications, or documents which they are required to file under the Securities Act of 1933, the Securities Exchange Act of 1934, the Public Utility Holding Company Act of 1935, the Investment Company Act of 1940, and the Investment Advisers Act of 1940. Under the Securities Act of 1933 the Commission has adopted rule 485, which provides that information as to material contracts, or portions thereof, will be held confidential by the Commission if it determines that disclosure would impair the value of the contracts and is not necessary for the protection of investors. The other four statutes, in general, empower the Commission to hold confidential under certain conditions any information contained in any reports required to be filed under those statutes. Disclosure of information confidentially filed under the latter statutes is made only when the Commission determines that disclosure is in the public interest. As described elsewhere in this report, the Commission has adopted rules reintroducing the procedures followed under the former rules 171, X-6, and U-105, which were in effect during World War II, to permit the omission or confidential treatment of certain information as called for in all filings under the first three named statutes where its disclosure, would be detrimental to the national security.

Substantially over a hundred applications for confidential treatment were received and acted upon by the Commission during the 1951 fiscal year as indicated below.

(chart omitted)

STATISTICS AND SPECIAL STUDIES

In general, the statistical activities of the Commission relate to (a) operational data derived from official filings with the Commission and (b) data of general application on groups of companies subject and not subject to the legislation administered by the Commission.

Operational Statistics

In order to meet the Commission's responsibilities to the public, it is essential to organize and present in meaningful and convenient form, out of the masses of information filed with the Commission, pertinent data on registered issues and issuers. Much of these data are not available elsewhere, nor in such complete form. Filed under strict requirements, they are notable for accuracy. Extending over the years, they present an ever widening base for comparisons and aggregates. Data made available by the Commission are availed of in many forms by the investing public, by the registrants themselves, by investment advisers, accountants, trade organizations, and by numerous government agencies, national and state. Numerous reports have been compiled and tabulated contributing materially to the satisfaction of the needs of the Congress' and defense agencies during the present national emergency.

Survey of American Listed Corporations

Corporate data have been published annually by the Commission for the years 1934r-1947, under the title "Survey of American Listed Corporations" covering well over half of all national manufacturing based on asset size. More recent figures are in many cases available or in course of preparation.

Registration Statistics

Data are published quarterly in the Statistical Bulletin and yearly in the Annual Report of the Commission, covering registration of all securities under the Securities Act of 1933. The data, taken from the filings made by registrants with the Commission, include purpose of registration, method of offering, compensation to distributors, total expenses, intended use of proceeds, type of security, and industry classification.

Underwriting Statistics

Underwriting statistics cover participations of investment bankers in effectively registered issues, a showing of the leading underwriters, and of firms managing the groups. The data carry on a series commenced in 1938, and are reported quarterly in the Statistical Bulletin.

Cost of Flotation

Data on the cost of flotation of issues effectively registered with the Commission under the Securities Act of 1933 have been published for the years 1945-1949, inclusive, under the title "Cost of Flotation," dated in February 1951. Quarterly compilations under the same title have been made and published separately commencing with the first quarter of 1950. While these studies are prepared primarily for the operational uses of the Commission's staff, they are also available to issuers and distributors of securities and other interested persons.

Investment Companies

Investment company data are published quarterly in the Statistical Bulletin, on about 200 registrants, segregated by open and closed-end types. The coverage includes purchases and sales of their own securities, portfolio changes, and aggregates of securities and assets.

Saving Study

The Commission continued its series of quarterly releases on the volume and composition of individuals' saving in the United States. These releases show the aggregate volume of individuals' saving as well as the components contributing to the total, such as changes in securities, cash, insurance and consumers' indebtedness, etc. These data have been extremely useful in the determination of fiscal policy and as a measurement of the inflationary potential.

Financial Position of Corporations

The Commission together with the Department of Commerce continued the joint series of quarterly releases on the plant and equipment expenditures of United States business other than agricultural. Shortly after the close of each quarter these releases present industry totals on the actual capital expenditures of that quarter and anticipated expenditures for the next two quarters. In addition a survey is made at the beginning of each year of the plans of business as regards expansion during that year. These data have provided a useful index of present and future activity in the capital markets and of business in general. In view of the volatile nature of capital expenditures and their relation to the level of production and employment, the series has been of considerable importance for business management and in the formation of government policy.

The series of quarterly releases on the working capital position of all United States corporations exclusive of banks and insurance companies was also continued. These releases show the principal components of current assets and current liabilities and an abbreviated analysis of the sources and uses of corporate funds. These data are important in measuring the liquid position of the corporate segment of the economy taken as a whole.

The Commission together with the Federal Trade Commission continued the joint series of quarterly industrial financial reports. These reports developed as an extension of the working capital series and present a complete balance sheet and an abbreviated income account for manufacturing corporations as a whole. In addition the data are shown for various size groups of corporations and for minor industry groups. The financial report program includes data on manufacturers' profits, which are extremely important in the formulation of a tax program and renegotiation policy. The data are basic to any appraisal

of corporate financial position and any analysis of corporation finance and the capital markets.

During the past fiscal year the report on manufacturing was adapted to the needs of the Office of Price Stabilization in connection with the determination of price policy. The program was also expanded at their request to cover wholesale and retail trade.

Capital Markets

The Commission has also continued its monthly series on new securities offerings published in the Statistical Bulletin, and a quarterly series published together with a brief analysis in release form. These data show the volume and character of all securities offerings in the United States, both registered and unregistered, public offerings and private placements. Collateral studies based on these data have been undertaken from time to time pursuant to the Commission's needs and requests from other branches of the government, and the public. 'These included a study of the cost of flotation of privately placed securities and a survey of issues offered under Regulation A.

PERSONNEL

As of June 30, 1951, the personnel of the Commission consisted of the following:

Commissioners: 4 (1 vacancy)

Staff:
Headquarters office: 690
Regional offices: 333

Total: 1,027

During the fiscal year, the Commission lost a considerable number of its experienced employees whose specialized skills were in great demand by newly created or rapidly expanding defense agencies. Some 80 employees transferred to other agencies, and 10 employees entered on full time active duty in the military service. In addition, about 20 employees were granted leave for tours of military training duty.

The loss of these employees, representing almost 10 percent of the entire staff, created serious problems for the Commission in carrying out its important role in the Nation's economy. However, inasmuch as the needs of the defense agencies for the services of these employees were even more urgent, no objections to their release were interposed by the Commission.

Two major revisions in the Commission's personnel management program were effected during the year. A Performance Rating Plan, designed to strengthen work performance and employee morale, was developed pursuant to the Performance Rating Act of 1950 and put into operation. To facilitate the identification and recognition of employees having a potential for development, and to further insure that its capable employees would have a real opportunity for career service, the Commission revised and formally restated its promotion policy, incorporating in it certain standards prescribed by the Civil Service Commission.

Staff assistance on all personnel matters is provided by the Commission's Division of Personnel. The regular work of this Division embraces employment, placement and separation; job evaluation and classification; employee relations and services; training; operation of various committees and boards such as the Committee of Expert Examiners (which conducts examinations for positions peculiar to the Securities and Exchange Commission); wage administration; the performance rating program; administration of Commission regulations governing the personal securities and commodities transactions of its personnel; and processing, recording and reporting of all personnel matters. A staff of eight employees is assigned to this work, representing a ratio of one personnel employee to each 130 Commission employees.

In addition, the Division of Personnel is responsible for the conduct of pre-appointment character investigations, leave administration and accounting, retirement counseling, and the maintenance of an emergency medical unit. Four additional employees, including a registered nurse, are assigned to the Division of Personnel to carry out these functions.

FISCAL AFFAIRS

Appropriation and Expenditures

The following is a summary of the appropriation and expenditures for the fiscal year 1951.

Appropriation: $6,230,000

Expenditures: $6,031, 820

Unexpended balance: $198,180

Fees and Revenue

The Commission receives fees (a) for the registration of securities under the Securities Act of 1933 (1/100th of 1 percent of the maximum price at which the securities are proposed to be offered); (b) from registered national securities exchanges representing

1/500th of 1 percent of the aggregate dollar volume of the sales of securities on such exchanges; (c) for applications for the qualifications of indentures under the Trust Indenture Act of 1939 ($100 for each application); (d) for the sale of photocopies of documents or portions thereof filed by corporations under one or more of the Acts the Commission administers; and (e) various receipts, such as the proceeds of the sale of excess or surplus Government property, the sale of waste paper, etc.

The following is the amount of the fees received in fiscal 1951:

Character of fees:

Registration of securities issued: $612,505

Qualification of trust indentures: $700

From registered exchanges: $456,800

Sale of copies of documents or portions thereof: $13,275

Miscellaneous receipts: $3,742

Total: $1,087,022

Fees and other receipts must be turned in to the General Fund of the Treasury and are not available for expenditure by the Commission.

PUBLICATIONS

Public Releases

Releases of the Commission consist primarily of official announcements of filings under and actions taken pursuant to the several Acts which it administers. These include notices of filings, hearings, orders, decisions, regulations, and related Commission matters. The Commission is continuing to improve its service and to effect economies in connection with its mailing lists through the continuation of procedures which avoid the full-scale distribution of the complete releases except to those persons who are sufficiently interested to make a special request therefor.

The announcements issued during the past fiscal year included 37 releases under the Securities Act of 1933; 159 under the Securities Exchange Act of 1934; 691 under the Public Utility Holding Company Act of 1935; 142 under the Investment Company Act of 1940; and 3 under the Investment Advisers Act of 1940. In addition, 2 releases were issued concerning the Commission's activities in corporate reorganization under Chapter

X of the Bankruptcy Act, and 5 releases were issued under the Trust Indenture Act of 1939.

The following breakdown of the releases for the month of June, 1951 is fairly illustrative of the general nature of the releases issued throughout the year:

Announcements of filings, orders for hearing, and notices giving opportunity to request hearing: 27

Interim and final decisions and orders: 61

The balance of the Commission's releases are of an informational nature, the following having been issued during the year: 74 announcements of publication of reports on corporate survey and statistical studies; 66 reports of court actions in injunction and criminal prosecution cases initiated by the Commission; and 8 miscellaneous announcements regarding appointments of Commissioners, staff officials, and related matters.

Other publications issued during the 1951 fiscal year:

Daily Registration Record.

Monthly Statistical Bulletin.

Bound Volumes 17 and 18 of the Decisions and Reports (October 1, 1944 to December 31, 1944, and January 1, 1945 to April 26, 1945).

Twelve monthly issues of the Official Summary of Securities Transactions and Holdings of Officers, Directors, and Principal Stockholders.

The Sixteenth Annual Report of the Commission.

List of Securities Traded on Exchanges under the Securities Exchange Act of 1934, as of December 31, 1950.

List of Companies Registered under the Investment Company Act of 1940, as of December 31, 1950.

Working Capital of 1,275 Registered Corporations, quarterly.

Registered Public Utility Holding Companies, June 30, 1950.

Securities Registered under the Securities Act of 1933, Cost of Flotation. Second, third, and fourth quarters, 1950, and first quarter, 1951.

Cost of Flotation, 1945-1949.

Quarterly Industrial Financial Report Series. Second, third, and fourth 1950, and first, 1951.

The Work of the Securities and Exchange Commission, January 1, 1951.

INFORMATION AVAILABLE FOR PUBLIC INSPECTION

The Commission maintains public reference rooms at the central office in Washington, D. C., and in its regional offices in New York City and Chicago, Illinois.

Copies of all public information on file with the Commission contained in registration statements, applications, reports, declarations, and other public documents are available for inspection in the public reference room in Washington. In addition to providing facilities for personal inspection of registered public information, there were received in the public reference room thousands of letters and telephone calls from persons requesting registered public information and copies of forms, releases, and other material of a public nature. There were 2,633 persons who visited this public reference room seeking such information during the fiscal year 1951. Through the facilities provided for the sale of photocopies of public registered information, 1,610 orders involving a total of 99,586 pages were filled. In addition to the sale of photocopies, the Commission mailed 291,779 pieces of mail containing releases, forms, Acts, etc., to persons requesting them.

In its New York Regional Office, located at 120 Broadway, facilities are provided for the inspection of certain public information on file with the Commission. This includes copies of (1) applications for registration of securities on all national securities exchanges except the New York Stock Exchange and the New York Curb Exchange, together with copies of annual reports, supplemental reports and amendments thereto and (2) annual reports filed pursuant to the provisions of section 15 (d) of the Securities Exchange Act of 1934 by issuers having securities registered under the Securities Act of 1933, as amended. During the fiscal year 1951, 12,166 persons visited the New York public reference room and more than 6,500 telephone calls were received from persons seeking registered public information, copies of forms, releases, and other material.

In the Chicago Regional Office, located at 105 West Adams Street, copies of applications for registration of securities on the New York Stock Exchange and the New York Curb Exchange, together with copies of all annual reports, supplemental reports and amendments thereto, are available for public inspection. During the fiscal year 1951, 2,679 members of the public visited this public reference room, and approximately 1,734 telephone calls were received from persons seeking registered public information, forms, releases, and other material of a public nature.

In addition to the material which is available in the New York and Chicago public reference rooms, there are available in each of the Commission's regional offices copies of all prospectuses used in public offerings of securities effectively registered under the Securities Act of 1933. Duplicate copies of applications for registration of brokers or dealers transacting business on over-the-counter markets, together with supplemental statements thereto, filed under the Securities Exchange Act of 1934 and duplicate copies of applications for registration of investment advisers and supplemental statements thereto, filed under the Investment Advisers Act of 1940, are available for inspection in the regional office having jurisdiction over the zone in which the registrant's principal office is located. Also, inasmuch as letters of notification under Regulation A exempting small issues of securities from registration requirements of the Securities Act of 1933, as amended, may be filed with the regional office of the Commission for the region in which the issuer's principal place of business is located, copies of such material are available for inspection at the particular regional office where filed.

Copies of all applications for registration of securities on national securities exchanges and annual reports, supplemental reports and amendments are available for public inspection at the respective exchanges upon which the securities are registered.

PUBLIC HEARINGS

The following public hearings were held by the Commission under the Acts indicated during the fiscal year 1951:

Securities Exchange Act of 1934: 10

Public Utility Holding Company Act of 1935: 58

Trust Indenture Act of 1939: 1

Investment Company Act of 1940: 3

Total hearings during year: 72