MISSOURI SECURITIES LAW EXEMPTIONS
CORPORATIONS
EXEMPTIONS UNDER MISSOURI SECURITIES LAW
PUBLIC UTILITY HOLDING COMPANIES

) Such companies and their
) subsidiaries registered under
) the Public Utility Holding
) Company Act of 1935 exempt
under the provisions of the
Missouri Securities Law.

June 27, 1949

FILED
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Mr. W. Randall Smart
Commissioner of Securities
Office of the Secretary of State
Capitol Building
Jefferson City, Missouri

Dear Sir:

Reference is herewith made to your letter of April 26th, 1949, which reads as follows:

> "Section 8260 (d) R. S. Mo. 1939 exempts certain securities from the provisions of the Missouri Securities Law. In describing exempt securities, it reads in part as follows:
>
> > 'Any security issued or guaranteed, by a corporation owning or operating a railroad or any other public service utility: Provided, that such corporation is subject to regulation or supervision either as to its rates and charges or as to the issue of its own securities by a public commission, board or offices of the government of the United States...'
>
> "The question has arisen as to whether or not public utility corporation's securities are exempt from registration in Missouri for the reason that the company comes under the 'Public Utility Holding Company Act of 1935.' A copy of this act is attached.
>
> "We respectfully request your opinion in this matter."

In answer to our inquiry as to the nature of the specific public utility company which you had in mind when you made your request, we were in receipt of your letter of May 11th, 1949,

reading as follows:

"RE: TEXAS ELECTRIC SERVICE COMPANY

"Dear Mr. Crowe:

"In reply to your letter of May 10th, advise the corporation in question is a subsidiary company doing an intrastate business. You have a copy of the prospectus."

The Public Utility Holding Company Act of 1935 (15 U.S.C.A., Section 79 and sequence) provides for the registration and regulation of gas and electric public utility holding companies and their subsidiaries. In Section 1 of that Act Congress sets out the reasons which it believes necessitates the control of such companies and indicates its intent to remedy the evils growing out therefrom by the regulation provided for in the Act. Section 1 of the Act reads as follows:

"Section 1. (a) Public-utility holding companies and their subsidiary companies are affected with a national public interest in that, among other things, (1) their securities are widely marketed and distributed by means of the mails and instrumentalities of interstate commerce and are sold to a large number of investors in different States; (2) their service, sales, construction, and other contracts and arrangements are often made and performed by means of the mails and instrumentalities of interstate commerce; (3) their subsidiary public-utility companies often sell and transport gas and electric energy by the use of means and instrumentalities of interstate commerce; (4) their practices in respect of and control over subsidiary companies often materially affect the interstate commerce in which those companies engage; (5) their activities extending over many States are not susceptible of effective control by any State and make difficult, if not impossible, effective State regulation of public-utility companies.

"(b) Upon the basis of facts disclosed by the reports of the Federal Trade Commission made pursuant to S. Res. 83 (Seventieth Congress, first session), the reports of the Committee on Interstate and Foreign Commerce, House of Representatives, made pursuant to

H. Res. 59 (Seventy-second Congress, first session) and H. J. Res. 572 (Seventy-second Congress, second session) and otherwise disclosed and ascertained, it is hereby declared that the national public interest, the interest of investors in the securities of holding companies and their subsidiary companies and affiliates, and the interest of consumers of electric energy, and natural and manufactured gas, are or may be adversely affected--

"(1) when such investors cannot obtain the information necessary to appraise the financial position or earning power of the issuers, because of the absence of uniform standard accounts; when such securities are issued without the approval or consent of the States having jurisdiction over subsidiary public-utility companies; when such securities are issued upon the basis of fictitious or unsound asset values having no fair relation to the sums invested in or the earning capacity of the properties and upon the basis of paper profits from intercompany transactions, or in anticipation of excessive revenues from subsidiary public-utility companies; when such securities are issued by a subsidiary public-utility company under circumstances which subject such company to the burden of supporting an overcapitalized structure and tend to prevent voluntary rate reductions;

"(2) when subsidiary public-utility companies are subjected to excessive charges for services, construction work, equipment, and materials, or enter into transactions in which evils result from an absence of arm's-length bargaining or from restraint of free and independent competition; when service, management, construction, and other contracts involve the allocation of charges among subsidiary public utility companies in different States so as to present problems of regulation which cannot be dealt with effectively by the States;

"(3) when control of subsidiary public-utility companies affects the accounting practices and rate, dividend, and other policies of such companies so as

to complicate and obstruct State regulation of such companies, or when control of such companies is exerted through disproportionately small investment;

"(4) when the growth and extension of holding companies bears no relation to economy of management and operation or the integration and coordination of related operating properties; or

"(5) when in any other respect there is lack of economy of management and operation of public-utility companies or lack of efficiency and adequacy of service rendered by such companies, or lack of effective public regulation, or lack of economies in the raising of capital.

"(c) When abuses of the character above enumerated become persistent and wide-spread the holding company becomes an agency which, unless regulated, is injurious to investors, consumers, and the general public; and it is hereby declared to be the policy of this title, in accordance with which policy all the provisions of this title shall be interpreted, to meet the problems and eliminate the evils as enumerated in this section, connected with public-utility holding companies which are engaged in interstate commerce or in activities which directly affect or burden interstate commerce; and for the purpose of effectuating such policy to compel the simplification of public-utility holding-company systems and the elimination therefrom of properties detrimental to the proper functioning of such systems, and to provide as soon as practicable for the elimination of public-utility holding companies except as otherwise expressly provided in this title."

Section 2, (7), (A), defines a holding company in the following manner:

"(7) 'Holding company' means--

"(A) any company which directly or indirectly owns, controls, or holds with power to vote, 10 per

centum or more of the outstanding voting securities of a public-utility company or of a company which is a holding company by virtue of this clause or clause (B), unless the Commission, as hereinafter provided, by order declares such company not to be a holding company; and * * *."

Section 2, (8), (A), defines a subsidiary company as follows:

"(8) 'Subsidiary company' of a specified holding company means--

"(A) any company 10 per centum or more of the outstanding voting securities of which are directly or indirectly owned, controlled, or held with power to vote, by such holding company (or by a company that is a subsidiary company of such holding company by virtue of this clause or clause (B)), unless the Commission, as hereinafter provided, by order declares such company not to be a subsidiary company of such holding company; and * * *."

Section 3 of the Act provides that in certain instances the Securities and Exchange Commission of the United States may exempt holding companies and subsidiaries from the provisions of the Act.

Section 4 of the Act provides that holding companies which are not registered with the Securities and Exchange Commission are prohibited from doing certain things. In effect the sum of these prohibited activities is the complete strangulation of holding company operations.

Section 5 provides for the registration of holding companies.

Section 6 provides one of the regulatory provisions contained by the Act. This particular regulation is peculiarly important with regard to this opinion because it deals with the issuance of securities. Section 6, (a), provides as follows:

"Sec. 6. (a) Except in accordance with a declaration effective under section 7 and with the order under such section permitting such declaration to become effective, it shall be unlawful for any registered holding company or subsidiary company thereof, by use of the mails or any means or instrumentality of interstate commerce, or otherwise, directly or indirectly

(1) to issue or sell any security of such company; or (2) to exercise any privilege or right to alter the priorities, preferences, voting power, or other rights of the holders of an outstanding security of such company."

Section 7, (a), makes provision for the actions prohibited to a registered holding company under the provisions of Section 6, by setting out the method by which the registered companies and their subsidiaries may gain the approval of the Securities and Exchange Commission, thus, complying with the provisions of the Act, after which they may conduct the activities prohibited in Section 6. This section provides that a declaration shall be filed by a company desiring to issue securities. Subsection (c) of Section 7 provides as follows:

"(c) The Commission shall not permit a declaration regarding the issue or sale of a security to become effective unless it finds that--

"(1) such security is (A) a common stock having a par value and being without preference as to dividends or distribution over, and having at least equal voting rights with, any outstanding security of the declarant; (B) a bond (i) secured by a first lien on physical property of the declarant, or (ii) secured by an obligation of a subsidiary company of the declarant secured by a first lien on physical property of such subsidiary company, or (iii) secured by any other assets of the type and character which the Commission by rules and regulations or order may prescribe as appropriate in the public interest or for the protection of investors; (C) a guaranty of, or assumption of liability on, a security of another company; or (D) a receiver's or trustee's certificate duly authorized by the appropriate court or courts; or

"(2) such security is to be issued or sold solely (A) for the purpose of refunding, extending, exchanging, or discharging an outstanding security of the declarant and/or a predecessor company thereof or for the purpose of effecting a merger, consolidation, or other reorganization; (B) for the purpose of financing the business of the declarant

as a public-utility company; (C) for the purpose of financing the business of the declarant, when the declarant is neither a holding company nor a public-utility company; and/or (D) for necessary and urgent corporate purposes of the declarant where the requirements of the provisions of paragraph (1) would impose an unreasonable financial burden upon the declarant and are not necessary or appropriate in the public interest or for the protection of investors or consumers; or

"(3) such security is one of the issuance of which was authorized by the company prior to January 1, 1935, and which the Commission by rules and regulations or order authorizes as necessary or appropriate in the public interest or for the protection of investors or consumers."

Subsection (g) of Section 7 provides as follows:

"(g) If a State commission or State securities commission, having jurisdiction over any of the acts enumerated in subsection (a) of section 6, shall inform the Commission, upon request by the Commission for an opinion or otherwise, that State laws applicable to the act in question have not been complied with, the Commission shall not permit a declaration regarding the act in question to become effective until and unless the Commission is satisfied that such compliance has been effected."

Subsection (d) of Section 7 provides as follows:

"(d) If the requirements of subsections (c) and (g) are satisfied, the Commission shall permit a declaration regarding the issue or sale of a security to become effective unless the Commission finds that--

"(1) the security is not reasonably adapted to the security structure of the declarant and other companies in the same holding-company system;

"(2) the security is not reasonably adapted to the earning power of the declarant;

"(3) financing by the issue and sale of the particular security is not necessary or appropriate to the economical and efficient operation of a business in which the applicant lawfully is engaged or has an interest;

"(4) the fees, commissions, or other remuneration, to whomsoever paid, directly or indirectly, in connection with the issue, sale, or distribution of the security are not reasonable;

"(5) in the case of a security that is a guaranty of, or assumption of liability on, a security of another company, the circumstances are such as to constitute the making of such guaranty or the assumption of such liability an improper risk for the declarant; or

"(6) the terms and conditions of the issue or sale of the security are detrimental to the public interest or the interest of investors or consumers."

From the above provisions of the Public Utility Holding Company Act of 1935, it will be observed that all holding companies, unless exempt by the Securities and Exchange Commission, are subject to regulation regarding the issuance of their securities and they must subject themselves to this regulation in order to carry on business. It will be noted from Section 6 (a) of the Act that the subsidiary companies of such holding companies are also subject to the regulation as to the issuance of their securities.

The constitutionality of the Public Utility Holding Company Act of 1935, in its entirety, has been challenged in several instances. The courts have refused to pass on its entirety but have restricted their holdings in this regard to the specific sections involved in the particular case. It so happens that Sections 6 and 7, relative to the issuance of securities, have not been specifically involved to date. There is, therefore, no specific holding that these sections are constitutional. However, the cases have made no distinction between any of the sections of the Act with regard to constitutionality, and have upheld the congressional power to remedy the evils which brought about the passage of the Public Utility Holding Company Act of 1935.

In Electric Bond and Share Company, et al., v. Securities and Exchange Commission, et al., 303 U.S. 419 (1938), the Supreme Court

of the United States held constitutional Sections 4 and 5 of the Act, which sections provide for the registration of holding companies and the denial of business operations to unregistered companies. In order to show the contentions which were made by counsel and urged upon the court with regard to the constitutionality questioned, we quote the following from the argument for the petitioners, l. c. 423:

> "These sections do not regulate interstate commerce or the use of the mails. The companies which comprise the electric and gas utility industry are not, as such instrumentalities or agents of interstate commerce, nor is their business, as such, interstate commerce. Some of the companies do engage in particular business or transactions which constitute interstate commerce and which may be regulated, but other companies do no such business. This Act predicates the regulation of all alike merely on the holding company relationship and not upon engagement in any business or activities which constitute or affect interstate commerce.
>
> "Nor are the control sections predicated upon or confined to the regulation of activities constituting or directly affecting interstate commerce or the use of the mails. They relate to the issue and sale of securities (Sections 6-7); to the acquisition of assets or securities (Sections 8-10); to sundry corporate and financial transactions (Section 12); to the reorganization or dissolution of holding company systems (Section 11); and to the performance of service, sales and construction contracts (Section 13). In none of these sections is interstate commerce or the use of the mails a condition of the regulation of a particular transaction, nor need the company whose transactions are so regulated be engaged in interstate commerce or activities directly affecting such commerce."

The court in deciding the case stated the following:

> " * * * The 'electric operations' of subsidiaries in the Bond and Share system are conducted in

> thirty-two States. Some operate only within a single State, some in two or more States, transmitting energy across state lines for their own account, and some sell energy at wholesale in interstate commerce."
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> * * * * * * * * * * * * * * * *
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> "We need not go further in the description of the operations of these Companies, as petitioners concede that the carrying out of these service contracts, as found by the trial court, involves continuous and extensive use of the mails and instrumentalities of interstate commerce, although petitioners are careful to qualify the concession by saying that they agree with the trial court that 'this is not to say that the entire business of Ebasco or American Gas constitutes interstate commerce and is therefore subject to unlimited federal regulations.'"

The petitioners in that case argued that Sections 4 and 5, relating to registration and to submission of documents containing information to the commission were not separable from the other sections of the Act which contained the regulatory provisions of the Act. The Supreme Court refused this contention and ruled that the intent of Congress was that each of the regulatory provisions, as well as Sections 4 and 5, were intended to stand alone, since each of them applied to matters which it was necessary to regulate or to be informed of in order that the evil which Congress was striking at could be remedied. They specifically refused to rule that Sections 4 and 5 could not be separated, and thus upheld those sections as to constitutionality, but refused to rule on the constitutionality of the other sections. This case also sets out the court's reasoning with regard to the congressional purpose for the Act. They ruled that Sections 4, (a), and 5 of the Act were necessary to accomplish the purpose which Congress had intended, and that as such they were constitutional, in the following language:

> "Congress has set forth in the Act what it considers to be the factual situation and the need of federal supervision. The following statement is found in paragraph (a) of Section 1:

"'Public-utility holding companies and their subsidiary companies are affected with a national public interest in that, among other things, (1) their securities are widely marketed and distributed by means of the mails and instrumentalities of interstate commerce and are sold to a large number of investors in different States; (2) their service, sales, construction, and other contracts and arrangements are often made and performed by means of the mails and instrumentalities of interstate commerce; (3) their subsidiary public-utility companies often sell and transport gas and electric energy by the use of means and instrumentalities of interstate commerce; (4) their practices in respect of and control over subsidiary companies often materially affect the interstate commerce in which those companies engage; (5) their activities extending over many States are not susceptible of effective control by any State and make difficult, if not impossible, effective State regulation of public-utility companies.'

"Congress has further declared in paragraph (b) of that section, upon the basis of facts disclosed by the reports of the Federal Trade Commission and of the Committee on Interstate and Foreign Commerce of the House of Representatives, and otherwise ascertained, the circumstances in which the national interest and the interest of investors and consumers may be adversely affected by the operation of public utility holding companies. And after this catalogue of the abuses which may exist in the circumstances described, Congress declares it to be its policy 'to meet the problems and eliminate the evils as enumerated in this section, connected with public-utility holding companies which are engaged in interstate commerce or in activities which directly affect or burden interstate commerce.' Without attempting to state the limits of permissible regulation in the execution of this declared policy, we have no reason to doubt that

> from these defendants, with their highly important relation to interstate commerce and the national economy, Congress was entitled to demand the fullest information as to organization, financial structure and all the activities which could have any bearing upon the exercise of congressional authority. The regulation found in Section 5 (b) goes no further than to require this information and we are of the opinion that its validity must be sustained.
>
> "Section 4 (a) prescribes the penalty for failure to register under Section 5, and that section as an incident to registration imposes the duty to file the described registration statement. Treating the requirements of Sections 4 (a) and 5 as a separable part of the Act, the question is whether that penalty may be validly imposed."
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> * * * * * * * * * * * * * * * *
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> " * * * We think that the imposition of such a penalty does not transgress any constitutional provision."

In 1946 the Supreme Court of the United States in North American Company v. Securities and Exchange Commission, 327 U.S. 686 (1946), had before it the question of the constitutionality of Section 11 (b), (1), of the Act authorizing the Securities and Exchange Commission to act to bring about the geographic integration of holding company systems. In this case, as in the Electric Bond & Share Company case, the Electric Bond & Share Company system was involved. The latter company was the pinnacle of the great pyramid of corporations which were primarily engaged in operating gas and utility company properties. Electric Bond & Share controlled several companies which were holding companies in themselves. The latter, in turn, controlled operating subsidiary companies and, again, some of these companies were wholly intrastate companies and others actually did an interstate business. The Securities and Exchange Commission ordered the dissolution of the North American Company, which was a holding company underneath Electric Bond & Share Company, on the ground that North American served no useful purpose. This was done under Section 11 (b) (1) of the Act, and thus was raised the question regarding this section. The Supreme Court went thoroughly into the question of constitutionality. They said the operations of North American were interstate in character, and, as such, it was not unconstitutional for Congress to regulate the operations thereof with the view toward eradicating evils which grow out of such operations. The court said in this regard:

> "The interstate character of North American and its subsidiaries is readily apparent from the

Commission's survey of their activities. North American is more than a mere investor in its subsidiaries. See Northern Securities Co. v. United States, 193 U.S. 197, 353-354. It is the nucleus of a far-flung empire of corporations extending from New York to California and covering seventeen states and the District of Columbia. Its influence and domination permeate the entire system and frequently evidence themselves in affirmative ways. The mails and the instrumentalities of interstate commerce are vital to the functioning of this system. They have more than a casual or incidental relationship. Cf. Ware & Leland v. Mobile County, 209 U.S. 405; Blumenstock Bros. v. Curtis Pub. Co., 252 U.S. 436; Federal Baseball Club v. National League, 259 U.S. 200. Without them, North American would be unable to float the various security issues of its own or of its subsidiaries, thereby selling securities to residents of every state in the nation. Without them, North American would be unable to exercise and maintain the influence arising from its large stock holdings, receiving notices and reports, sending proxies to stockholders' meetings, collecting dividends and interest, and transmitting whatever instructions and advice may be necessary. Nor could North American maintain its other relationships and contacts with its own subsidiaries without the use of the mails and facilities of interstate commerce. Such interstate commercial transactions involve the very essence of North American's business. See International Textbook Co. v. Pigg, 217 U.S. 91. They enable it 'to promote the sound development' of its investments from its headquarters in New York City. In short, they are commerce which concerns more states than one. Gibbons v. Ogden, 9 Wheat. 1, 194; Second Employers' Liability Cases, 223 U.S. 1, 46; Minnesota Rate Cases, 230 U.S. 352, 398. As stated by this Court in Associated Press v. Labor Board, 301 U.S. 103, 128, 'Interstate communication of a business nature, whatever the means of such communication is interstate commerce regulable by Congress under the Constitution.'

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"These requirements of Section 11 (b) (1) apply only to registered holding companies. A holding company, by statutory definition, is a company that controls or possesses a controlling influence over an electric or gas utility company. Section 2 (a) (7). A holding of 10% or more of the outstanding voting securities of such a utility company is presumed to be sufficient to constitute such a relationship, but this presumption may be rebutted by proof before the Commission of a lack of control or controlling influence. Accordingly, a company that is a mere investor in utility securities and that does not control or possess a controlling influence over the utility companies need not comply with Section 11 (b) (1).

"A holding company as so defined must register and hence must obey the commands of Section 11 (b) (1) if it uses the mails or the instrumentalities of interstate commerce directly or through its subsidiaries in the operation of its business. * * *

"By making these enumerated interstate transactions unlawful unless the holding company registers with the Commission and by extending Section 11 (b) (1) to registered holding companies, Congress has effectively applied Section 11 (b) (1) to those holding companies that are in fact in the stream of interstate activity and that affect commerce in more states than one. Congress has further declared in Section 1 (c) that all the provisions of the Act, thus including Section 11 (b) (1), shall be interpreted to meet the problems and remove the evils connected with public utility holding companies 'which are engaged in interstate commerce or in activities which directly affect or burden interstate commerce . . .' Section 11 (b) (1) is thus clearly and unmistakably applicable to holding companies engaged in interstate commerce.

"Not all holding companies that are engaged in interstate activities, however, must necessarily

comply with Section 11 (b) (1). By the terms of Section 3 (a) (1), if a holding company and all of its subsidiaries are predominantly intrastate in character and carry on their business substantially in a single state in which such holding company and every subsidiary thereof are organized, the Commission may grant an exemption from any provision of the Act 'unless and except insofar as it finds the exemption detrimental to the public interest or the interest of investors or consumers . . .'

" * * * This problem, however, is academic so far as North American is concerned. Like most public utility holding companies, North American is engaged in interstate commerce directly and through its subsidiaries. It can lay no claim to a predominantly intrastate character; as to it, Section 3 (a) (1) is wholly inapplicable. * * *

"The crucial constitutional issue, so far as the commerce clause is concerned, resolves itself into the query whether Congress may validly require holding companies engaged in interstate commerce to dispose of their security holdings and to confine their activities in accordance with the standards of Section 11 (b) (1). In urging the negative answer to this query, North American relies upon the settled doctrine that the federal commerce power extends to intrastate activities only where those activities 'so affect interstate commerce, or the exertion of the power of Congress over it, as to make regulation of them appropriate means to the attainment of a legitimate end, the effective execution of the granted power to regulate interstate commerce.' United States v. Wrightwood Dairy Co., 315 U.S. 110, 119. See also Santa Cruz Fruit Packing Co., v. Labor Board, 303 U.S. 453, 466; United States v. Darby, 312 U.S. 100, 118-123; Wickard v. Filburn, 317 U.S. 111, 122-124. It is said that the ownership by North American of securities of other system companies is not in itself commerce, interstate or intrastate, and that the right to own or retain property

is characteristically governed by state laws, the Federal Government having no concern with such matters except as an incident to the due exercise of one of its granted powers. North American denies that the necessary relationship between the ownership of securities and interstate commerce is self-evident or that it has been found as a fact by Congress, the Commission or any court. The absence of this relationship, it is concluded, causes Section 11 (b) (1) to fall.

"This argument, however, misconceives not only the power of Congress over interstate commerce but also the basic nature of public utility holding companies and the effect that stock ownership has upon their activities. The dominant characteristic of a holding company is the ownership of securities by which it is possible to control or substantially to influence the policies and management of one or more operating companies in a particular field of enterprise. To be sure, other devices may be utilized to effectuate control, such as voting trusts, interlocking directors and officers, the control of proxies, management contracts and the like. But the concentrated ownership of voting securities is the prime method of achieving control, constituting a more fundamental part of holding companies than of other types of business. Public utility holding companies are thereby able to build their gas and electric utility systems, often gerrymandered in such ways as to bear no relation to economy of operation or to effective regulation. The control arising from this ownership of securities also allows such holding companies to exact unreasonable fees, commissions and other charges from their subsidiaries, to make undue profits from the handling of the issue, sale and exchange of securities for their subsidiaries, to issue unsound securities of their own based upon the inflated value of the subsidiaries, and to affect adversely the accounting practices and the rate and dividend policies of the subsidiaries. See Section 1 (b). Congress

has found that all of these various abuses and evils occur and are spread and perpetuated through the mails and the channels of interstate commerce. And Congress has further found that such interstate activities, which grow out of the ownership of securities of operating companies, have caused public utility holding companies to be 'affected with a national public interest.' Section 1 (a).

* * * * * * * * * * * * * * * * *

"The constitutionality of Section 11 (b) (1) under the commerce clause thus becomes apparent. For nearly one hundred and twenty-five years, this Court has recognized that the power of Congress over interstate commerce is 'the power to regulate; that is, to prescribe the rule by which commerce is to be governed. This power, like all others vested in Congress, is complete in itself, may be exercised to its utmost extent, and acknowledges no limitations, other than are prescribed in the constitution.' Gibbons v. Ogden, supra, 196. This is not to say, of course, that Congress is an absolute sovereign. It is limited by express provisions in other parts of the Constitution, such as Section 9 of Article 1 and the Bill of Rights. But so far as the commerce clause alone is concerned Congress has plenary power, a power which 'extends to every part of interstate commerce, and to every instrumentality or agency by which it is carried on; and the full control by Congress of the subjects committed to its regulation is not to be denied or thwarted by the commingling of interstate and intrastate operations.' Minnesota Rate Cases, supra, 399."

On the same reasoning and principles as set out in the above case, the Supreme Court of the United States in American Power and Light Company v. Securities and Exchange Commission, 329 U.S. 90 (1946), upheld the constitutionality of Section 11 (b) (2). The court in that case said at l.c. 97:

"Like Section 11 (b) (1), its statutory companion, Section 11 (b) (2) applies only to registered holding companies and their subsidiaries. * * *"

(Underscoring ours.)

In discussing the interstate character which brought the company under the regulation of the holding company Act the court said:

> "The Bond and Share system, including American and Electric, possesses an undeniable interstate character which makes it properly subject, from the statutory standpoint, to the provisions of Section 11 (b) (2). This vast system embraces utility properties in no fewer than 32 states, from New Jersey to Oregon and from Minnesota to Florida, as well as in 12 foreign countries. Bond and Share dominates and controls this system from its headquarters in New York City. As was the situation in the North American case, the proper control and functioning of such an extensive multi-state network of corporations necessitates continuous and substantial use of the mails and the instrumentalities of interstate commerce. Only in that way can Bond and Share, or its subholding companies or service subsidiary, market and distribute securities, control and influence the various operating companies, negotiate inter-system loans, acquire or exchange property, perform service contracts, or reap the benefits of stock ownership. See Section 1 (a). See also International Textbook Co. v. Pigg, 217 U.S. 91. Moreover, many of the operating companies on the lower echelon sell and transmit electric energy or gas in interstate commerce to an extent that cannot be described as spasmodic or insignificant. Electric Bond & Share Co. v. S.E.C., supra, 432-33. Such activities serve to augment the interstate nature of the Bond and Share system. And they make even plainer the fact that this system falls within the intended scope of Section 11 (b) (2)."

Other cases have upheld the constitutionality of Sections of the Act. Section 11 has been upheld by the Federal Circuit Courts (United Gas and Improvement Company v. Securities and Exchange Commission, 138 Fed. (2d) 1010 (1943); American Power and Light Company v. Securities and Exchange Commission, 141 Fed. (2d) 606 (1944); North American Company v. the Securities and Exchange Commission, 133 Fed. (2d) 148 (1943)). Section 12 (h) has been upheld (Egan v. the United States, 137 Fed. (2d) 369 (1943)).

With regard to subsidiary companies, the courts have held that when a subsidiary company is a member of a holding company system, that is, is a subsidiary under the terms of the Act to a holding company, the subsidiary company is subject to regulation under the Act when the parent holding company is a registered holding company under the Act. The Eighth Circuit Court of Appeals held in Panhandle Eastern Pipeline Company v. Securities and Exchange Commission, 170 Fed. (2d) 453 (1948), that intrastate subsidiaries were subject to regulations under the Act when the holding company was a registered holding company, but no constitutional question was raised. In Detroit Edison Company v. Securities and Exchange Commission, 119 Fed. (2d) 730 (1941), the Sixth Circuit Court of Appeals held a subsidiary which did only intrastate business was subject to regulation under Sections 24 (a) and 2 (a) (8) of the Act, even though it was contended in that case that Congress lacked the power to regulate it because the activities were purely intrastate. The court did not pass on the constitutionality but said that the registration of the parent holding company was prima facie evidence that the subsidiary was subject to the provisions of the Act. The same holding was made in Hartford Gas Company v. Securities and Exchange Commission, 192 Fed. (2d) 794 (1942). Here again the petitioner was a subsidiary company operating wholly within one state.

Sections 6 and 7, the sections with which we are primarily interested in this opinion, were involved in the holding in Okin v. Securities and Exchange Commission, 154 Fed. (2d) 27 (1946). The petitioner in that case sought a review of orders of the Securities and Exchange Commission which affected the issuance of securities by American and Foreign Power Company, a Maine corporation and subsidiary of Electric Bond and Share Company, the former not operating directly or indirectly any public utility within the United States and deriving its income from utility operations of subsidiary companies operating solely in foreign companies. The court in that case said:

> "(1) Foreign Power is a Maine corporation, many of whose securities are held by American investors. It is a subsidiary of Bond and Share, which has registered as a holding company under the Act. Foreign Power does not operate directly or indirectly any public utility within the United States, and its income from utility operations is derived solely from subsidiary companies operating in foreign countries. Because of these facts the

petitioner argues that the Public Utility Holding Company Act of 1935 does not give the Commission jurisdiction to regulate any of Foreign Power's affairs. We cannot agree with this contention. Foreign Power is within the literal definitions of 'holding company' and 'subsidiary company,' set forth in sections 2(a) (7) and 2(a) (8), 15 U.S.C.A. Section 79b(a) (7,8) respectively, neither of which contains any geographical limitation. Under section 3(a) (5), 15 U.S.C.A. Section 79c (a) (5), the Commission is directed to exempt by rule or order a holding company from any provision or provisions of the Act 'unless and except insofar as it finds the exemption detrimental to the public interest or the interest of investors * * * if-- * * * (5) such holding company is not, and derives no material part of its income, directly or indirectly, from any one or more subsidiary companies which are, a company or companies the principal business of which within the United States is that of a public-utility company.' A similar provision for the exemption of a subsidiary company of a holding company is found in section 3(b). The discretion which sections 3(a) (5) and 3(b) confer upon the Commission to consider the public interest and the interest of investors in determining the extent of the exemption to be granted to a company such as Foreign Power would be meaningless, if the definitions of 'holding company' and 'subsidiary' were to be so limited as ipso facto to make the Act inapplicable to such a company. Consequently, in our opinion, the Commission had power to rule, as it did in 6 S. E. C. 396, that Foreign Power was entitled to only partial exemption from regulation under the Act. We do not understand the petitioner to argue, nor could he successfully do so, that the partial exemption granted Foreign Power was broad enough to exempt it from the provisions upon which the Commission relied in making the orders now under review.

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"(3) In support of its power to make the orders under review the Commission refers to numerous sections of the Act, and particularly to 6(a), 7(d)

and (f), and 12 (c) and (f) 15 U.S.C.A. Sections 79f(a), 79g(d,f), 79l(c,f). Section 6(a) provides that, except in accordance with a declaration effective under section 7, no 'registered holding company or subsidiary company thereof' shall 'issue or sell any security of such company.' The notes which Foreign Power proposed to issue in renewal of its debt to its parent were a 'security' within the definition of section 2(a) (16). Under section 7(d) the Commission had to consider whether 'the terms and conditions' of the proposed issue were 'detrimental to the public interest or the interest of investors'; and under section 7(f) its order permitting the proposal to become effective could contain 'such terms and conditions as the Commission finds necessary to assure compliance with the conditions specified in this section.' Section 12(c) declares it unlawful for a subsidiary company of a registered holding company to 'retire, or redeem any security of such company, in contravention of such rules and regulations or orders as the Commission deems necessary or appropriate to protect the financial integrity of companies in holding-company systems.' Also apparently applicable are the provisions of section 12(f) which make it 'unlawful for any registered holding company or subsidiary company thereof' to enter into or perform 'any transaction not otherwise unlawful under this title, with any company in the same holding-company system * * * in contravention of such rules and regulations or orders * * * as the Commission deems necessary or appropriate in the public interest or for the protection of investors * * * or to prevent the circumvention of the provisions of this title or the rules and regulations thereunder.' The foregoing sections are broad enough in terms to empower the Commission in its order approving issuance of the renewal notes to impose conditions designed to preserve the status quo pending a later determination of the rank and status of the debt claim of Bond and Share against its subsidiary; and the purpose of the Act supports the same construction. * * *"

It thus appears that in the above case the Federal Circuit Court assumed the constitutionality of Sections 6 and 7.

From the above authorities, we are of the opinion that holding companies, not exempt by the Securities and Exchange Commission, are required to register with the commission under and according to the provisions of the Public Utility Holding Company Act of 1935, that they must do so whether their subsidiary companies are doing intrastate or interstate business and operations, that a holding company registered or required to be registered under the terms of the Act is subject to the regulation under the Act, that a subsidiary of such holding company is also subject to regulation under the provisions of the Act, and that this regulation extends to the issuance of securities to the holding companies and their subsidiaries, since the same reasons for upholding the regulations and provisions of the Act in the case of other sections of that Act apply with equal force to Sections 6 (a) and 7, which deal with the issuance of securities by holding companies and their subsidiaries.

Only one case would seem to be in variance with the conclusions stated immediately above. This is North American Company v. Securities and Exchange Commission, 81 Fed. (2d) 461 (1936), in which the Federal Circuit Court held that a holding company which was in bankruptcy did not have to register under the Public Utility Holding Company Act of 1935, before going forward with a reorganization plan, because all of its subsidiaries were entirely intrastate in character. This was an early case and we think that the decisions of the United States Supreme Court following that case, as well as the other federal decisions, have overruled it. We believe this conclusion is inescapable because it seems obvious that the same evils at which Congress was striking when it passed the Public Utility Holding Company Act of 1935 would be in evidence with relation to a holding company which held subsidiaries which were all intrastate companies as well as to a holding company which held subsidiaries doing interstate business. The courts held that Congress had the right to eradicate the evils against which the 1935 Act was directed. The evils are the manipulation of the subsidiaries by the holding company and the only way to remedy these evils is to regulate the holding companies and the subsidiaries, and this is true whether the subsidiary is intrastate, interstate, or a combination of both, with regard to its operations. We think this conclusion is further substantiated by the fact that the Supreme Court of the United States in the cases which we have quoted above, upheld the constitutionality of provisions of the Act on the reasoning which we have set out in the above sentences of this paragraph (and quoted from the cases) in the face of the facts in some of the cases showing that some of the subsidiaries of the holding companies involved were intrastate in character. It would appear that, if the Supreme Court of the United States was not completely opposed to the theory set

out in this Federal case, it not only would not have ruled on the basis of the reasoning which it used, but it would have been compelled to distinguish between the subsidiaries of these holding companies involved, and to say that, where the subsidiary was intrastate in character, the provisions of the Holding Company Act of 1935 did not apply to it. The Supreme Court, however, did not make such a distinction.

In our opinion, therefore, a Public Utility Holding Company and its subsidiaries, of the type described in your letters relating to the request for this opinion, would be required to register under the Public Utility Holding Company Act of 1935, and that the holding company and its subsidiaries would be subject to the regulations under the Act, including the approval of the issuance of its securities.

One more question remains, however. This is whether or not, assuming that the company here in question is subject to regulation under the Public Utility Holding Company Act of 1935, the regulation therein contained is that which is contemplated by the Missouri Statutes regarding the regulation of securities and their sale in Missouri. This is important, because, if this were not true, we do not think such congressional regulation would bring the company within the meaning of the exemption clause in the Missouri Statutes which you set out in your letter. However, the above quoted provisions of the Public Utility Holding Company Act of 1935 and the quotations from the Federal cases, show that the purpose in the Federal regulation of the issuance of securities is to protect the investor in such securities. While the question of the prevention of monopoly is the primary consideration of the Act of 1935, it is necessary for the issuance of securities to be regulated in order that monopoly be restricted and the reason that monopoly is to be restricted and regulated is for the protection of the investor in securities.

We quote from Section 8264, R. S. Missouri 1939:

> "If upon examination of any application the commissioner shall find that the sale of security referred to therein would not be fraudulent or would not work or tend to work a fraud upon the purchaser, or that the enterprise or business of the issuer is not based upon unsound business principles, then upon the payment of the fee provided in this section, he shall record the registration of such security in the register of securities, and thereupon such

security so registered may be sold by the issuer or by any registered dealer who has notified the commissioner of his intentions so to do, in the manner hereinafter provided in section 8279, subject, however, to the further order of the commissioner as hereinafter provided."

As will be seen from the above quoted paragraph, the protection of the investor in securities is the purpose for the regulation of the sale of securities in Missouri under the Missouri Statutes. It seems clear, therefore, that the purpose of the regulation by the Missouri Statutes and the purpose for the regulation under the Public Utility Holding Company Act of 1935 is the same. We are of the opinion, therefore, that if a public utility gas and electric holding company and its subsidiaries are subject to the regulation under the Public Utility Holding Company Act of 1935, the protection of the investor is provided for as if the company was registered under the Missouri Statutes and subject to the regulations of those statutes.

In expressing the opinions above, we make these reservations. Our conclusions above would not necessarily be true where the securities involved are not of a type which may be regulated under the provisions of the Public Utility Holding Company Act of 1935. We do not quote those provisions here, but refer the department to the Act in this regard. The opinions which we express here also do not apply where the Securities and Exchange Commission has, under the provisions of the Act of 1935, exempted any gas and electric public utility company from the provisions of the Act of 1935. We are also assuming in this opinion that the statements in the prospectus of the Texas Electric Service Company, to the effect that that company is a subsidiary of a holding company registered under the Public Utility Holding Company Act of 1935, is correct.

CONCLUSION.

It is, therefore, the opinion of this department subject to the reservations contained in this opinion, that the securities of the Texas Electric Service Company, a subsidiary of a Public Utility Holding Company registered under the Public Utility Holding Company Act of 1935, are exempt securities from the provisions of the Missouri Security Law, in accordance with the terms of Section 8260 (d), R. S. Missouri 1939.

Respectfully submitted,

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APPROVED:

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